



PETER VAN DEN BOSSCHE

# The **Law and Policy** of the **World Trade Organization**

Text, Cases and Materials

SECOND EDITION

CAMBRIDGE

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## The Law and Policy of the World Trade Organization

As the leading student text in the field, this title provides both a detailed examination of the law of the World Trade Organization and a clear introduction to the basic principles and underlying logic of the world trading system. It explores the institutional aspects of the WTO together with the substantive law. New to this edition are examinations of the WTO rules on the protection of intellectual property rights and the rules on technical barriers to trade and sanitary and phytosanitary measures. Assignments are integrated throughout to allow students to assess their understanding, while chapter summaries reinforce learning. In addition, exercises have been included to draw on primary sources and real-life trade scenarios, enabling students to hone their practical and analytical skills. The title is an essential tool for any student of the WTO, either at undergraduate or at postgraduate level. Practising lawyers and policy-makers who are looking for an introduction to WTO law will also find this title invaluable.

PETER VAN DEN BOSSCHE is Professor of International Economic Law, Head of the Department of International and European Law and Academic Director of the Institute for Globalisation and International Regulation at Maastricht University, the Netherlands. He studied law at the University of Antwerp (Lic. jur.), the University of Michigan (LLM) and the European University Institute, Florence (Dr jur.). From 1997 to 2001, Peter Van den Bossche was Counsellor to the Appellate Body of the WTO, Geneva. In 2001 he served as Acting Director of the Appellate Body Secretariat.



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Second Edition

Peter Van den Bossche

*Maastricht University*



CAMBRIDGE  
UNIVERSITY PRESS

CAMBRIDGE UNIVERSITY PRESS  
Cambridge, New York, Melbourne, Madrid, Cape Town, Singapore,  
São Paulo, Delhi, Dubai, Tokyo

Cambridge University Press  
The Edinburgh Building, Cambridge CB2 8RU, UK

Published in the United States of America by Cambridge University Press, New York

[www.cambridge.org](http://www.cambridge.org)

Information on this title: [www.cambridge.org/9780521898904](http://www.cambridge.org/9780521898904)

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First published in print format 2008

ISBN-13 978-0-511-66910-1 eBook (Adobe Reader)

ISBN-13 978-0-521-89890-4 Hardback

ISBN-13 978-0-521-72759-4 Paperback

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# Preface to the first edition

Since the entry into force of the *WTO Agreement* in January 1995, international trade law has developed from a technical backwater of international law to one of its most vibrant fields. Before 1995, international trade law was taught at few universities and was only of interest to a relatively small group of legal practitioners. Over the past decade, however, interest in this field of international law has increased dramatically. Students, academics, legal practitioners, advisers of businesses and NGOs, and officials of national governments and international organisations have woken up to its importance. Now, most universities give much attention to trade law in international law courses or offer specialised courses on WTO law.

Concrete plans for this book were first made on the eve of my departure from the WTO and return to academia at the end of 2001. For five years, I had the privilege to serve, during the seminal early days of the WTO and its law, as a senior legal advisor to the Appellate Body of the WTO.

This book is primarily a textbook for graduate and senior undergraduate students of law. However, it was also written with practising lawyers and policy-makers, looking for an introduction to WTO law, in mind. The book covers both the institutional and the substantive law of the WTO. Chapter 1 is an introduction on whether economic globalisation and international trade are a bane or a blessing, on the need for WTO law, and on the main principles and sources of this law. Chapter 2 discusses the WTO as the prime intergovernmental organisation for international trade, and deals with its origins, objectives, functions, membership, institutional structure and decision-making procedures. Chapter 3 concerns the WTO's all-important and unique dispute settlement system and explores the origins, principles, institutions and proceedings of WTO dispute settlement. Chapter 4 discusses the fundamental WTO principles of non-discrimination, the most-favoured-nation treatment obligation and the national treatment obligation as they apply to trade in goods and trade in services. Chapter 5 deals with market access for goods, services and service suppliers and discusses, *inter alia*, the WTO rules on tariff and non-tariff barriers to trade in goods and barriers to trade in services. Chapter 6 concerns the WTO rules on unfair trade and, in particular, the rules on dumping and subsidised trade. Chapter 7 deals with the inevitable conflict between trade liberalisation and other societal values and interests. It discusses the many situations in which WTO law allows Members to deviate from the basic rules and let other societal values and interests prevail over trade liberalisation. The concluding chapter 8

briefly sets out two major challenges for the future of the WTO, namely, the integration of developing countries in the multilateral trading system and the further expansion of the scope of WTO law. While the treatment of the law is often quite detailed, the prime aim of this textbook is to make clear the basic principles and underlying logic of WTO law and the world trading system.

Special attention was given to the focus, approach and structure of this book. Each section contains questions and assignments, to allow students to assess their understanding and to develop useful practical skills. At the end of each chapter, there is a helpful summary as well as an exercise on specific true-to-life international trade problems encountered by the Kingdom of Richland, a developed-country Member, and the Republic of Newland, a developing-country Member. These exercises are ideally intended to be dealt with in tutorials, but are equally suitable for individual study. While challenging, these exercises can be done on the basis of the knowledge acquired in the chapter they conclude. It was a deliberate choice to refer sparingly to the vast academic literature on many of the topics addressed in this book. The focus is clearly on the provisions of the WTO agreements themselves, the case law of panels and the Appellate Body and official policy documents. For advanced courses on WTO law, this book can be usefully supplemented by academic articles from the *Journal of International Economic Law*, the *Journal of World Trade*, the *World Trade Review* and other specialised or general law journals. The reader can find suggestions on recent academic articles and case law, organised according to the chapters of this book, at [www.egeg.org](http://www.egeg.org).

In writing this book I owe much to many. I am particularly indebted to Gabrielle Marceau and Denise Prévost who supported and encouraged me from the beginning and commented on all chapters. I am similarly indebted to Edwin Vermulst and Folkert Graafsma who also read through the whole manuscript and made many useful comments, and to Julie Soloway, who made a very important contribution to the section on dumping and anti-dumping measures. I am grateful to Marco Bronckers, Stephanie Cartier, Bill Davey, Piet Eeckhout, Barbara Eggers, Lothar Ehring, Mary Footer, Susan Hainsworth, Valerie Hughes, Pieter-Jan Kuijper, Bernard Kuiten, Hoe Lim, Jim Mathis, Marielle Matthee, Elisabetta Montaguti, Joost Pauwelyn, Roberto Rios Herrera, Jochem Wiers, Jan Wouters and Werner Zdouc, who all read, and commented on, specific chapters, or contributed otherwise to this book. I would like to pay tribute to John Jackson, my first mentor and guide in the land of international trade. I would also like to acknowledge my profound and lasting debt towards the Members of the original Appellate Body, and, in particular, James Bacchus, Claus-Dieter Ehlermann, Florentino Feliciano and Julio Lacarte, whom I had the privilege to serve for five years and from whom I learned so much. I address a special word of thanks to Debra Steger, the first director of the Appellate Body Secretariat and 'sister-in-arms' during the fascinating but very demanding first years of the Appellate Body. I am grateful to Finola O'Sullivan, publisher at Cambridge University Press, and her staff, Jane O'Regan, Mary Leighton, Martin Gleeson, Eva Huehne and Jennie Rubio, for their confidence and excellent support. I am equally grateful to the Faculty of Law of Maastricht University, for facilitating the work on



this book. My special thanks to Paul Adriaans, Sophie Janssen and Roger Snijder. Finally, this book would never have been finished without the untiring help and capable assistance of, in particular, Adeshola Odusanya, Katalin Fritz and Carol Ní Ghiollarnáth, my research assistants, and also Iveta Alexovičová, Natalya Bayurova, Kasper Hermans, Stelios Katevatis, Sergey Ripinsky, Eva Schöfer, Nikolaos Skoutaris, Damian Smith and Ruta Zarnauskaite, all graduate or undergraduate students at Maastricht University in the period 2002–4. Of course, none of those mentioned above bears any responsibility for any error or omission in this book. In recognition of the support I received from so many colleagues and students in the writing of this book, all royalties go to Maastricht University to set up a scholarship and research fund for students and scholars from developing countries.

Peter Van den Bossche  
Maastricht, September 2004



# Preface to the second edition

In the three years that have passed since I completed work on the first edition of this book, the interest in the world trading system has continued to grow. Ever more universities offer courses on international economic law in general and WTO law in particular. While unsubstantiated and misinformed criticism of the WTO is still the rave and *bon ton* in many circles, the WTO seems to be doing a better job at selling itself and slowly enlarging its base of support. This is all the more amazing since opposition to economic globalisation is not weakening and the Doha Development Round has thus far mainly produced disappointment. Perhaps there is a growing realisation, or in some circles reluctant acceptance, that the WTO and its law – while obviously wanting in many respects – make an effective contribution to managing economic globalisation and international trade. The WTO, and in particular its dispute settlement system applying and interpreting WTO law, have done a good job in balancing trade liberalisation with other societal values and interests, such as the protection of public health, the environment and economic development of developing countries. However, undoubtedly, the road is still long and the journey hazardous.

Braced by encouragement and inspired by comments of readers from Lesotho to India, many of them students but also many government officials and legal practitioners, I started in early 2007 on the second edition of *The Law and Policy of the World Trade Organization*. This second edition not only updates and revises the 2005 edition, it also considerably expands the text by including a new chapter, entitled ‘Towards harmonisation of national regulation’, discussing in some detail the rules of the *TRIPS Agreement* on the protection of intellectual property rights, the *TBT Agreement* on technical barriers to trade, and the *SPS Agreement* on sanitary and phytosanitary measures.

The writing of this second edition has been a much larger task than I had initially envisaged. Fortunately, as with the first edition, I had much help. To many of those I thanked in the Preface of the first edition, I owe once again my thanks for their support and advice. I appreciate the continued support of Gabrielle Marceau. Chapter 6 has greatly benefited from the comments of Edwin Vermulst and Katalin Fritz. The section on the *TRIPS Agreement* of chapter 8 owes much to the comments of Anselm Kamperman Sanders. I am particularly indebted to Denise Prévost, my senior research associate at Maastricht University. Without her commitment, knowledge of WTO law and eye for detail this second edition would not have been. She is the principal author of large parts of the new chapter 8. I am also indebted to Marieke van Overveld, a former Maastricht student and

graduate of the World Trade Institute, who diligently and with great stamina selected and prepared materials for the second edition. My heartfelt thanks go Iveta Alexovičová, Nina Buttgen, Anke Dahrendorf, Ana Maria Daza Vargas, Lennard Duijvestijn, Vydyanathan Lakshmanan, Elissavet Malathouni, Angeliki Mavridou, Bas Megens, Lorin van Nuland, Gustavo Ferreira Ribeiro, Mark Seitter and Wen Shuying, my researchers and research assistants, at Maastricht University and elsewhere, whose untiring help and capable assistance made work on this second edition definitely lighter. Of course, none of those mentioned above bear any responsibility for any error or omission in this book. I am grateful to Finola O'Sullivan, Editorial Director, Law, at Cambridge University Press and her staff, in particular Sinéad Moloney, Richard Woodham and Diane Illott, for their continued confidence and unfailing support. I am equally grateful to the Faculty of Law of Maastricht University for facilitating the work on the second edition of this book. My special thanks go to Marijn Blok, my secretary at the Maastricht Faculty of Law. With the royalties from the first edition of this book, the Maastricht University Fund for Education and Research in International Economic Law (MUFERIEL) was established. This Fund, which is now managed by the Institute for Globalisation and International Regulation at Maastricht University ([www.igir.org](http://www.igir.org)), has been used to give financial assistance to students and scholars from developing countries. I intend to use the royalties of the second edition for the same purpose. Finally, I would like to dedicate this second edition to Patricia Murillo Montesdeoca, my wife, for her patience and unwavering support.

Peter Van den Bossche  
Maastricht, December 2007

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# 1

# Economic globalisation and the law of the WTO

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## 1.1. INTRODUCTION

At the largest-ever gathering of Heads of State and Government, the Millennium Summit of the United Nations in September 2000, the UN General Assembly solemnly declared:

We will spare no effort to free our fellow men, women, and children from the abject and dehumanizing conditions of extreme poverty, to which more than a billion of them are

currently subjected. We are committed to making the right to development a reality for everyone and to freeing the entire human race from want.<sup>1</sup>

It was decided to *halve* the proportion of the world's people living in extreme poverty by the year 2015.<sup>2</sup> While data of the World Bank show that the number of people living in extreme poverty<sup>3</sup> is declining, the enormity of the task ahead is obvious to all. According to the latest data available, 985 million people still live in extreme poverty.<sup>4</sup> Moreover, the income gap between the richest 20 per cent of the world's population and the poorest 20 per cent does not cease to grow. During the 1990s, this gap increased from 60:1 to 86:1.<sup>5</sup> In discussing the greatest challenges that the world faces, Jimmy Carter, the former US President, stated in his Nobel Peace Prize Lecture in December 2002:

Among all the possible choices, I decided that the most serious and universal problem is the growing chasm between the richest and poorest people on earth. The results of this disparity are root causes of most of the world's unresolved problems, including starvation, illiteracy, environmental degradation, violent conflict, and unnecessary illnesses that range from guinea worm to HIV/Aids.<sup>6</sup>

Another Nobel Peace Prize winner, Muhammad Yunus, founder of the Grameen Bank for the Poor, stated in his Nobel Lecture in December 2006:

World's income distribution gives a very telling story. Ninety-four percent of the world income goes to 40 percent of the population while sixty percent of people live on only 6 percent of world income. Half of the world population lives on two dollars a day. Over one billion people live on less than a dollar a day. This is no formula for peace . . . Poverty is the absence of all human rights. The frustrations, hostility and anger generated by abject poverty cannot sustain peace in any society. For building stable peace we must find ways to provide opportunities for people to live decent lives.<sup>7</sup>

One of the defining features of today's world is the process of economic globalisation, a process characterised by high levels of international trade and foreign direct investment. This chapter examines this process and notes the broad consensus among economists and policy-makers that economic globalisation in general, and international trade and foreign direct investment in particular, offers an unprecedented *opportunity* to significantly reduce poverty worldwide.<sup>8</sup>

<sup>1</sup> United Nations General Assembly, *UN Millennium Declaration*, Resolution adopted on 8 September 2000, para. 11. <sup>2</sup> *Ibid.*, para. 19. <sup>3</sup> Extreme poverty is defined as living on less than \$1 a day.

<sup>4</sup> Note that the number of people living in extreme poverty in developing countries fell by 260 million in the period 1990–2004. This is in large part due to massive poverty reduction in China. See World Bank, *World Development Indicators 2007*, [www.worldbank.org/data/wdi2007/index.htm](http://www.worldbank.org/data/wdi2007/index.htm), visited on 30 October 2007. In contrast, the number of people in absolute poverty continued to increase in Sub-Saharan Africa, rising by almost 60 million.

<sup>5</sup> Note that the income gap between the richest 20 per cent of the world's population and the poorest 20 per cent stood at around 3:1 in 1820, 11:1 in 1913 and 30:1 in 1970. See <http://hdr.undp.org/reports/global/1999/en>, visited on 1 January 2004.

<sup>6</sup> President Jimmy Carter, Nobel Lecture, Oslo, 10 December 2002, available at [http://nobelprize.org/nobel\\_prizes/peace/laureates/2002/carter-lecture.html](http://nobelprize.org/nobel_prizes/peace/laureates/2002/carter-lecture.html), visited on 7 November 2007.

<sup>7</sup> Muhammad Yunus, Nobel Lecture, Oslo, 10 December 2006, available at [http://nobelprize.org/nobel\\_prizes/peace/laureates/2006/yunus-lecture-en.html](http://nobelprize.org/nobel_prizes/peace/laureates/2006/yunus-lecture-en.html), visited on 7 November 2007.

<sup>8</sup> The World Bank, for instance, estimated that abolishing all trade barriers could increase global income by US\$2.8 trillion and lift 320 million people out of poverty by 2015. See M. Bachchetta and M. Jansen, *Adjusting to Trade Liberalization: The Role of Policy, Institutions and WTO Disciplines*, Special Studies Series (WTO, 2003), 6.



However, to ensure that this opportunity is realised, economic globalisation has to be *managed* and *regulated* at the international level. If not, economic globalisation is likely to be a curse, rather than a blessing, to humankind, aggravating economic inequality, social injustice, environmental degradation and cultural dispossession. The law of the World Trade Organization is currently the most ambitious effort to manage and regulate international trade. By way of introduction to this book, this chapter discusses the need for international rules on international trade, and gives an overview of the basic rules and disciplines of WTO law. It also discusses the different sources of WTO law and examines the sometimes contentious relationship between WTO law and other international law as well as between WTO law and national law.

## 1.2. ECONOMIC GLOBALISATION AND INTERNATIONAL TRADE

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### 1.2.1. The emergence of the global economy

#### 1.2.1.1. The concept of 'economic globalisation'

'Economic globalisation' has been a popular buzzword for more than a decade now. Politicians, government officials, businesspeople, trade unionists, environmentalists, church leaders, public health experts, third-world activists, economists and lawyers all speak of 'economic globalisation'. The concepts of 'globalisation', and, in particular, 'economic globalisation' have been used by many to describe one of the defining features of the post-Cold War world in which we live. But what do these terms mean?

Joseph Stiglitz, former Chief Economist of the World Bank and winner of the Nobel Prize for Economics in 2001, described the concept of globalisation, in his 2002 book, *Globalization and Its Discontents*, as:

the closer integration of the countries and peoples of the world which has been brought about by the enormous reduction of costs of transportation and communication, and the breaking down of artificial barriers to the flow of goods, services, capital, knowledge, and (to a lesser extent) people across borders.<sup>9</sup>

In *The Lexus and the Olive Tree: Understanding Globalisation*, Thomas Friedman, the award-winning journalist of the *New York Times*, defined 'globalisation' as follows:

it is the inexorable integration of markets, nation-states and technologies to a degree never witnessed before – in a way that is enabling individuals, corporations and nation-states to reach around the world farther, faster, deeper and cheaper than ever before, and in a way that is enabling the world to reach into individuals, corporations and nation-states farther, faster, deeper and cheaper than ever before.<sup>10</sup>

<sup>9</sup> J. Stiglitz, *Globalization and Its Discontents* (Penguin, 2002), 9.

<sup>10</sup> T. Friedman, *The Lexus and the Olive Tree: Understanding Globalisation*, 2nd edition (First Anchor Books, 2000), 9.

Economic globalisation is a multifaceted phenomenon which undoubtedly is not yet fully understood. In essence, however, economic globalisation is the gradual integration of national economies into one borderless global economy. It encompasses both (free) international trade and (unrestricted) foreign direct investment. Economic globalisation affects people everywhere and in many aspects of their daily lives. It affects their jobs, their food, their health, their education and their leisure time.

While economic globalisation is often presented as a new phenomenon, it deserves to be mentioned that today's global economic integration is not unprecedented. During the fifty years before the First World War, there were also large cross-border flows of goods and capital and, more than now, of people. In that period, globalisation was driven by the lowering of trade barriers and by significant reductions in transport costs resulting from technological innovations such as railways and steamships. If one looks at the ratio of trade to output, Britain and France are only slightly more open to trade today than they were in 1913, while Japan is less open now than it was then.<sup>11</sup> However, that earlier attempt at globalisation ended with the First World War and was followed by one of the darkest periods in the history of humankind.

While the *trend* towards globalisation is clear, the extent of today's global economic integration can be, and frequently is, exaggerated. International trade should normally force high-cost domestic producers to lower their prices and bring the prices of products and services between different countries closer together. However, large divergences in prices persist. Even within the European Union, price differences from one country to another remain significant for a number of products and services. This is partly due to differences in transport costs, taxes and the efficiency of distribution networks. But it is also due, at least outside the European Union, to the continued existence of important barriers to trade. Further, while goods, services and capital move across borders with greater ease, restrictions on the free movement of workers, i.e. restrictions on economic migration, remain multiple and rigorous.

### Questions and Assignments 1.1

How would you define 'economic globalisation'? Does economic globalisation also affect non-economic matters? Give three concrete examples of how *you* are affected by economic globalisation. Is economic globalisation a historically unique and all-pervasive phenomenon?

#### 1.2.1.2. Forces driving economic globalisation

It is commonly argued that economic globalisation has been driven by two main forces. The first, *technology*, makes globalisation feasible; the second, the

<sup>11</sup> 'One World?', *The Economist*, 18 October 1997.

liberalisation of trade and foreign direct investment, makes it happen.<sup>12</sup> Due to technological innovations resulting in a dramatic fall in transport, communication and computing costs, the natural barriers of time and space that separate national markets have been coming down. Between 1920 and 1990, average ocean freight and port charges for US import and export cargo fell by almost 70 per cent. Between 1930 and 1990, average air-transport fares per passenger mile fell by 84 per cent.<sup>13</sup> The cost of a three-minute telephone call between New York and London has fallen from US\$300 in 1930 to US\$1 in 1997 (in 1996 dollars); the cost of computer processing power has been falling by an average of 30 per cent per year in real terms over recent decades.<sup>14</sup> As noted by Thomas Friedman in his 2005 book, *The World is Flat – A Brief History of the Globalised World in the Twenty-first Century*:

Clearly, it is now possible for more people than ever to collaborate and compete in real time with more other people on more different kinds of work from more different corners of the planet and on more equal footing than at any previous time in the history of the world – using computers, e-mail, networks, teleconferencing, and dynamic new software.<sup>15</sup>

As a result of cheap and efficient communication, companies can locate different parts of their production process in different parts of the world while remaining in close contact. Activities such as writing software or accounting can be carried out anywhere in the world, far away from the customer or consumer. New technological developments are likely to further accelerate the process of economic globalisation.

The second driving force of economic globalisation has been the liberalisation of international trade and foreign direct investment. Over the last fifty years, most developed countries have gradually but significantly lowered barriers to foreign trade and allowed free movement of capital. In recent years, the liberalisation of trade and investment has become a worldwide trend, including in developing countries, although liberalisation still proceeds at different speeds in different parts of the world.

In his book, *Has Globalization Gone Too Far?*, Dani Rodrik, of the John F. Kennedy School of Government at Harvard University, highlighted an arguably less positive dimension of globalisation:

Globalization is not occurring in a vacuum. It is part of a broader trend that we may call marketization. Receding government, deregulation, and the shrinking of social obligations are the domestic counterparts of the intertwining of national economies. Globalization could not have advanced this far without these complementary forces.<sup>16</sup>

While some politicians and opinion-makers claim otherwise, the process of economic globalisation is not irreversible. Lionel Barber, US Managing Editor of the *Financial Times*, noted in 2004:

<sup>12</sup> See also M. Wolf, 'Global Opportunities', *Financial Times*, 6 May 1997.

<sup>13</sup> R. Porter, 'The Global Trading System in the 21st Century', in R. Porter, P. Sauvé A. Subramanian and A. Beviglia Zampetti (eds.), *Efficiency, Equity and Legitimacy: The Multilateral Trading System at the Millennium* (Brookings Institution Press, 2001), 4. <sup>14</sup> 'One World?', *The Economist*, 18 October 1997.

<sup>15</sup> T. Friedman, *The World is Flat – A Brief History of the Globalised World in the Twenty-first Century* (Farrar, Straus & Giroux, 2005), 8.

<sup>16</sup> D. Rodrik, *Has Globalization Gone Too Far?* (Institute for International Economics, 1997), 85.

For all its merits, globalization must never be taken for granted. The continued integration of the world economy depends on support not only from rich beneficiaries in the west but increasingly from the still disadvantaged in Africa, India, and Latin America. Cultural barriers also pose increasingly powerful obstacles to globalization. The rise of Islamic fundamentalism offers an alternative vision of society, one which will appeal to all those left behind in countries with exploding populations and persistent high unemployment among young people.<sup>17</sup>

However, it would be very difficult, and foolhardy, for governments to reverse the current globalisation process. Three reasons come to mind. First, new technology has created distribution channels especially for services, such as satellite communications and the Internet, that governments with protectionist intentions will find very difficult to control. Secondly, liberal international trade policies now have a firm institutional basis in the multilateral trading system of the WTO, discussed in detail in this book. Thirdly, the price to be paid in terms of economic prosperity for withdrawing from the global economy would be very high. Autarkies, such as North Korea, do not flourish in today's world.

### *Questions and Assignments 1.2*

What explains the process of economic globalisation? Could governments reverse the process of economic globalisation? Should they?

#### *1.2.1.3. Facts and figures on world trade and investment*

In 1948, world exports of goods amounted to US\$58 billion per year. By 2006, world exports of goods had increased to US\$11,783 billion, or almost US\$12 trillion, per year.<sup>18</sup> World exports of commercial services, marginal in 1948, amounted in 2006 to US\$2,755 billion.<sup>19</sup>

The ratio of global trade in goods and commercial services to world gross domestic product (GDP) is a reliable measurement of economic globalisation. In 1950, exports of goods and commercial services represented 8 per cent of GDP; in 2000, these exports represented 24.6 per cent of GDP.<sup>20</sup>

It is not only the volume and value of world trade in goods and the ratio of global trade to GDP that have changed significantly over the last fifty years. The share of world trade of various regions of the world also changed over this period. Most remarkable are the decline of the share of North America (the United States, Canada and Mexico) from 28.1 per cent in 1948 to 14.2 per cent in 2006, and the increase of the share of Western Europe (primarily the European

<sup>17</sup> L. Barber, 'A Symposium of Views: Is Continued Globalisation of the World Economy Inevitable?' *The International Economy*, Summer 2004, 70.

<sup>18</sup> See WTO, *International Trade Statistics 2007*, available at [www.wto.org/english/res\\_e/statistics\\_e/its2007\\_e/section1\\_e/i06.xls](http://www.wto.org/english/res_e/statistics_e/its2007_e/section1_e/i06.xls), visited on 30 November 2007.

<sup>19</sup> See WTO, *International Trade Statistics 2007*, available at [www.wto.org/english/res\\_e/statistics\\_e/its2007\\_e/section3\\_e/iii01.xls](http://www.wto.org/english/res_e/statistics_e/its2007_e/section3_e/iii01.xls), visited on 30 November 2007.

<sup>20</sup> See World Bank, *World Data Profile*, available at <http://devdata.worldbank.org/external/CPPProfile.asp?PTYPE=CP&CCODE=WLD>, visited on 1 December 2007.

Union) from 35.1 per cent in 1948 to 42.1 per cent in 2006 (down from 45.9 per cent in 2003).<sup>21</sup> Equally remarkable are the steep decline of the shares of both Latin America (down from 11.3 per cent to 3.6 per cent) and Africa (down from 7.3 per cent to 3.1 per cent), and the significant increase of Asia's share (up from 14 per cent to 27.8 per cent).<sup>22</sup> The share of developing countries, as a group, in world trade has increased over the last fifteen years. However, it must be noted that all fifty least-developed countries together still account for only 0.5 per cent of world trade. Their share has actually fallen over time – it stood at 1.7 per cent in 1970.

Developing countries have registered particularly rapid increases in their ratios of exports to GDP. Exports now account for more than one-quarter of their combined GDP, a proportion which is higher than that of many developed countries.<sup>23</sup> Also, the composition of exports from developing countries has changed in recent years. While many developing countries remain dependent on their exports of primary commodities, the share of manufactured goods has been growing. Since the early 1990s, there has been a boom in high-technology exports, with countries such as China, India and Mexico emerging as major suppliers of cutting-edge technologies, as well as labour-intensive goods.<sup>24</sup>

With respect to trade between developing countries, Supachai Panitchpakdi, the then WTO Director-General and current Secretary-General of UNCTAD, noted:

Enhanced South–South activity offers a potentially great source of expanded trade opportunities in the coming decade. Between 1990 and 2001, South–South trade grew faster than world trade with the share of intra-developing country trade in world merchandise exports rising from 6.5% to 10.6%.<sup>25</sup>

Next to international trade, an important aspect of economic globalisation is foreign direct investment (FDI). FDI inflows have increased from US\$59 billion in 1982 to US\$1,306 billion in 2006.<sup>26</sup> Worldwide employment of personnel in foreign affiliates increased from 21.5 million in 1982 to 72.6 million in 2006.<sup>27</sup>

The *World Investment Report 2007* underlined the growing importance of FDI in developing countries. In 2006, FDI inflows attained their highest level ever for developing countries and transition economies, accounting for US\$379 billion, representing an increase of 55.9 per cent as compared to 2001, when FDI inflows accounted for US\$212 billion.<sup>28</sup> The UNCTAD data also show, however, that foreign investment remains very unequally distributed. In 2006, developed

<sup>21</sup> See WTO, *International Trade Statistics 2007*, available at [www.wto.org/english/res\\_e/statistics\\_e/its2007\\_e/section1\\_e/it06.xls](http://www.wto.org/english/res_e/statistics_e/its2007_e/section1_e/it06.xls), visited on 30 November 2007. <sup>22</sup> *Ibid.*

<sup>23</sup> Oxfam, *Rigged Rules and Double Standards: Trade, Globalization and the Fight Against Poverty*, 2002, Summary of chapter 1, available at [www.maketrade4fair.org](http://www.maketrade4fair.org), visited on 11 August 2003. <sup>24</sup> *Ibid.*

<sup>25</sup> Supachai Panitchpakdi, 'The Doha Development Agenda: What's at Stake for Business in the Developing World?', *International Trade Forum*, August 2003, available at [www.tradeforum.org/news/fullstory.php/aid/557/The\\_Doha\\_Development\\_Agenda:\\_What%92s\\_at\\_Stake\\_for\\_Business\\_in\\_the\\_Developing\\_World\\_.html](http://www.tradeforum.org/news/fullstory.php/aid/557/The_Doha_Development_Agenda:_What%92s_at_Stake_for_Business_in_the_Developing_World_.html), visited on 15 May 2004.

<sup>26</sup> See UNCTAD Secretariat, *World Investment Report 2007: Transnational Corporations, Extractive Industries and Development, An Overview*, available at [www.unctad.org/en/docs/wir2007overview\\_en.pdf](http://www.unctad.org/en/docs/wir2007overview_en.pdf), visited on 30 November 2007, 9. <sup>27</sup> *Ibid.*, 10. <sup>28</sup> *Ibid.*, 2.

economies had a share of 65.7 per cent in global FDI inflows and 84.1 per cent in global FDI outflows, compared to 29 per cent of global inflows and 14.3 per cent of global outflows for developing economies.<sup>29</sup> Least-developed countries accounted for less than 1 per cent of global inward FDI stock in 2006..<sup>30</sup>

The *Financial Times* reported this telling example of economic globalisation in February 2003:

Dr Martens, boot-maker to generations of punks, skinheads and factory workers, will this month quietly end centuries of volume shoe manufacturing in Britain by moving its production to a dusty plain in southern China.

... The Pearl river delta – an area the size of Belgium that winds inland from Hong Kong through a series of tightly packed islands – produces \$10 billion worth of exports and attracts \$1 billion of foreign investment a month. Already, 30m people work in manufacturing here; every day thousands more pour off trains from farms further north.

... The catalyst for the delta's explosive export growth is globalisation. China joined the World Trade Organization last year. Increasing competition, falling transport costs and flagging consumer demand are forcing multi-national manufacturing companies to flock to the region with the lowest production costs.

In Dr Martens' case, fierce price competition from rival US brands already produced in China forced the company's hand. 'It was absolutely obvious from the moment I arrived that we had to move to China like everyone else,' says David Suddens, managing director. Dr Martens will outsource production to factories owned by Pou Chen and Golden Chang, Taiwanese companies that moved to the mainland to take advantage of lower labour costs.

Pou Chen's plants, one in Zhuhai and one in Dongguan, employ 110,000 people and churn out 100m pairs of shoes a year for Nike, Adidas, Caterpillar, Timberland, Hush Puppy, Reebok, Puma and others.

... Dr Martens pays its 1,100 UK workers about \$490 a week and has built a stadium for the local football club. Pou Chen pays about Rmn800 (\$100) a month, or 36 cents an hour, for up to 69 hours a week and provides dormitories for migrant workers who must obey strict curfews. The light, well ventilated working conditions are far better than many visitors expect. Stung by complaints of exploitation, Nike and other buyers have full-time local offices monitoring most aspects of employee life.

... Nevertheless, older shoe factories are beginning to find it hard to attract and retain workers tempted by better-paid jobs in other plants. Pou Chen is opening a factory further inland where labour is more plentiful.<sup>31</sup>

In August 2003, the *Financial Times* reported on the globalisation of the trade in services with the following story:

Clutching her side in pain, the woman with suspected appendicitis who was rushed to a hospital on the outskirts of Philadelphia last week had little time to ponder how dependent her life had become on the relentless forces of globalisation. Within minutes of her arrival at the Crozer-Chester Medical Center, the recommendation on whether to operate was being made by a doctor reading her computer-aided tomography (CAT) scan from a computer screen 5,800 miles away in the Middle East.

Jonathan Schlakman, a Harvard-trained radiologist based in Jerusalem, is one of a new breed of skilled professionals proving that geographic distance is no obstacle to outsourcing even the highest paid jobs to overseas locations. The migration of white-collar work has moved up the value chain from call centre operators and back-office clerks to occupations such as equity research, accounting, computer programming and chip design.

<sup>29</sup> *Ibid.*, 2.      <sup>30</sup> *Ibid.*, 17.

<sup>31</sup> D. Roberts and J. Kynge, 'The New Workshop of the World', *Financial Times*, 3 February 2003.

The trend – still only a trickle at present – may look to some like a temporary fad pursued by companies seeking to cut costs. For trade unions in the US and Europe, it heralds a fundamental restructuring of rich-world economies, akin to the globalisation of manufacturing in the 1980s and the outsourcing of unskilled service jobs in the 1990s.

At present, only 35 patients' scans are transmitted each day from US emergency rooms to Dr Schlakman's small team of doctors in Israel. But with senior radiologists costing up to \$300,000 a year to hire in the US and many emergency cases arriving at night, the use of medical expertise based in a different time zone and earning less than half US rates is almost certain to rise. 'It's much more expensive to use night staff in the US because they need time off the following day,' says Dr Schlakman.<sup>32</sup>

Patients also travel around the world to find good and affordable medical care. An increasing number of foreigners are going to India for heart bypass operations. The average cost, including air fare, is about US\$7,000 – roughly one-quarter of what it would be in the UK private sector – and there are no waiting lists. At the Escorts Heart Institute in New Delhi, almost 4,000 heart operations were performed in the year ending August 2006.<sup>33</sup> At 0.8 per cent, Escorts' mortality rate was comparable with international standards.<sup>34</sup>

### Questions and Assignments 1.3

Discuss the trends in international trade and foreign direct investment over the last ten years. Do these trends reveal an ever-increasing degree of economic globalisation? Comment on the developing countries' share in world trade in goods and services.

## 1.2.2. Economic globalisation: a blessing or a curse?

### 1.2.2.1. Backlash against economic globalisation

Everyone around the world feels the effects of economic globalisation, but these effects are not felt by all in an even or equitable way. Over the last ten years, massive street protests in Seattle, Prague, Montreal, Washington, Geneva, Göteborg, Genoa and Zurich have shown that many people in developed countries are 'dissatisfied' with economic globalisation.<sup>35</sup> As Fred Bergsten, Director of the Institute for International Economics in Washington DC, noted at the 2000 Annual Meeting of the Trilateral Commission:

there is a big backlash against globalization. We see it in the financial world. We certainly see it in the trading world as well. It's much more fundamental than pure economics. We know that globalization does increase income and social disparities within countries. We know that globalization does leave some countries and certainly some groups of people behind. We do know that a lot of Europeans don't want to eat genetically modified American foods and that adds to their resistance to globalization. We know that a lot of Americans worry about races to the bottom, labor standards, environmental standards,

<sup>32</sup> D. Roberts, E. Luce and K. Merchant, 'Service Industries Go Global', *Financial Times*, 20 August 2003.

<sup>33</sup> See [www.ehirc.com/individuals/statistics.htm](http://www.ehirc.com/individuals/statistics.htm), visited on 28 October 2007. <sup>34</sup> *Ibid.*

<sup>35</sup> See 'In the Shadow of Prosperity', *The Economist*, 18 January 2007.



and other perceived doubts about dealing with the rest of the world. We know that a lot of developing countries are raising doubts about the entire system, and such specifics as whether having agreed to the enshrinement of intellectual property rights is really in their national interest. . . . There is therefore a backlash against [globalization], which I think we have to take as an extremely serious economic, political, and social matter.<sup>36</sup>

According to opponents of the current economic globalisation process, there is excessive emphasis on the economic interests of transnational corporations. In their opinion, social, cultural and environmental interests and the interests of developing countries are not sufficiently taken into account. Often, they hold economic globalisation responsible for world poverty and hunger, environmental disasters, unemployment and many other wrongs of today's world. To many, global economic integration is a malignant force that is destroying the livelihood of millions of workers and exacerbates inequality, social injustice and environmental degradation.

A 2001 study by the Institute of International Economics in Washington DC concluded that numerous surveys indicated that a significant number of Americans opposed further liberalisation of trade, immigration and foreign direct investment, and that an absolute majority of Americans wanted liberalisation to go more slowly. According to the study, most Americans know the advantages of open markets but tend to view the costs – especially the supposedly negative impact on American jobs and wages – as more important.<sup>37</sup> In Europe, the popular backlash against economic globalisation is probably even more pronounced. In some European countries, in particular France, there is a widespread perception that globalisation is a product of a conspiracy of ruthless Anglo-Saxons.<sup>38</sup> Also, in leading developing countries such as India and Brazil, sections of the population appear equally fearful of, and hostile towards, further trade liberalisation and economic globalisation. WTO Director-General Pascal Lamy noted in 2007:

[P]ublic opinion has become considerably more anxious about the effects of globalization. We have thus seen concerns, for instance, about the impact on socioeconomic fabrics of increased competition or about outsourcing labour-intensive services. The issue of global trade imbalances has also been taken up in similar terms. Some people are no longer convinced that a rising tide of trade will lift all boats. Many countries today are at a crossroads, whether to continue to support more open trade or erect new walls to imported goods and services or foreign investments.<sup>39</sup>

Unfortunately, the discussion of globalisation and trade liberalisation is often emotionally charged and thus not always productive. Oxfam noted in its 2002 study, *Rigged Rules and Double Standards: Trade, Globalization, and the Fight Against Poverty*, the following:

<sup>36</sup> F. Bergsten, 'The Backlash Against Globalization', Remarks made to the 2000 Annual Meeting of the Trilateral Commission in Tokyo, available at [www.trilateral.org/annmtgs/trialog/trlgtxts/t54/ber.htm](http://www.trilateral.org/annmtgs/trialog/trlgtxts/t54/ber.htm), visited on 15 May 2004.

<sup>37</sup> As reported by R. Dale, 'Anti-Globalization Forces Gain Steam: Movement Brings Together Strange Bedfellows from Right and Left', *International Herald Tribune*, 16 March 2001.

<sup>38</sup> F. Bolkenstein, 'To the Enemies of Globalization', *Wall Street Journal*, 25 September 2000.

<sup>39</sup> See P. Lamy, 'Trends and Issues Facing Global Trade', Speech delivered in Kuala Lumpur, Malaysia on 17 August 2007, available at [www.wto.org/english/news\\_e/sppl\\_e/sppl65\\_e.htm](http://www.wto.org/english/news_e/sppl_e/sppl65_e.htm), visited on 29 October 2007.



Current debates about trade are dominated by ritualistic exchanges between two camps: the 'globaphiles' and the 'globaphobes'. 'Globaphiles' argue that trade is already making globalisation work for the poor. Their prescription for the future is 'more of the same'. 'Globaphobes' turn this world-view on its head. They argue that trade is inherently bad for the poor. Participation in trade, so the argument runs, inevitably leads to more poverty and inequality. The corollary of this view is 'the less trade the better'.

The anti-globalisation movement deserves credit. It has raised profoundly important questions about social justice – and it has forced the failures of globalisation on to the political agenda. However, the war of words between trade optimists and trade pessimists that accompanies virtually every international meeting is counter-productive. Both world views fly in the face of the evidence – and neither offers any hope for the future.<sup>40</sup>

#### 1.2.2.2. Problems of current economic globalisation

Economic globalisation and international trade currently give rise to problems and tensions in developed as well as developing countries.

Bill Jordan, General Secretary of the International Confederation of Free Trade Unions, wrote in December 2000:

If you want to belittle a point of view, it is easiest to caricature that point of view as nothing more than a slogan daubed on a placard and paraded through the streets. Too often this has led to misrepresenting the views of labor unions in the face of globalization . . . The international labor movement is not against globalization; indeed we would agree that globalization can be a big part of the answer to the problems of the world's poor. But it also is a big part of the problem. In other words, globalization is neither entirely beneficial nor entirely harmful. It is not an unstoppable force of nature, but is shaped by those who set the rules. And while it has the potential to help lift more than 2 billion people out of poverty, it is not doing so now.<sup>41</sup>

War on Want, one of the more thought-provoking NGOs with close links to the international labour movement, summarises its position regarding economic globalisation as follows:

Jobs are always welcomed by those who live in the developing world. But many of these employees are paid next to nothing, and work in dangerous conditions facing physical and verbal abuse from their employers. Meanwhile, in the developed world, workers are being laid off at an alarming rate and made to feel that they need to compete with workers in the developing world. The globalisation of trade and investment affects labour standards, working conditions, the environment, human health and many other aspects of our lives. Currently, too little attention is being paid to these effects. We need to ensure there are global rules to govern the effects of a global economy.<sup>42</sup>

War on Want is not opposed to globalisation, but wants to see the benefits of globalisation more evenly spread across the world. According to this NGO, economic globalisation now primarily benefits transnational corporations (TNCs)

<sup>40</sup> Oxfam, *Rigged Rules and Double Standards: Trade, Globalization, and the Fight Against Poverty*, 2002, Summary of chapter 1, available at: [www.maketrade4fair.org/en/index.php?file=03042002153411.htm&cat=3&subcat=3&select=4](http://www.maketrade4fair.org/en/index.php?file=03042002153411.htm&cat=3&subcat=3&select=4), visited on 15 May 2004.

<sup>41</sup> B. Jordan, 'Yes to Globalization, But Protect the Poor', *International Herald Tribune*, 21 December 2000.

<sup>42</sup> Excerpts from 'The Global Workplace', a project of War on Want, available at [www.globalworkplace.org/?lid=74](http://www.globalworkplace.org/?lid=74), visited on 15 May 2004.

and often spells disaster for industries in developing countries as well as for workers worldwide:

TNCs can treat the world like their assembly line – manufacturing goods where labour is cheapest, basing operations where taxes are lowest and selling goods where the price is highest. If taxes or labour laws are imposed in one country, they can simply move to another.<sup>43</sup>

ATTAC, the Association for the Taxation of Financial Transactions for the Aid of Citizens, takes a similar position against ‘corporate globalisation’, which, it contends, results in:

the concentration of wealth in the hands of the rich few, growing inequality within and between nations, increasing poverty for the majority of the world’s peoples, displacement of farmers and workers especially in third world countries, and unsustainable patterns of production and consumption.<sup>44</sup>

ATTAC argues for the replacement of the current ‘unfair and oppressive trade system’ with a new, socially just and sustainable trading framework. This framework should be one that protects cultural, biological, economic and social diversity; introduces progressive policies to prioritise local economies and trade; secures internationally recognised economic, cultural, social and labour rights; and reclaims the sovereignty of peoples and national and subnational democratic decision-making processes.<sup>45</sup>

Daniel Mittler from Greenpeace International noted in 2004:

Greenpeace opposes the current form of globalization that is increasing corporate power. Free trade at all costs is leading to the overuse of natural resources, more pollution as we produce and consume more, and greater inequities both among and within countries. This kind of globalization will and should be obstructed. If it were to continue unchecked, the global ecosystem will collapse. Business as usual is in real danger of undermining the ecological basis of our economic system.<sup>46</sup>

Developing countries’ governments and third-world activists commonly argue: first, that developing countries are being forced to open their markets too far, too fast; secondly, that rich countries are conspiring to keep their markets closed to products from developing countries which compete with their products (in particular agricultural products, textiles and clothing); and, thirdly, that developing countries lack the resources and the information to negotiate effectively, to implement trade agreements and to exploit world trade rules to their advantage. Former UN Secretary-General Kofi Annan once noted:

Try to imagine what globalization can possibly mean to the half of humanity that has never made or received a telephone call; or to the people of Sub-Saharan Africa, who have less Internet access than the inhabitants of the borough of Manhattan.<sup>47</sup>

<sup>43</sup> *Ibid.*

<sup>44</sup> Excerpts from ATTAC Quarterly Report, September 2001, *International Trade*, no. 2, vol. I, available at [www.attac.org](http://www.attac.org), visited on 11 August 2003. <sup>45</sup> *Ibid.*

<sup>46</sup> L. Barber, ‘A Symposium of Views: Is Continued Globalisation of the World Economy Inevitable?’ *The International Economy*, Summer 2004, 74.

<sup>47</sup> From the Address by UN Secretary-General Kofi Annan in Davos, Switzerland, on 28 January 2001 to the World Economic Forum, available at [www.unis.unvienna.org/unis/pressrels/2001/sg2772.html](http://www.unis.unvienna.org/unis/pressrels/2001/sg2772.html), visited on 13 August 2003.

While not sharing the extreme positions of anti-globalists and being careful ‘not to make the mistake of attributing to globalization the blemishes of other faces’,<sup>48</sup> many observers and scholars recognise the dangers of the economic globalisation process.

In his 2002 book, *Globalization and Its Discontents*, Joseph Stiglitz reflected on the bright side of globalisation as follows:

Opening up to international trade has helped many countries grow far more quickly than they would otherwise have done. International trade helps economic development when a country’s exports drive its economic growth. Export-led growth was the centrepiece of the industrial policy that enriched much of Asia and left millions of people there far better off. Because of globalization many people in the world now live longer than before and their standard of living is far better. People in the West may regard low-paying jobs at Nike as exploitation, but for many people in the developing world, working in a factory is a far better option than staying down on the farm and growing rice.

Globalization has reduced the sense of isolation felt in much of the developing world and has given many people in the developing countries access to knowledge well beyond the reach of even the wealthiest in any country a century ago . . . Even when there are negative sides to globalization, there are often benefits. Opening up the Jamaican milk market to US imports in 1992 may have hurt local dairy farmers but it also meant poor children could get milk more cheaply. New foreign firms may hurt protected state-owned enterprises but they can also lead to the introduction of new technologies, access to new markets, and the creation of new industries.<sup>49</sup>

Stiglitz commented that those who vilify globalisation too often overlook its benefits.<sup>50</sup> However, Stiglitz pointed out:

[T]he proponents of globalization have been, if anything, even more unbalanced. To them, globalization (which typically is associated with accepting triumphant capitalism, American style) *is* progress; developing countries must accept it, if they are to grow and to fight poverty effectively. But to many in the developing world, globalization has not brought the promised economic benefits.<sup>51</sup>

Elsewhere, Stiglitz wrote about the problems and dangers of current economic globalisation and trade liberalisation:

We should be frank. Trade liberalization, conducted in the wrong way, too fast, in the absence of adequate safety nets, with insufficient reciprocity and assistance on the part of developed countries, can contribute to an increase in poverty . . .

Complete openness can expose a country to greater risk from external shocks. Poor countries may find it particularly hard to buffer these shocks and to bear the costs they incur, and they typically have weak safety nets, or none at all, to protect the poor. These shocks, resulting essentially from contagion associated with globalization, integration and interdependence can affect workers and employers in the developed world. It must be said, however, that highly industrialized countries are able to deal with these shocks a lot better through re-employment and through other safety nets.<sup>52</sup>

In 2006, Stiglitz reflected on the dark side of globalisation as follows:

<sup>48</sup> J. Bhagwati, ‘Globalization in Your Face’, *Foreign Affairs*, July/August 2000, 137.

<sup>49</sup> J. Stiglitz, *Globalization and Its Discontents* (Penguin, 2002), 4–5.

<sup>50</sup> *Ibid.*, 5

<sup>51</sup> *Ibid.*

<sup>52</sup> J. Stiglitz, ‘Addressing Developing Country Priorities and Needs in the Millennium Round’, in R. Porter and P. Sauvé (eds.), *Seattle, the WTO and the Future of the Multilateral Trading System* (Harvard University Press, 2000), 53–5.

There were once hopes that globalisation would benefit all, both in advanced industrial countries and the developing world. Today, the downside of globalisation is increasingly apparent. Not only do good things go more easily across borders, so do bad; including terrorism. We see an unfair global trade regime that impedes development and an unstable global financial system in which poor countries repeatedly find themselves with unmanageable debt burdens. Money should flow from the rich to the poor countries, but increasingly, it goes in the opposite direction.

What is remarkable about globalisation is the disparity between the promise and the reality. Globalisation seems to have unified so much of the world against it, perhaps because there appear to be so many losers and so few winners . . . Growing inequality in the advanced industrial countries was a long predicted but seldom advertised consequence: full economic integration implies the equalisation of unskilled wages throughout the world. Although this has not (yet) happened, the downward pressure on those at the bottom is evident. Unfettered globalisation actually has the potential to make many people in advanced industrial countries worse off, even if economic growth increases.<sup>53</sup>

On the positive and negative aspects of economic globalisation, Pascal Lamy, the WTO Director-General, made the following remarks in August 2007:

Globalization has enabled individuals, corporations and nation-states to influence actions and events around the world – faster, deeper and cheaper than ever before – and equally to derive benefits for them. Trade opening and the vanishing of many walls have the potential for expanding freedom, empowerment, democracy, innovation, social and cultural exchanges, while offering outstanding opportunities for dialogue and understanding. This is the good side of globalization.

But the global nature of an increasing number of worrisome phenomena – the scarcity of energy resources, the deterioration of the environment, the migratory movements provoked by insecurity, poverty and political instability or even financial markets volatility, as we have seen in recent weeks – are also by-products of globalization. Indeed, it can be argued that in some instances, globalization has reinforced the strong economies and weakened those that were already weak.<sup>54</sup>

In a 2007 contribution to the *Financial Times*, Dani Rodrik asked whether the greatest threat to globalization is: the ‘protesters on the streets every time the International Monetary Fund or the World Trade Organization meets’, or ‘globalisation’s cheerleaders, who push for continued market opening while denying that the troubles surrounding globalisation are rooted in the policies they advocate’.<sup>55</sup> According to Rodrik:

A good case can be made that the latter camp presents the greater menace. Anti-globalisers are marginalised. But cheerleaders in Washington, London and the elite universities of north America and Europe shape the intellectual climate. If they get their way, they are more likely to put globalisation at risk than the protesters they condemn for ignorance of sound economics. That is because the greatest obstacle to sustaining a healthy, globalised economy is no longer insufficient openness. Markets are freer from government interference than they have ever been. Import restrictions such as tariff and non-tariff barriers are lower than ever. Capital flows in huge magnitudes. Despite barriers, legal and illegal immigration approaches levels not seen since the 19th century . . . Closed markets may have been a fundamental problem during the 1950s and 1960s; it is hard to believe they still are.

<sup>53</sup> J. Stiglitz, ‘We Have Become Rich Countries of Poor People’, *Financial Times*, 7 September 2006.

<sup>54</sup> See P. Lamy, ‘Trends and Issues Facing Global Trade’, Speech delivered in Kuala Lumpur, Malaysia on 17 August 2007, available at [www.wto.org/english/news\\_e/sppl\\_e/sppl65\\_e.htm](http://www.wto.org/english/news_e/sppl_e/sppl65_e.htm), visited on 29 October 2007.

<sup>55</sup> D. Rodrik, ‘The Cheerleaders’ Threat to Global Trade’, *Financial Times*, 26 March 2007.

The greatest risk to globalisation is elsewhere. It lies in the prospect that national governments' room for manoeuvre will shrink to such levels that they will be unable to deliver the policies that their electorates want and need in order to buy into the global economy.<sup>56</sup>

In Rodrik's opinion, developed and developing countries need flexibility – or 'breathing space' – to interfere in trade:

Rich countries need . . . flexibility to interfere in trade when trade conflicts with deeply held values at home – as, for example, with child labour or health and safety concerns – or severely weakens the bargaining power of workers. Poor nations need room to engage in exchange rate and industrial policies that will diversify and restructure their economies, without which their ability to benefit from globalisation is circumscribed.<sup>57</sup>

In reply to the question contained in the title of his 1997 book, *Has Globalization Gone Too Far?*, Rodrik had already stated that, in his opinion, this is not the case if 'policymakers act wisely and imaginatively'.<sup>58</sup>

In *The Lexus and the Olive Tree*, Thomas Friedman also saw the need for government action when he noted:

the more I observed the system of globalization at work, the more obvious it was that it had unleashed forest-crushing forces of development and Disney-round-the-clock homogenization, which, if left unchecked, had the potential to destroy the environment and uproot cultures at a pace never before seen in human history.<sup>59</sup>

### Questions and Assignments 1.4

What are the main dangers associated with the current process of economic globalisation? Who stands to gain most from the current process of economic globalisation? Who loses?

## 1.2.3. Trade liberalisation versus protectionism

### 1.2.3.1. The case for international trade and liberalisation

Economic globalisation in general and international trade in particular is blamed by many for much that is wrong in today's world: from hunger and child labour to environmental pollution and cultural impoverishment. Is international trade beneficial to anyone other than multinational corporations, the well-educated in developed countries and the privileged elite in developing countries? Can economic globalisation in general and international trade in particular benefit all humankind?

Most economists agree that countries can benefit from international trade. In 1776, Adam Smith wrote in his classic book, *The Wealth of Nations*:

<sup>56</sup> *Ibid.*      <sup>57</sup> *Ibid.*

<sup>58</sup> D. Rodrik, *Has Globalization Gone Too Far?* (Institute for International Economics, 1997), 9.

<sup>59</sup> T. Friedman, *The Lexus and the Olive Tree: Understanding Globalisation*, 2nd edition (First Anchor Books, 2000), 23.

It is the maxim of every prudent master of a family, never to attempt to make at home what it will cost him more to make than to buy. The tailor does not attempt to make his own shoes, but he buys them from the shoemaker. The shoemaker does not attempt to make his own cloths, but employs a tailor. The farmer attempts to make neither the one nor the other, but employs those different artificers. All of them find it for their interest to employ their whole industry in a way in which they have some advantage over their neighbours, and to purchase with a part of its produce, or what is the same thing, with the price of a part of it, whatever else they have occasion for.

What is prudence in the conduct of every private family, can scarce be folly in that of a great kingdom. If a foreign country can supply us with a commodity cheaper than we ourselves can make it, better buy it of them with some part of the produce of our own industry, employed in a way in which we have some advantage. The general industry of the country . . . will not thereby be diminished, no more than the above-mentioned artificers; but only left to find out the way in which it can be employed with the greatest advantage. It is certainly not employed to the greatest advantage, when it is thus directed towards an object which it can buy cheaper than it can make.<sup>60</sup>

Smith's lucid and compelling argument for specialisation and international trade was further built upon by David Ricardo who, in his 1817 book, *The Principles of Political Economy and Taxation*, developed the theory of 'comparative advantage'. This theory is still the predominant explanation for why countries, even the poorest, can and do benefit from international trade.

What did the classical economist David Ricardo (1772–1823) mean when he coined the term *comparative advantage*? Suppose country A is better than country B at making automobiles, and country B is better than country A at making bread. It is obvious (the academics would say 'trivial') that both would benefit if A specialized in automobiles, B specialized in bread and they traded their products. That is a case of *absolute* advantage. But what if a country is bad at making everything? Will trade drive all producers out of business? The answer, according to Ricardo, is no. The reason is the principle of comparative advantage, arguably the single most powerful insight in economics. According to the principle of comparative advantage, countries A and B still stand to benefit from trading with each other even if A is better than B at making everything, both automobiles and bread. If A is much more superior at making automobiles and only slightly superior at making bread, then A should still invest resources in what it does best – producing automobiles – and export the product to B. B should still invest in what it does best – making bread – and export that product to A, even if it is not as efficient as A. Both would still benefit from the trade. A country does not have to be best at anything to gain from trade. That is *comparative* advantage. The theory is one of the most widely accepted among economists. It is also one of the most misunderstood among non-economists because it is confused with *absolute* advantage. It is often claimed, for example, that some countries have no comparative advantage in anything. That is virtually impossible. Think about it . . .<sup>61</sup>

The Ricardo model is of course a vast simplification, in that it is built on two products and two countries only and assumes constant costs and constant prices. Many of the complexities of the modern economy are not taken into account in this model. Economists in the twentieth century have endeavoured to refine and build on the classic Ricardo model. While pushing the analysis further, the refined models, such as the Heckscher–Ohlin model, have confirmed

<sup>60</sup> A. Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations* (1776), edited by E. Cannan (University of Chicago Press, 1976), vol. 1, 478–9.

<sup>61</sup> WTO Secretariat, *Trading into the Future*, 2nd edition, revised (WTO, 2001), 9.

the basic conclusions drawn from the Ricardo model concerning the theory of comparative advantage and the gains from trade via specialisation.<sup>62</sup>

While the theory of comparative advantage has won approval from most economists since the early nineteenth century and continues to win approval,<sup>63</sup> Jagdish Bhagwati observed in *Free Trade Today* that it has only infrequently carried credibility with the populace at large. In search of an explanation, he noted that when asked which proposition in the social science was the most counterintuitive yet compelling, Paul Samuelson, the 1970 winner of the Nobel Prize for Economics, chose the theory of comparative advantage.<sup>64</sup>

According to Samuelson, there is essentially only one – but one very powerful – argument for freer trade:

Free trade promotes a mutually profitable division of labor, greatly enhances the potential real national product for all nations, and makes possible higher standards of living all over the globe.<sup>65</sup>

On the question whether free trade, or rather freer international trade, indeed leads to greater economic growth, Jagdish Bhagwati observed:

So those who assert that free trade will also lead necessarily to greater growth *either* are ignorant of the finer nuances of theory and the vast literature to the contrary on the subject at hand *or* are nonetheless basing their argument on a different premise: that is, that the preponderant evidence on the issue (in the postwar period) suggests that freer trade tends to lead to greater growth after all.<sup>66</sup>

A 2001 study by the World Bank showed that the developing countries that increased their integration into the world economy in the 1980s and 1990s achieved higher growth in incomes, longer life expectancy and better schooling. These countries, home to some 3 billion people, enjoyed an average 5 per cent growth rate in income per capita in the 1990s compared to 2 per cent in developed countries. Many of these countries, including China and India, have adopted domestic policies and institutions that have enabled people to take advantage of global markets and have thus sharply increased the share of trade in their GDP. These countries have been catching up with the rich ones – their annual growth rates increased from 1 per cent in the 1960s to 5 per cent in the 1990s. In 2006, India and China achieved an economic growth of 9.4 per cent and 11.1 per cent respectively.<sup>67</sup> However, not all countries have integrated successfully into the

<sup>62</sup> Note, however, as Jagdish Bhagwati does, that: 'The case of free trade rests on the extension to an open economy of the case for market-determined allocation of resources. If market prices reflect "true" or social costs, then clearly Adam Smith's invisible hand can be trusted to guide us to efficiency; and free trade can correspondingly be shown to be the optimal way to choose trade (and associated domestic production). But if markets do not work well, or are absent or incomplete, then the invisible hand may point in the wrong direction: free trade cannot then be asserted to be the best policy.' See J. Bhagwati, *Free Trade Today* (Princeton University Press, 2002), 12.

<sup>63</sup> For a dissenting, neo-Marxist view from legal scholars, see M. H. Davis and D. Neacsu, 'Legitimacy, Globally: The Incoherence of Free Trade Practice, Global Economics and Their Governing Principles of Political Economy', *Kansas City Law Review*, 2001, 733–90.

<sup>64</sup> See J. Bhagwati, *Free Trade Today* (Princeton University Press, 2002), 5.

<sup>65</sup> P. Samuelson, *Economics*, 10th edition (1976), 692.

<sup>66</sup> J. Bhagwati, *Free Trade Today* (Princeton University Press, 2002), 42.

<sup>67</sup> The Economist Intelligence Unit: Country Briefings: China, available at [www.economist.com/countries/China/profile.cfm?folder=Profile-Economic%20Structure](http://www.economist.com/countries/China/profile.cfm?folder=Profile-Economic%20Structure), and India, available at [www.economist.com/countries/India/profile.cfm?folder=Profile-Economic%20Structure](http://www.economist.com/countries/India/profile.cfm?folder=Profile-Economic%20Structure), visited on 29 October 2007.



global economy. The World Bank's 2001 report found that some 2 billion people – particularly in Sub-Saharan Africa, the Middle East and the former Soviet Union – live in countries that are being left behind. On average these economies have contracted, poverty has increased and education levels have risen less rapidly than in the more globalised countries.<sup>68</sup>

As a 2000 WTO study, *Trade, Income Disparity and Poverty*, on the relationship between international trade and poverty concluded, the evidence seems to indicate that trade liberalisation is *generally* a positive contributor to poverty alleviation. It allows people to exploit their productive potential, assists economic growth, curtails arbitrary policy interventions and helps to insulate against shocks in the domestic economy. The study warned, however, that most trade reforms will create some losers (some even in the long run). Poverty may be exacerbated temporarily, but the appropriate policy response in those cases is to alleviate the hardship and facilitate adjustments rather than abandon the reform process.<sup>69</sup> A 2003 WTO study, *Adjusting to Trade Liberalization*, concluded that adjustment costs are typically smaller, and sometimes much smaller, than the gains from trade.<sup>70</sup> Also, governments can identify individuals and groups that are likely to suffer from the adjustment process, and they can develop policies to alleviate the burden on those adversely affected.<sup>71</sup>

In its 2002 study, *Rigged Rules and Double Standards: Trade, Globalization, and the Fight Against Poverty*, Oxfam stated:

History makes a mockery of the claim that trade cannot work for the poor. Participation in world trade has figured prominently in many of the most successful cases of poverty reduction – and, compared with aid, it has far more potential to benefit the poor.<sup>72</sup>

According to Oxfam, since the mid-1970s rapid growth in exports has contributed to a wider process of economic growth which has lifted more than 400 million people out of poverty.<sup>73</sup> Few will question that international trade has the *potential* to make a significant contribution to economic growth and poverty reduction. However, it is definitely not a 'magic bullet for achieving development'.<sup>74</sup> More is needed to achieve sustained economic growth and widespread poverty reduction.<sup>75</sup>

International trade not only has the potential for bringing economic benefits, there may also be considerable non-economic gains. International trade increases both the incentives for not making war and the costs of going to war.

<sup>68</sup> P. Collier and D. Dollar, *Globalization, Growth and Poverty: Building an Inclusive World Economy* (World Bank, 2001), available at <http://econ.worldbank.org>, visited on 15 May 2004. See also J. Sachs and A. Warner, 'Economic Reform and the Process of Global Integration', *Brookings Papers on Economic Activity*, 1 (1995), 1–95; and A. Krueger, 'Trade Policy and Economic Development: How We Learn', *NBER Working Paper Series* (Working Paper 5896) (1997).

<sup>69</sup> See D. Ben-David, H. Nordström and A. Winters, *Trade, Income Disparity and Poverty*, Special Studies Series (WTO, 2000), 6.

<sup>70</sup> See M. Bacchetta and M. Jansen, *Adjusting to Trade Liberalization: The Role of Policy, Institutions and WTO Disciplines*, Special Studies Series (WTO, 2003), 6. <sup>71</sup> *Ibid.*

<sup>72</sup> Oxfam, *Rigged Rules and Double Standards: Trade, Globalization, and the Fight Against Poverty*, 2002, Summary of chapter 2, available at [www.maketrade-fair.org](http://www.maketrade-fair.org), visited on 11 August 2003. <sup>73</sup> *Ibid.*

<sup>74</sup> See Justice C. Nwobike, 'The Emerging Trade Regime under the Cotonou Partnership Agreement: Its Human Rights Implications', *Journal of World Trade*, 2006, 292. <sup>75</sup> See below, p. ##.



International trade intensifies cross-border contacts and exchange of ideas, which may contribute to better mutual understanding. In a free-trading world, other countries and their people are more readily seen as business partners, less as enemies. As Baron de Montesquieu wrote in 1748 in *De l'Esprit des Lois*:

Peace is the natural effect of trade. Two nations who traffic with each other become reciprocally dependent; for if one has an interest in buying, the other has an interest in selling; and thus their union is founded on their mutual necessities.<sup>76</sup>

A country taking trade-restrictive measures directly inflicts economic hardship upon exporting countries. Therefore, trade protectionism is a festering source of conflict. It is often stated that 'if goods do not cross frontiers, soldiers will'.<sup>77</sup> Likewise, international trade can make an important contribution to peaceful and constructive international relations. Just two weeks after the terrorist attacks of 11 September 2001 on the World Trade Center in New York and on the Pentagon in Washington DC, Robert Zoellick, the then US Trade Representative and current President of the World Bank, made the following simple but profound statement about the importance of continued openness in trade:

Let me be clear where I stand: Erecting new barriers and closing old borders will not help the impoverished. It will not feed hundreds of millions struggling for subsistence. It will not liberate the persecuted. It will not improve the environment in developing countries or reverse the spread of AIDS. It will not help the railway orphans I visited in India. It will not improve the livelihoods of the union members I met in Latin America. It will not aid the committed Indonesians I visited who are trying to build a functioning, tolerant democracy in the largest Muslim nation in the world.<sup>78</sup>

Two months after the attacks of 11 September 2001, the WTO Members agreed to start the Doha Development Round, a new round of negotiations on the further liberalisation of international trade. According to WTO Director-General Pascal Lamy, the rationale behind this decision was, and in his view remains, simple: 'terrorism is about increasing instability; global trade rules are about promoting stability'.<sup>79</sup>

However, as Edward Alden wrote in the *Financial Times* in February 2003:

US trade policy risks isolating the Muslim states that are on the front line in the war on terrorism, according to a study released on Tuesday. The report – from the Washington-based Progressive Policy Institute – warns that the Muslim world has been 'the blank spot on the map of the Bush administration's trade policy'. It adds: 'That policy risks undermining, rather than supporting, the war on terrorism.' The failing economies of many

<sup>76</sup> C. de Montesquieu, *De l'Esprit des Lois*, original version available online at [http://classiques.uqac.ca/classiques/montesquieu/de\\_esprit\\_des\\_lois/de\\_esprit\\_des\\_lois\\_tdm.html](http://classiques.uqac.ca/classiques/montesquieu/de_esprit_des_lois/de_esprit_des_lois_tdm.html). An English translation by Thomas Nugent is available at [www.constitution.org/cm/sol.htm](http://www.constitution.org/cm/sol.htm), visited on 8 November 2007.

<sup>77</sup> P. Lamy, 'Managing Global Security: the Strategic Importance of Global Trade', Speech to the International Institute for Strategic Studies, in Geneva on 8 September 2007, available at [www.wto.org/english/news\\_e/sppl\\_e/sppl66\\_e.htm](http://www.wto.org/english/news_e/sppl_e/sppl66_e.htm), visited on 28 October 2007.

<sup>78</sup> As reported by the then WTO Director-General Mike Moore in a speech to the Foreign Affairs Commission of the French Assemblée Nationale in October 2001, available at [www.wto.org](http://www.wto.org), visited on 6 February 2004.

<sup>79</sup> P. Lamy, 'Managing Global Security: the Strategic Importance of Global Trade', Speech to the International Institute for Strategic Studies, in Geneva on 8 September 2007, available at [www.wto.org/english/news\\_e/sppl\\_e/sppl66\\_e.htm](http://www.wto.org/english/news_e/sppl_e/sppl66_e.htm), visited on 28 October 2007.

Muslim states have been repeatedly acknowledged by the White House as fertile recruiting grounds for terrorist groups. But critics say the US has done little to tackle the problem, and has been stingy with trade concessions to some of its closest allies in the war on terrorism. Kursheed Kasuri, Pakistan's foreign minister, said last week that 'economics is the key to fighting terrorism', and criticised Washington for failing to offer greater trade concessions. Pakistan had hoped for about \$1 billion in additional sales of textiles and clothing to the US to offset the costs of the war on terrorism, but – under pressure from its own textile industry – the US granted just \$143m.<sup>80</sup>

Apart from peaceful relations between nations, open international trade may also promote democracy. In *Free Trade Today*, Jagdish Bhagwati observed:

One could argue this proposition by a syllogism: openness to the benefits of trade brings prosperity that, in turn, creates or expands the middle class that then seeks the end of authoritarianism. This would fit well with the experience in South Korea, for instance. It was also the argument that changed a lot of minds when the issue of China's entry into the WTO came up in the US Congress recently. I guess there is something to it.<sup>81</sup>

It has been reported that international trade and investment have already had a certain impact on the political system in China:

Not only is the southern boom town of Shenzhen about to be designated a test-bed for the boldest political reform since the 1949 revolution but cities in coastal China are also embarking on experiments to introduce checks and balances to single party rule. Yu Youjun, mayor of Shenzhen, said in an interview that the wishes of multinational corporations were one motive for the city's experiment. Foreign companies, especially those establishing high-technology factories, are mindful of the need to protect intellectual property. For this, they need a fair local government. 'Every multinational company and investor is influenced by the investment environment created by governments', said Mr Yu, whose city was chosen 22 years ago as a laboratory for China's first capitalist reforms and now leads the country in per capita income. The 'hard environment' of roads, railways, ports and telecommunications was important for multinationals, Mr Yu said. But more crucial was the 'soft environment', meaning a government that is 'democratic' and transparent. 'We have made achievements in building our economic structural reform', said Mr Yu. 'Now we need to make reforms to our political system to promote democratic politics.'<sup>82</sup>

### 1.2.3.2. *Reasons and excuses for protectionist trade policies*

While most economists advise that countries should – in their own interest and that of the world at large – pursue policies aimed at promoting international trade and exchange goods and services on the basis of their comparative advantage, political decision-makers do not necessarily heed this wise advice. In fact, countries frequently intervene in international trade by adopting trade restrictive measures. Why do countries restrict international trade? Why do they adopt protectionist trade policies? A prime reason is to protect a domestic industry, and employment in that industry, from competition arising from imported products, foreign services or service suppliers. As noted in the 2003 WTO study on *Adjusting to Trade Liberalization*:

<sup>80</sup> E. Alden, 'US Trade Policy "Isolates Muslim States"', *Financial Times*, 4 February 2003.

<sup>81</sup> J. Bhagwati, *Free Trade Today* (Princeton University Press, 2002), 43–4.

<sup>82</sup> D. Roberts and J. Kynge, 'The New Workshop of the World', *Financial Times*, 3 February 2003.

In the United States, for instance, 45,000 steelworkers have lost their jobs since 1997 and 30 per cent of the country's steel making capacity has filed for bankruptcy since 1998, while steel imports were on the rise. In Mozambique liberalization of trade in cashew nuts resulted in 8,500 of 10,000 cashew processing workers losing their jobs.<sup>83</sup>

When a domestic industry is in crisis and jobs are lost, the political decision-makers may well 'scramble for shelter' by adopting protectionist measures.<sup>84</sup> This may happen even when the decision-makers are well aware that such measures are by no means the best response to the crisis in the industry concerned. While the import competition would probably benefit most of their constituents (through lower prices, better quality and/or more choice), import competition is likely to hurt a small group of their constituents significantly (through lower salaries or job losses). If this small group is vocal and well organised, as it often is, it will put a great deal of pressure on the elected decision-makers to take protectionist measures for the benefit of the few and to the detriment of the many. In such a situation, protectionism can constitute 'good' politics.<sup>85</sup> The *public choice theory* explains that, when the majority of the voters are unconcerned with the (*per capita* small) losses they suffer, the vote-maximising political decision-makers will ignore the interests of the many, and support the interests of the vocal and well-organised few. WTO Director-General Pascal Lamy has called for recognition of the fact that the politics of trade suffer from an 'inbuilt asymmetry'. He noted:

[T]hose who benefit from gains in purchasing power stemming from trade opening are millions, but they are little aware of the source of their gains. Those who suffer from trade opening are thousands who can easily identify the source of their pain. For politicians, such an asymmetry is difficult to cope with and too often the easy way out is to treat foreigners as scapegoats, which we know is one of the safest old tricks of domestic politics.<sup>86</sup>

However, as discussed above, trade protectionist measures to protect the interests of some eventually leave everyone worse off. Joseph Stiglitz, reflecting on his own experience as Chairman of the Council of Economic Advisors in the Clinton Administration, observed in this respect:

One might have thought that each country would promote liberalization in those sectors where it had most to gain from a societal perspective; and similarly, that it would be most willing to give up protectionism in those sectors where protection was costing the most. But political logic prevails over economic logic: after all, if economic logic dominated, countries would engage in trade liberalization on their own. High levels of protection are usually indicative of strong political forces, and these higher barriers may be the last to give way . . . The political force behind the resistance to free trade is a simple one: Although the country as a whole may be better off under free trade, some special interests will actually be worse off. And although policy could in principle rectify this situation (by

<sup>83</sup> M. Bacchetta and M. Jansen, *Adjusting to Trade Liberalization: The Role of Policy, Institutions and WTO Disciplines*, Special Studies Series (WTO, 2003), 6.

<sup>84</sup> 'Survey World Trade', *The Economist*, 3 October 1998, 3.

<sup>85</sup> B. Hoekman and M. Kostecki, *The Political Economy of the World Trading System: The WTO and Beyond*, 2nd edition (Oxford University Press, 2001), 22.

<sup>86</sup> See P. Lamy, 'Trends and Issues Facing Global Trade', Speech delivered in Kuala Lumpur, Malaysia on 17 August 2007, available at [www.wto.org/english/news\\_e/sppl\\_e/sppl65\\_e.htm](http://www.wto.org/english/news_e/sppl_e/sppl65_e.htm), visited on 29 October 2007.

using redistribution to make everybody better off), in actuality, the required compensations are seldom paid.<sup>87</sup>

Another reason for national decision-makers to pursue a protectionist trade policy is *infant industry protection*.<sup>88</sup> The argument for infant industry protection was made by Alexander Hamilton in 1791, Friedrich List in 1841 and John Stuart Mill in 1848, and has been invoked many times since. In the nineteenth century, the infant manufacturing industries of the United States and Germany were protected against import competition on the basis of this argument. Today, this argument may be of particular relevance to developing countries, which may find that while they have a potential comparative advantage in certain industries, new producers in these countries cannot (yet) compete with established producers in the developed countries. By means of a customs duty or import restriction, temporary protection is then given to the national producers to allow them to become strong enough to compete with well-established producers. The infant industry argument for protectionist measures has definitely some appeal and validity. However, protecting the new producers from import competition does not necessarily remedy the problems that caused the new producers to be uncompetitive. Furthermore, the success of an infant industry policy crucially depends on a correct diagnosis of which industries could over time become competitive. It is often very difficult for governments to identify, in an objective manner and free from pressure from special interest groups, the new industries that merit protection. Moreover, in practice, the protection, which is by nature intended to be temporary, frequently becomes permanent. When it becomes clear that the protected national industry will never 'grow up' and will always be unable to face import competition, it is often politically difficult to remove the protection in place.<sup>89</sup>

When a country is in a position to lower the price it pays for imports by restricting its imports, national decision-makers of that country may also be tempted to adopt trade restrictive measures on the basis of the *optimal tariff* argument. If a country can reduce world demand for a product, by raising the tariff on that product, it may make economic sense to raise the tariff, and thus restrict trade, because this will lead to the cutting of the world price of the product concerned. In this way, a country can tilt the terms of trade in its favour. Alan Deardorff and Robert Stern noted in this respect:

This argument is sometimes thought to require that the country in question be large and therefore to apply only to such large industrialized countries as the US. However, the argument applies to some extent to any country that is not insignificantly small. Furthermore the size that is important is not the size of the country as a whole but rather its share of world trade in markets in which it exports and imports.<sup>90</sup>

<sup>87</sup> J. Stiglitz, 'Addressing Developing Country Priorities and Needs in the Millennium Round', in R. Porter and P. Sauvé (eds.), *Seattle, the WTO and the Future of the Multilateral Trading System* (Harvard University Press, 2000), 51–3. <sup>88</sup> See also below, pp. 725–6.

<sup>89</sup> A. Deardorff and R. Stern, 'Current Issues in US Trade Policies: An Overview', in R. Stern (ed.), *US Trade Policies in a Changing World Economy* (Massachusetts Institute of Technology, 1987), 39–40.

<sup>90</sup> *Ibid.*, 37–8.

However, as Deardorff and Stern observed, it is a key feature of the optimal tariff argument that it involves gains by one country at other countries' expense. It is thus referred to as an 'exploitative intervention' policy.

Such policies are typically available to more than one country, each of which can have adverse effects on the others (and even many), and therefore require that strategic issues be considered. Like other forms of exploitative intervention the optimal tariff argument is likely to find countries in the classic position of the Prisoner's Dilemma; that is, each country has available a policy that will benefit itself at the expense of others, but if all countries simultaneously pursue that policy, all are likely to lose.<sup>91</sup>

A relatively new argument for national decision-makers to opt for trade restrictions is the *strategic trade policy* argument. In an industry with economies of scale, a country may, by imposing a tariff or quantitative restriction and thus reserving the domestic market for a domestic firm, allow that firm to cut its costs and undercut foreign competitors in other markets. This may work in an industry where economies of scale are sufficiently large that there is only room for very few profitable companies in the world market. Economists reckon that this might be the case for civil aircraft, semiconductors and cars.<sup>92</sup> The aim of government intervention is to ensure that the domestic rather than a foreign company establishes itself on the world market and thus contributes to the national economic welfare. However, as Paul Krugman noted:

Strategic trade policy aimed at securing excess returns for domestic firms and support for industries that are believed to yield national benefits are both beggar-thy-neighbour policies and raise income at the expense of other countries. A country that attempts to use such policies will probably provoke retaliation. In many (though not all) cases, a trade war between two interventionist governments will leave both countries worse off than if a hands-off approach were adopted by both.<sup>93</sup>

This does not mean that such policies will not be pursued, because, as Krugman also pointed out:

Governments do not necessarily act in the national interest, especially when making detailed microeconomic interventions. Instead, they are influenced by interest group pressures. The kinds of interventions that new trade theory suggests can raise national income will typically raise the welfare of small, fortunate groups by large amounts, while imposing costs on larger, more diffuse groups. The result, as with any microeconomic policy, can easily be that excessive or misguided intervention takes place because the beneficiaries have more knowledge and influence than the losers.<sup>94</sup>

Trade-restrictive measures, and, in particular, customs duties, have also been and still are imposed to *generate revenue for government*. Taxing trade is an easy method to collect revenue. While taxation of trade for revenue is no longer significant for developed countries, for many developing country governments customs duties remain a significant source of revenue.<sup>95</sup>

<sup>91</sup> *Ibid.*, 37–8.      <sup>92</sup> 'Survey World Trade', *The Economist*, 3 October 1998, 6.

<sup>93</sup> P. Krugman, 'Is Free Trade Passé?', *Journal of Economic Perspectives*, 1987, 141.

<sup>95</sup> See below, pp. 404–5, 409–11.

<sup>94</sup> *Ibid.*

Governments also adopt trade restrictive measures for reasons of *national security* and *self-sufficiency*. The steel industry, as well as farmers, can, for example, be heard to argue that their presence and prosperity is essential to the national security of the country. The basic argument is that a country should be able to rely on its domestic industries and farmers to meet its basic needs for vital material and food, because it will be impossible to rely – in times of crisis and conflict – on imports from other countries. Allan Sykes noted in this respect:

The likelihood of imports becoming unavailable in wartime must then be carefully considered. For a nation like the United States, serious interruption of seaborne commercial traffic seems unlikely to occur for most goods and commodities in any scenario short of global conventional conflict on the scale of World War II. The probability of such conflict seems small at best in the nuclear age. Further, in the event of an interruption in seaborne traffic, adjacent trading partners may be able to take up much of the slack on many items . . .

Where interruption of necessary imports seems a serious risk, the next issue is whether domestic capacity can be restored with reasonable dispatch. Even if an industry has closed down certain productive facilities that might be needed in wartime, it does not follow that those facilities cannot be reopened or rebuilt quickly enough to satisfy essential needs.

Finally, stockpiling during peacetime may well be a superior alternative to the protection of domestic capacity. Where the item in question is not perishable, a nation might be better off by buying up a supply of vital material at low prices in an open trading system than to burden itself over time with the high prices attendant on protectionism as a hedge against armed conflict. The funds tied up in a stockpile have some opportunity cost to be sure, but this cost can easily be smaller than the costs of excluding efficient foreign suppliers from the domestic market.<sup>96</sup>

Sykes concluded that arguments for protectionism from the national security perspective will rarely hold up to careful scrutiny.<sup>97</sup>

Finally, and to an ever more significant extent, governments adopt trade restrictive measures, or measures that have a trade restrictive effect, in pursuit of non-economic societal values such as public morals, public health, consumer safety, a clean environment and cultural identity. Trade in products or services that do not meet specific health, safety or environmental regulations or standards or that may, more generally, threaten a fundamental societal value may be prohibited or significantly limited. Many of such trade restrictive measures are not only legitimate but also necessary. Other such measures, however, are mere fronts for protectionist measures intending to shield domestic producers from import competition. Protectionism can take on very sophisticated guises.<sup>98</sup>

### Questions and Assignments 1.5

Why is it that according to most economists even the poorest countries can, at least in theory, benefit from international trade? Why do governments resort to trade restrictive measures?

<sup>96</sup> J. Jackson, W. Davey and A. Sykes, *Legal Problems of International Economic Relations*, 4th edition (Westgroup, 2002), 20–1. <sup>97</sup> *Ibid.* <sup>98</sup> See below, pp. 650–1.

### 1.2.4. Globalisation and trade to the benefit of all?

In presenting the *United Nations Millennium Report* to the UN General Assembly in April 2000, former UN Secretary General Kofi Annan spoke of addressing the inequities of globalisation as the ‘overarching challenge’ of our times. In this presentation to the General Assembly, he argued as follows:

the benefits of globalization are obvious . . . faster growth; higher living standards; and new opportunities, not only for individuals, but also for better understanding between nations, and for common action. One problem is that, at present, these opportunities are far from equally distributed. How can we say that the half of the human race, which has yet to make or receive a telephone call, let alone use a computer, is taking part in globalization? We cannot, without insulting their poverty. A second problem is that, even where the global market does reach, it is not yet underpinned, as national markets are, by rules based on shared social objectives. In the absence of such rules, globalization makes many people feel they are at the mercy of unpredictable forces.

. . . the overarching challenge of our times is to make globalization mean more than bigger markets. To make a success of this great upheaval, we must learn how to govern better, and – above all – how to govern better together. We need to make our States stronger and more effective at the national level. And we need to get them working together on global issues, all pulling their weight and all having their say.<sup>99</sup>

In the *Millennium Declaration* adopted by the UN General Assembly on 8 September 2000, the Heads of State and Government of the Member States of the United Nations solemnly declared:

We believe that the central challenge we face today is to ensure that globalization becomes a positive force for all the world’s people. For while globalization offers great opportunities, at present its benefits are very unevenly shared, while its costs are unevenly distributed. We recognize that developing countries and countries with economies in transition face special difficulties in responding to this central challenge. Thus, only through broad and sustained efforts to create a shared future, based upon our common humanity in all its diversity, can globalization be made fully inclusive and equitable. These efforts must include policies and measures, at the global level, which correspond to the needs of developing countries and economies in transition and are formulated and implemented with their effective participation.<sup>100</sup>

Three years later, at the Cancún Session of the WTO Ministerial Conference in September 2003, Kofi Annan noted, not without a certain measure of frustration:

The reality of the international trading system today does not match the rhetoric (of improving the quality of life). Instead of open markets, there are too many barriers that stunt, stifle and starve. Instead of fair competition, there are subsidies by rich countries that tilt the playing field against the poor. And instead of global rules negotiated by all, in the interest of all, and adhered to by all, there is too much closed-door decision-making, too much protection of special interests, and too many broken promises.<sup>101</sup>

In its 2002 study, *Rigged Rules and Double Standards: Trade, Globalization, and the Fight Against Poverty*, Oxfam formulated recommendations and suggestions to

<sup>99</sup> United Nations General Assembly, *UN Millennium Declaration*, Resolution adopted on 8 September 2000, para. 11. <sup>100</sup> *Ibid.*, para. 5.

<sup>101</sup> See [www.wto.mvs.com/mino3\\_webcast\\_e.htm/archives](http://www.wto.mvs.com/mino3_webcast_e.htm/archives), visited on 31 May 2004.



make economic globalisation and international trade work for the poor. According to Oxfam, international trade can realise its full potential only if rich and poor countries alike take action to *redistribute opportunities* in favour of the poor. This will require action at the national level, new forms of international cooperation and a new architecture of global governance at the WTO. With respect to action at the national level, Oxfam observed:

The challenge of extending opportunity at the national level goes beyond the narrow confines of trade policy. Inequalities in health and education services, and in the ownership of assets, are a formidable barrier to making markets work for poor people. Lacking access to land, marketing infrastructure, and financial resources, the poor are often least equipped to take advantage of market opportunities, and the most vulnerable to competition from imports.

In many countries, extensive corruption and excessive bureaucracy act as a tax on trade – and the tax falls most heavily on the poor.<sup>102</sup>

With respect to international cooperation, Oxfam noted:

International cooperation must be strengthened in a range of areas. Developing countries need development assistance if they are to integrate into world markets on more favourable terms and to extend opportunities to the poor.

Yet rich countries reduced their aid budgets by \$13 billion between 1992 and 2000. Some of the heaviest cuts fell on the poorest countries and in areas – such as agriculture – where well-targeted aid can make a difference to levels of poverty.<sup>103</sup>

With respect to a new architecture of global governance at the WTO, Oxfam stated:

The WTO is one of the youngest international institutions, but it is old before its time. Behind the facade of a ‘membership-driven’ organisation is a governance system based on a dictatorship of wealth. Rich countries have a disproportionate influence. This is partly because of a failure of representational democracy. Each WTO country may have one vote, but eleven of its members among the least-developed countries are not even represented at the WTO base in Geneva.<sup>104</sup>

Oxfam correctly stated that, just as in any national economy, economic integration in the global economy can be a source of shared prosperity and poverty reduction, or a source of increasing inequality and exclusion:

Managed well, the international trading system can lift millions out of poverty. Managed badly, it will leave whole economies even more marginalised. The same is true at a national level. Good governance can make trade work in the interests of the poor. Bad governance can make it work against them.<sup>105</sup>

According to Oxfam, international trade is at present badly managed, both at the global level and, in many countries, at the national level.<sup>106</sup>

In a reaction to this study, the European Commission took issue with Oxfam’s finding that the European Union is the most protectionist of the large trading

<sup>102</sup> Oxfam, *Rigged Rules and Double Standards: Trade, Globalization, and the Fight Against Poverty*, 2002, Summary of chapter 9, available at [www.maketrade4fair.org/en/index.php?file=03042002174753.htm&cat=3&subcat=3&select=12](http://www.maketrade4fair.org/en/index.php?file=03042002174753.htm&cat=3&subcat=3&select=12), visited on 15 June 2004.

<sup>103</sup> *Ibid.* <sup>104</sup> *Ibid.* <sup>105</sup> *Ibid.* <sup>106</sup> *Ibid.*



entities *but* fully supported Oxfam's analysis of how trade could help to fight poverty. Commenting on the report, the then EU Trade Commissioner Pascal Lamy said:

The Oxfam report is a substantive and in general well-researched contribution to the debate on the link between trade and development. I fully share the basic philosophy underlying the report: trade has the potential to lift millions out of poverty (and this is borne out by past experience, for instance in East Asia), but the benefits of trade are not automatic – a lot depends on the domestic context.<sup>107</sup>

In a speech to the G-20 Finance Ministers and Central Bank Governors in November 2001, James Wolfensohn, then President of the World Bank, made the following analysis of the challenge of economic globalisation:

In my view, with the improvements in both technology and policies that we have seen over recent decades, some form of globalization is with us to stay. But the kind of globalization is not yet certain: it can be either a *globalization of development and poverty reduction* – such as we have begun to see in recent decades, although this trend still cannot be taken for granted – or a *globalization of conflict, poverty, disease, and inequality*. What can we do to tip the scales decisively toward the right kind of globalization?<sup>108</sup>

To ensure that economic globalisation and trade liberalisation contribute to economic development, equity and the well-being of all people, Wolfensohn advocated the following four-point agenda for action: better governance, reduction of trade barriers, more development aid and better international cooperation:

First, developing countries must continue the move toward *better policies, investment climate, and governance*. Despite progress in macroeconomic management and openness, there remain many domestic barriers to integration. Many countries have fallen short in creating an investment climate for productivity, growth, entrepreneurship, and jobs. These domestic barriers include inadequate transport infrastructure, poor governance, bureaucratic harassment of small businesses, a lack of electric power, an unskilled workforce . . . And countries also need to make possible the participation of poor people in growth, through support for targeted education, health, social protection, and their involvement in key decisions that shape their lives. Poor people need much greater voice.

Second, all countries – developed and developing – must *reduce trade barriers* and give developing countries a better chance in world markets . . . Rich countries must increase market access for the exports of developing countries, through both multilateral negotiations and unilateral action, to increase the payoffs to developing-country policy and institutional reforms. Dismantling trade barriers, as our recent publication *Global Economic Prospects: Making Trade Work for the World's Poor* shows, could increase income in developing countries by an estimated \$1.5 trillion over a decade and increase GDP growth in the developing countries by 0.5 per cent per year over the long run. This in turn would lift an additional 300 million people out of poverty by 2015 (even beyond the 600 million that will escape poverty with the growth we are currently anticipating) . . .

Third, developed countries must *increase development aid*, but allocate it better and cut down the burden its implementation can impose . . . The evidence from the Bank's research is that well-directed aid, combined with strong reform efforts, can greatly reduce poverty. If

<sup>107</sup> European Commission, Memorandum, Brussels, 22 April 2002, available at [www.europa.eu.int](http://www.europa.eu.int), visited on 15 July 2004.

<sup>108</sup> 'Responding to the Challenges of Globalization', Remarks to the G-20 Finance Ministers and Central Bank Governors by James D. Wolfensohn, President, World Bank Group, Ottawa, 17 November 2001, available at [www.worldbank.org](http://www.worldbank.org), visited on 15 November 2002.

we are serious about ensuring a beneficial globalization and meeting multilateral development goals we have all signed up to, we must double ODA [overseas development aid] from its current level of about \$50 billion a year.

Fourth, we must *act as a global community* where it really matters. Effective globalization requires institutions of global governance, and multilateral action to confront global problems and provide global public goods. This means confronting terrorism, internationalized crime, and money laundering, as we are doing in response to September 11th. But it also means that as a community, we need to address longer-term needs, by: combating communicable diseases like AIDS and malaria; building an equitable global trading system; promoting financial stability to prevent deep and sudden crises; and safeguarding the natural resources and environment on which so many poor people depend for their livelihoods. As we do all this, we must bring poor countries into the decision-making of this global community.<sup>109</sup>

According to Wolfensohn, if the international community can act on these four priorities, it will have created the conditions to achieve true global integration and to reach the millennium goals of halving extreme poverty by 2015.<sup>110</sup>

In addressing the question of how to ensure that economic globalisation and international trade benefits all, WTO Director-General Pascal Lamy noted in 2007 that this question has two sides:

A first one is how to ensure trade benefits are shared more fairly among nations. The second side is how to ensure a better distribution of the benefits stemming from trade within a nation.

On the first side, I believe two elements are fundamental: fairer multilateral trade rules and building of trade capacity in developing countries. One primary objective of the ongoing WTO negotiations under the Doha Development Agenda is precisely to address the remaining imbalances in the WTO rules against developing countries, whether in agriculture or in areas such as textiles or footwear . . . But negotiating a fairer playing field, difficult as it is, will not be enough. New trade opportunities do not automatically convert into growth and development. The international community also has a responsibility to make sure poorer countries have the capacity to trade and make full use of the market access opportunities provided to them, through more and better focused Aid for Trade . . .

The second side, as I said, is how to ensure a better distribution of the benefits stemming from trade within a nation. Trade opening can and does translate into greater growth and poverty alleviation, but this is neither automatic [nor] immediate. Trade opening must be accompanied by a solid domestic agenda to spur on growth and cushion adjustment costs. Appropriate tax policies, competition policy, investment in quality education, social safety nets and innovation fostering healthy environments must all be part of the mix needed for trade to translate into real benefits for the people. In this respect, trade policy cannot be isolated from domestic macroeconomic, social or structural policies. The same trade policy will result in different outcomes depending on the quality of economic policies, and this is true across the board, whether you look at the US, Europe, Japan, or at Vietnam, Cambodia, Kenya or Paraguay.<sup>111</sup>

In remarks to the UNCTAD Trade and Development Board meeting in September 2006, Lamy stated:

Let me start by saying that I share the views expressed in the Report about the contribution that trade can make to development and to poverty alleviation. Trade is today a

<sup>109</sup> *Ibid.*      <sup>110</sup> See *ibid.*

<sup>111</sup> P. Lamy, 'Trends and Issues Facing Global Trade', Speech delivered in Kuala Lumpur, Malaysia on 17 August 2007, available at [www.wto.org/english/news\\_e/sppl65\\_e/sppl65\\_e.htm](http://www.wto.org/english/news_e/sppl65_e/sppl65_e.htm), visited on 29 October 2007.

crucial ingredient in a policy mix which must nevertheless contain many other ingredients to achieve successfully this objective. This means, no blind adherence to free trade. But this also means no blind adherence to governments doing pretty much anything and certainly no blind adherence protectionism. If trade opening is not sufficient, it remains a necessary ingredient. This is the core of what I have called the '*Geneva Consensus*'. [Emphasis added]<sup>112</sup>

It must be noted, however, that not all share the belief in this 'Geneva Consensus' and the 'conditional optimism' of Oxfam, the World Bank and the WTO. In a reaction to what some call the rhetoric of 'globalisation as opportunity', the President of Tanzania, Benjamin Mkapa, said in a statement made at the 2000 Annual Meeting of the World Economic Forum in Davos:

Globalisation can deliver, just as Tanzania can play in the World Cup and win it.<sup>113</sup>

It is clear that economic openness is a necessary but not a sufficient condition for economic development and prosperity. The simple spread of markets will not eliminate poverty. A global economy and more international trade will not automatically lead to rising prosperity for all countries and for all people. Good governance is undoubtedly as important as international trade. Without functioning State institutions and without a legal system that protects fundamental rights and property and enforces contracts, globalisation will not bring prosperity but, on the contrary, poverty, corruption and exploitation.

Peter Sutherland, former GATT and WTO Director-General and EU Commissioner and currently Chairman of BP Amoco and Goldman Sachs International, emphasised that more than free markets is needed to eradicate poverty and inequality:

There are those who oppose redistribution policies in principle, whether in the domestic or the international context. This is wrong. It is morally wrong, it is pragmatically wrong, and we ought not be ashamed to say so. I have been personally and deeply committed to promoting the market system through my entire career. Yet it is quite obvious to me that the market will never provide all of the answers to the problems of poverty and inequality. The fact is that there are those who will not be able to develop their economies simply because market access has been provided. I do not believe that we in the global community will adequately live up to our responsibility if we have done no more than provide the poorest people and the poorest countries with an opportunity to succeed. We must also provide them with a foundation from which they have a reasonable chance of seizing that opportunity – decent health care, primary education, basic infrastructure.<sup>114</sup>

It is worth noting that there is also a cultural dimension to the issue of globalisation which may make it harder for certain countries and people to make use

<sup>112</sup> P. Lamy, Opening Remarks, 53rd Session of the UNCTAD Trade and Development Board, 27 September 2006, available at [www.wto.org/english/news\\_e/sppl\\_e/sppl40\\_e.htm](http://www.wto.org/english/news_e/sppl_e/sppl40_e.htm), visited on 20 October 2007. On the 'Geneva Consensus', see also P. Lamy, 'Humanising Globalization', Speech delivered in Santiago de Chile, Chile on 30 January 2006, available at [www.wto.org/english/news\\_e/sppl\\_e/sppl16\\_e.htm](http://www.wto.org/english/news_e/sppl_e/sppl16_e.htm), visited on 25 October 2007; and P. Lamy, 'Towards Global Governance?', Master of Public Affairs inaugural lecture at the Institut d'Études Politiques de Paris on 21 October 2005, available at [www.wto.org/english/news\\_e/sppl\\_e/sppl12\\_e.htm](http://www.wto.org/english/news_e/sppl_e/sppl12_e.htm), visited on 25 October 2007.

<sup>113</sup> As reported by J. Harris, 'Globalisation and World's Poor', *Economic and Political Weekly*, 9 June 2001, 2034.

<sup>114</sup> P. Sutherland, 'Beyond the Market, a Different Kind of Equity', *International Herald Tribune*, 20 February 1997.

of the opportunity globalisation, and international trade, offers for economic development:

Much of Latin America, for example, abandoned trade protectionism and favoritism for local companies. Between 1985 and 1996, average tariffs fell from 50 per cent to 10 per cent. The results have been modest. What explains the contrasts? Perhaps culture. The gospel of capitalism presumes that human nature is constant. Given the proper incentives – the ability to profit from hard work and risk taking – people will strive. Maybe not. In a recent book, *Culture Matters: How Values Shape Human Progress*, scholars from the United States, Africa and Latin America argue that strong social and moral values predispose some peoples for and against economic growth. As a result of history, tradition and religion, some societies cannot easily adopt capitalist attitudes and institutions. Even when they try, they often fail because it is so unnatural. ‘Competition is central to the success of an enterprise, the politician, the intellectual and the professional’, writes Mariano Grondona, an Argentine political scientist and columnist. ‘In resistant societies, competition is condemned as a form of aggression.’ Daniel Etounga-Manguelle of Cameroon contends that Africa suffers from a reverence for its history. ‘In traditional African society, which exalts the glorious past of ancestors through tales and fables, nothing is done to prepare for the future’, he writes. Once stated, culture’s impact seems obvious.<sup>115</sup>

However, culture, though deep, is not immutable. Culture is changed by experience. There are multiple examples of cultures changing over time. One such example, India, has shifted since the late 1980s from protectionism and State control towards pro-market policies, thereby raising annual economic growth to more than 9.4 per cent in 2006.<sup>116</sup>

Reflecting on the ‘acceptability’ of economic globalisation and international trade in particular in developed countries, Dani Rodrik concluded his book, *Has Globalization Gone Too Far?*, as follows:

The broader challenge for the 21st century is to engineer a new balance between market and society, one that will continue to unleash the creative energies of private entrepreneurship without eroding the social basis of cooperation. The tensions between globalization and social cohesion are real, and they are unlikely to disappear of their own accord.<sup>117</sup>

The General Secretary of the International Confederation of Free Trade Unions wrote in December 2000:

[G]lobalization is neither entirely beneficial nor entirely harmful. It is not an unstoppable force of nature, but is shaped by those who set the rules . . . The labor movement’s position is simply that the rules governing globalization should protect the interests of the poor and not just the rich, and that the benefits of increased trade and increased global output should be shared by all.<sup>118</sup>

Over the past ten years, the UN High Commissioner for Human Rights has argued repeatedly that fair and equitable economic globalisation and trade liberalisation can only be achieved by adopting a *human rights approach* to both processes. The UN Committee on Economic, Social and Cultural Rights adopted

<sup>115</sup> R. Samuelson, ‘Persistent Poverty Defies the Wisdom on Globalization’, *International Herald Tribune*, 21 September 2000. <sup>116</sup> See above, p. 17.

<sup>117</sup> D. Rodrik, *Has Globalization Gone Too Far?* (Institute for International Economics, 1997), 85.

<sup>118</sup> B. Jordan, ‘Yes to Globalization, But Protect the Poor’, *International Herald Tribune*, 21 December 2000.

in 1999 a resolution stating that ‘trade liberalization must be understood as a means, not an end’ and that:

The end which trade liberalization should serve is the objective of human well-being to which the international human rights instruments give legal expression. In this regard the Committee wishes to remind WTO Members of the central and fundamental nature of human rights obligations.<sup>119</sup>

Joseph Stiglitz described, in *Globalization and Its Discontents*, the experience of the United States during the nineteenth century with the formation of its national economy and the regulating and supporting role played by the federal government in that process.<sup>120</sup> According to Stiglitz, the experience of the United States makes a good parallel for today’s globalisation. The contrast helps illustrate the successes of the past and the failures of the present:

Today, with the continuing decline in transportation and communication costs, and the reduction of man-made barriers to the flow of goods, services, and capital (though there remain serious barriers to the free flow of labor), we have a process of ‘globalization’ analogous to the earlier processes in which national economies were formed. Unfortunately, we have no world government, accountable to the people in every country, to oversee the globalization process in a fashion comparable to the way national governments guided the nationalization process. Instead, we have a system that might be called *global governance without global government*, one in which a few institutions – the World Bank, the IMF, the WTO – and a few players – the finance, commerce, and trade ministries, closely linked to certain financial and commercial interests – dominate the scene, but in which those affected by their decisions are left almost voiceless.<sup>121</sup>

Criticising the current system of what he referred to as ‘global governance without global government’, Stiglitz called for a reform of the rules governing the international economic order. According to Stiglitz:

Globalization can be reshaped, and when it is, when it is properly, fairly run, with all countries having a voice in policies affecting them, there is a possibility that it will help to create a new global economy in which growth is not only more sustainable and less volatile but the fruits of this growth are more equitably shared.<sup>122</sup>

Muhammad Yunus noted in his Nobel Peace Prize Lecture in December 2006:

I support globalization and believe it can bring more benefits to the poor than its alternative. But it must be the right kind of globalization. To me, globalization is like a hundred-lane highway criss-crossing the world. If it is a free-for-all highway, its lanes will be taken over by the giant trucks from powerful economies. Bangladeshi rickshaw will be thrown off the highway. In order to have a win-win globalization we must have traffic rules, traffic police, and traffic authority for this global highway. Rule of “strongest takes it all” must be replaced by rules that ensure that the poorest have a place and piece of the action, without being elbowed out by the strong.<sup>123</sup>

<sup>119</sup> United Nations Economic and Social Council, ‘Statement of the UN Committee on Economic, Social and Cultural Rights to the Third Ministerial Conference of the World Trade Organization (Seattle, 30 November to 3 December 1999)’, adopted at the 47th meeting, twenty-first session, 26 November 1999, E/C.12/1999/9, 2. <sup>120</sup> J. Stiglitz, *Globalization and Its Discontents* (Penguin, 2002), 21.

<sup>121</sup> *Ibid.*, 21–2. <sup>122</sup> *Ibid.*, 22.

<sup>123</sup> Muhammad Yunus, Nobel Lecture, Oslo, 10 December 2006, available at [http://nobelprize.org/nobel\\_prizes/peace/laureates/2006/yunus-lecture-en.html](http://nobelprize.org/nobel_prizes/peace/laureates/2006/yunus-lecture-en.html), visited on 27 October 2007.

### Questions and Assignments 1.6

How can economic globalisation and international trade be made 'a positive force for all the world's people' as mandated in the *UN Millennium Declaration*? What is referred to as the 'Geneva Consensus'? What does Joseph Stiglitz mean when he refers to 'global governance without global government'? What is needed to ensure that there is room for a Bangladeshi rickshaw on Muhammad Yunus' hundred-lane highway?

## 1.3. INTERNATIONAL TRADE AND THE LAW OF THE WTO

As discussed above, economic globalisation and international trade need to be properly managed and regulated if they are to be of benefit to all humankind. This section discusses:

- the need for and existence of international rules for international trade; and
- the basic rules and disciplines of WTO law.

### 1.3.1. International rules for international trade

#### 1.3.1.1. Need for international rules

Peter Sutherland wrote in 1997:

The greatest economic challenge facing the world is the *need to create an international system* that not only maximizes global growth but also achieves a greater measure of equity, a system that both integrates emerging powers and assists currently marginalized countries in their efforts to participate in worldwide economic expansion . . . The most important means available to secure peace and prosperity into the future is to develop effective multilateral approaches and institutions.<sup>124</sup>

[Emphasis added]

These multilateral approaches and institutions to which Sutherland referred embrace many structures and take many forms but, as John Jackson noted:

it is very clear that law and legal norms play the most important part of the institutions which are essential to make markets work. The notion that 'rule of law' (ambiguous as that phrase is) or a *rule-based or rule-oriented system* of human institutions is essential to a beneficial operation of markets, is a constantly recurring theme in many writings.<sup>125</sup>

[Emphasis added]

Ronald Coase wrote:

It is evident that, for their operation, markets . . . require the establishment of legal rules governing the rights and duties of those carrying out transactions . . . *To realize all the gains of trade* . . . there has to be a legal system and political order.<sup>126</sup>

[Emphasis added]

<sup>124</sup> P. Sutherland, 'Beyond the Market, a Different Kind of Equity', *International Herald Tribune*, 20 February 1997.

<sup>125</sup> J. Jackson, 'Global Economics and International Economic Law', *Journal of International Economic Law*, 1998, 5 (reproduced by permission of Oxford University Press).

<sup>126</sup> R. Coase, *The Firm, the Market and the Law* (reprint of 1960 article), chapter 5, as quoted by Jackson, *ibid.*, 4.

But what exactly is the role of legal rules and, in particular, international legal rules in international trade? How do international trade rules allow countries to realise the gains of international trade?

There are basically four related reasons why there is a need for international trade rules. First, countries must be restrained from adopting trade-restrictive measures both in their own interest and in that of the world economy. International trade rules *restrain* countries from taking trade-restrictive measures. As noted above, national policy-makers may come under considerable pressure from influential interest groups to adopt trade-restrictive measures in order to protect domestic industries from import competition. Such measures may benefit the specific, short-term interests of the groups advocating them but they very seldom benefit the general economic interests of the country adopting them.<sup>127</sup> As Ernst-Ulrich Petersmann observed:

Governments know very well . . . that by 'tying their hands to the mast' (like Ulysses when he approached the island of the Sirenes), reciprocal international pre-commitments help them to resist the siren-like temptations from 'rent-seeking' interest groups at home.<sup>128</sup>

Countries also realise that, if they take trade-restrictive measures, other countries will do so too. This may lead to an escalation of trade-restrictive measures, a disastrous move for international trade and for global economic welfare. International trade rules help to avoid such escalation.

A second and closely related reason why international trade rules are necessary is the need of traders and investors for a degree of *security and predictability*. Traders and investors operating, or intending to operate, in a country that is bound by international legal rules will be able to predict better how that country will act in the future on matters affecting their operations in that country. The predictability and security resulting from international trade rules will encourage investments and trade and will thus contribute to global economic welfare. As John Jackson wrote:

At least in the context of economic behaviour . . . and particularly when that behaviour is set in circumstances of decentralized decision-making, as in a market economy, rules can have important operational functions. They may provide the only predictability or stability to a potential investment or trade-development situation. Without such predictability or stability, trade or investment flows might be even more risky and therefore more inhibited than otherwise . . . To put it another way, the policies which tend to reduce some risks, lower the 'risk premium' required by entrepreneurs to enter into international transactions. This should result in a general increase in the efficiency of various economic activities, contributing to greater welfare for everyone.<sup>129</sup>

A third reason why international trade rules are necessary is that national governments alone simply cannot *cope with the challenges presented by economic*

<sup>127</sup> See above, p. 21. On the optimal tariff argument and the strategic trade policy argument, see above, pp. 22–3.

<sup>128</sup> E. U. Petersmann, *The GATT/WTO Dispute Settlement System: International Law, International Organizations and Dispute Settlement* (Kluwer Law International, 1997), 36–7.

<sup>129</sup> J. Jackson, 'Global Economics and International Economic Law', *Journal of International Economic Law*, 1998, 5–6.



*globalisation*. The protection of important societal values such as public health, a clean environment, consumer safety, cultural identity and minimum labour standards is, as a result of the greatly increased levels of trade in goods and services, no longer a purely national matter but ever more a matter with significant international ramifications. Attempts to ensure the protection of these values at the national level alone are doomed to be ineffective and futile. Further, domestic regulatory measures regarding, for example, product safety, health, environmental protection and labour conditions may constitute important barriers to trade. These measures are often not directly or expressly related to the regulation of trade but the fact that they differ from country to country acts as a significant constraint on trade. International trade rules serve to ensure that countries only maintain national regulatory measures that are *necessary* for the protection of the key societal values referred to above.<sup>130</sup> International trade rules may also introduce a degree of harmonisation of domestic regulatory measures and thus promote an effective, international protection of these societal values.<sup>131</sup>

A fourth and final reason why international trade rules are necessary is the need to achieve a *greater measure of equity* in international economic relations. As Father Lacordaire had stated in his renowned 1835 sermons at the Notre Dame in Paris:

Entre le faible et le fort, entre le riche et le pauvre . . . c'est la liberté qui opprime et la loi qui affranchit.<sup>132</sup>

Without international trade rules, binding and enforceable on rich as well as poor countries, and rules recognising the special needs of developing countries, many of these countries would not be able to integrate fully in the world trading system and derive an equitable share of the gains of international trade.

However, for international legal rules to play these multiple roles, such rules have, of course, to be observed. It is clear that international trade rules are not always adhered to. Yet, while most attention, of both the media and academia, is inevitably paid to instances of breach, it should be stressed that international trade rules are generally well observed. Countries realise that they cannot expect other countries to observe the rules if they do not do so themselves. The desire to be able to depend on other countries' compliance with the rules leads many countries to observe the rules even though this might be politically inconvenient in a given situation.<sup>133</sup>

All countries and their people benefit from the existence of rules on international trade making the trading environment more predictable and stable.

<sup>130</sup> See below, pp. 621–9.      <sup>131</sup> See below, p. 616.

<sup>132</sup> Translation: 'Between the weak and the powerful, between the rich and the poor . . . it is freedom that oppresses and the law that sets free.' Abbé Jean-Baptiste Lacordaire (1802–61) was the greatest French pulpit orator of the nineteenth century.

<sup>133</sup> See L. Henkin, *How Nations Behave*, 2nd edition (1979); R. Fisher, *Improving Compliance with International Law* (1981); and A. Chayes, *The New Sovereignty: Compliance with International Regulatory Agreements* (1995), as referred to in J. Jackson, 'Global Economics and International Economic Law', *Journal of International Economic Law*, 1998, 5.



However, provided the rules take into account their specific interests and needs, developing countries, with generally limited economic, political and military power, should benefit even more from the existence of rules on international trade. The weaker countries are likely to suffer most where the law of the jungle reigns. They are more likely to thrive in a *rules-based*, rather than a power-based, international trading system.

While developing countries stand to benefit most from rules and disciplines on international trade, some developing countries frequently argue in favour of freedom from such rules and disciplines to allow them to pursue their domestic policy objectives. As reported in *BRIDGES Weekly Trade News Digest*, at the 2006 Annual Session of the Trade and Development Board of UNCTAD:

ministers and top trade diplomats returned to the so-called ‘policy space’ debate. This hinges on the extent to which governments should have to constrain their ability to pursue particular policies by embracing international economic rules. The issue has been a contentious one, with several developing countries calling for more space to pursue development policy, while industrialised countries peddle the merits of tying governments’ hands in order to avoid policy missteps. Nevertheless, member states managed to agree on language referring to the importance of policy space to developing countries. The report adopted at the end of the week of discussions stated that ‘It is for each government to evaluate the trade-off between the benefits of accepting international rules and commitments and the constraints posed by the loss of policy space. It is particularly important for developing countries, bearing in mind development goals and objectives, that all countries take into account the need for appropriate balance between national policy space and international disciplines and commitments.’<sup>134</sup>

At the start of this Session, WTO Director-General Pascal Lamy had stated in his opening remarks:

An important part of this year’s report is devoted to the issues of policy autonomy or policy space. The basic argument which UNCTAD is making is that international commitments in the finance or trade fields are preventing developing countries from realizing their true development potential, in that governments are prevented from intervening in the economy in ways that are essential to progress. When using this argument, I believe it is important to make the case not just for policy space but for ‘good policy’ space. We need to make a convincing case as to why a particular policy is needed, basing ourselves on the facts.<sup>135</sup>

### Questions and Assignments 1.7

Is there a need for international rules on trade? Who benefits from these rules and why? Do international rules on trade necessarily conflict with the ‘policy space’ that many governments of developing countries claim?

<sup>134</sup> ‘UNCTAD governing body highlights need for “policy space”’, *BRIDGES Weekly Trade News Digest*, 18 October 2006.

<sup>135</sup> P. Lamy, Opening Remarks, 53rd Session of the UNCTAD Trade and Development Board, 27 September 2006, available at [www.wto.org/english/news\\_e/sppl\\_e/sppl40\\_e.htm](http://www.wto.org/english/news_e/sppl_e/sppl40_e.htm), visited on 20 October 2007.

### 1.3.1.2. *International economic law and WTO law*

The legal rules, discussed above, governing trade relations between countries are part of international economic law. International economic law is a very broad field of international law. With regard to the concept of ‘international economic law’, John Jackson noted that:

[it] is not by any means a new phenomenon although the phrase may be considered relatively new. International law has always had considerable ‘economic content’, as manifested by international economic institutions and by the international law jurisprudence throughout the centuries devoted to various economic subjects including trade, investment, commerce, and navigation (FCN treaties). In addition, activities of the League of Nations, as well as, more currently, the United Nations, have had a very substantial economic institutional dimension.<sup>136</sup>

Jackson once suggested that 90 per cent of international law work relates in fact to international economic law in some form or another. He also observed that international economic law does not enjoy as much glamour or media attention as work on armed conflicts and human rights do.<sup>137</sup>

International economic law can be defined, broadly, as covering all those international rules pertaining to economic transactions and relations, as well as those pertaining to governmental regulation of economic matters. As such, international economic law includes international rules on trade in goods and services, economic development, intellectual property rights, foreign direct investment, international finance and monetary matters, commodities, food, health, transport, communications, natural resources, private commercial transactions, nuclear energy, etc. International rules on international trade in goods and services, i.e. international trade law, constitute the ‘hard core’ of international economic law.

International trade law consists of, on the one hand, numerous bilateral or regional trade agreements and, on the other hand, multilateral trade agreements. Examples of bilateral and regional trade agreements are manifold. The *North American Free Trade Agreement* (NAFTA) and the *MERCOSUR Agreement* are typical examples of regional trade agreements. The *Trade Agreement between the United States and Israel* or the *Agreement on Trade in Wine between the European Community and Australia* are examples of bilateral trade agreements. The number of multilateral trade agreements is more limited. This group includes, for example, the 1983 *International Convention on the Harmonised Commodity Description and Coding System* (the ‘Brussels Convention’) and the 1973 *International Convention on the Simplification and Harmonisation of Customs Procedures*, as revised in 2000 (the ‘Kyoto Convention’). The most important and broadest of all multilateral trade agreements is the *Marrakesh Agreement Establishing the World Trade Organization*,

<sup>136</sup> J. Jackson, ‘International Economic Law: Complexity and Puzzles’, *Journal of International Economic Law*, 2007, 3.

<sup>137</sup> J. Jackson, ‘International Economic Law: Reflections on the “Boilerroom” of International Relations’, *American University Journal of International Law and Policy*, 1995, 596.

concluded on 15 April 1994. It is the law of this Agreement – the law of the WTO – which is the subject-matter of this book.

### Questions and Assignments 1.8

What is international economic law and what does it cover? How does WTO law relate to international economic law?

## 1.3.2. Basic rules and principles of WTO law

The law of the WTO is a complex set of rules dealing with trade in goods and services and the protection of intellectual property rights. WTO law addresses a broad spectrum of issues, ranging from tariffs, import quotas and customs formalities to compulsory licensing, food safety regulations and national security measures. However, five groups of basic rules and principles can be distinguished:

- the principles of non-discrimination;
- the rules on market access;
- the rules on unfair trade;
- the rules on conflicts between trade liberalisation and other societal values and interests; including the rules on special and differential treatment for developing countries; and
- the rules promoting harmonisation of national regulation in specific fields.

In addition, WTO law contains institutional and procedural rules, including those relating to decision-making and dispute settlement.

These substantive and procedural rules and principles of WTO law make up what is commonly referred to as the *multilateral trading system*. Referring to this system, Peter Sutherland and others wrote in 2001:

The multilateral trading system, with the World Trade Organization (WTO) at its centre, is the most important tool of global economic management and development we possess.<sup>138</sup>

Martin Wolf of the *Financial Times* noted in 2001:

The multilateral trading system at the beginning of the twenty-first century is the most remarkable achievement in institutionalized global economic cooperation that there has ever been.<sup>139</sup>

*The Economist* noted the following in June 2005 with regard to the relevance of the rules of the multilateral trading system:

<sup>138</sup> P. Sutherland, J. Sewell and D. Weiner, 'Challenges Facing the WTO and Policies to Address Global Governance', in G. Sampson (ed.), *The Role of the World Trade Organization in Global Governance* (United Nations University Press, 2001), 81.

<sup>139</sup> M. Wolf, 'What the World Needs from the Multilateral Trading System', in G. Sampson (ed.), *The Role of the World Trade Organization in Global Governance* (United Nations University Press, 2001), 182.

Wherever you look, trade tensions are on the rise. America and the European Union are squealing about surging textile imports from China; both are slapping on 'safeguard' quotas to stem the flow. China is furious and has retaliated by scrapping voluntary export taxes on its textile exporters. Meanwhile Americans and Europeans are, once again, spitting at each other about subsidies to Boeing and Airbus. Both sides this week formally filed complaints at the World Trade Organization. Set against an increasingly protectionist backdrop – whether in America's Congress or among France's *non-voters* – this rash of disputes might suggest an ominous outlook for the global trading system.

There is one bright spot, however. The recent tensions show just how integral the rules of the global trading system, and the WTO that adjudicates those rules, have become to the way countries, rich and poor alike, think about trade policy. The safeguard quotas that America and Europe are using to staunch Chinese textiles may be of dubious economic merit, but they were agreed under the terms of China's entry into the WTO and therefore have limits (they must go by 2008). China can, and no doubt will, file a complaint if it reckons their application is unfair. Even on the aircraft dispute, the shift to an independent arbiter may be more constructive than endless acrimonious bilateral negotiations. And in America, the global rules are proving an important bulwark against protectionist backsliding. The Bush administration has been able to deter some of Congress's more extreme China-bashing plans by pointing out that they are illegal under world trade rules.<sup>140</sup>

The following sections of this chapter briefly review these basic rules and principles constituting the multilateral trading system. They will be discussed in greater detail in subsequent chapters of this book.

### 1.3.2.1. Principles of non-discrimination

There are two principles of non-discrimination in WTO law: the most-favoured-nation (MFN) treatment obligation and the national treatment obligation.

The *MFN treatment obligation* requires a WTO Member that grants certain favourable treatment to another country to grant that same favourable treatment to all other WTO Members. A WTO Member is not allowed to discriminate *between* its trading partners by, for example, giving the products imported from some countries more favourable treatment with respect to market access than the treatment it accords to the products of other Members.<sup>141</sup> In spite of many exceptions and deviations from this obligation, the MFN treatment obligation is the single most important rule in WTO law. Without this rule the multilateral trading system could and would not exist. Chapter 4 examines in detail this rule as it applies to trade in goods and trade in services.<sup>142</sup>

The *national treatment obligation* requires a WTO Member to treat foreign products, services and service suppliers no less favourably than it treats 'like' domestic products, services and service suppliers. Where the national treatment obligation applies, foreign products, for example, should, once they have crossed the border and entered the domestic market, not be subject to less favourable taxation or regulation than 'like' domestic products. Pursuant to the national treatment obligation, a WTO Member is not allowed to discriminate *against* foreign products, services and service suppliers. The national treatment obligation is an

<sup>140</sup> 'The Key to Trade and Aid', *The Economist*, 2 June 2005.

<sup>141</sup> See Article I of the GATT 1994 and Article II of the GATS.

<sup>142</sup> See below, pp. 322–43.

important rule in WTO law which has given rise to many trade disputes. For trade in goods, the national treatment obligation has *general* application to all trade.<sup>143</sup> By contrast, for trade in services, the national treatment obligation does not have such general application. It applies only to the extent a WTO Member has explicitly committed itself to grant 'national treatment' in respect of specific service sectors.<sup>144</sup> Such commitments to give 'national treatment' are made in a Member's Schedule of Specific Commitments on Services. Chapter 4 of this book discusses in detail the national treatment obligation as it applies to trade in goods and services.<sup>145</sup>

### 1.3.2.2. Rules on market access

WTO law contains four groups of rules regarding market access:

- rules on *customs duties* (i.e. tariffs);
- rules on *other duties and financial charges*;
- rules on *quantitative restrictions*; and
- rules on *other 'non-tariff barriers'*, such as rules on transparency of trade regulations; customs formalities; and government procurement practices.

Under WTO law, the imposition of customs duties is not prohibited and, in fact, WTO Members impose customs duties on many products. However, WTO law calls upon WTO Members to negotiate mutually beneficial reductions of customs duties.<sup>146</sup> These negotiations result in tariff concessions or bindings, set out in a Member's Schedule of Concessions. On products for which a tariff concession or binding exists, the customs duties imposed may no longer exceed the maximum level of duty agreed to.<sup>147</sup> Chapter 5 examines the rules applicable to customs duties.<sup>148</sup> It also discusses the rules on other duties and financial charges.<sup>149</sup>

While customs duties are, in principle, not prohibited, quantitative restrictions on trade in goods are, as a general rule, forbidden.<sup>150</sup> Unless one of many exceptions applies, WTO Members are not allowed to ban the importation or exportation of goods or to subject them to quotas. With respect to trade in services, quantitative restrictions are, in principle, prohibited in service sectors for which specific market-access commitments have been undertaken.<sup>151</sup> In those sectors, quantitative restrictions can only be imposed if such restrictions have been inscribed in a Member's Schedule of Specific Commitments. Chapter 5 examines the rules applicable to quantitative restrictions on trade in goods and services.<sup>152</sup>

Among 'other non-tariff barriers', the lack of transparency of national trade regulations definitely stands out as a major barrier to international trade. Uncertainty and confusion regarding the trade rules applicable in other countries

<sup>143</sup> See Article III of the GATT 1994. <sup>144</sup> See Article XVII of the GATS. <sup>145</sup> See below, pp. 344–95.

<sup>146</sup> See Article XXVIII *bis* of the GATT 1994. <sup>147</sup> See Article II of the GATT 1994.

<sup>148</sup> See below, pp. 403–38. <sup>149</sup> See below, pp. 438–44. <sup>150</sup> See Article XI of the GATT 1994.

<sup>151</sup> Article XVI of the GATS. In fact, the prohibition of Article XVI of the GATS applies only to 'market access barriers' as defined in Article XVI:2. See below, pp. 477–81. <sup>152</sup> See below, pp. 444–93.

has a chilling effect on trade. Likewise, the arbitrary application of these rules also discourages traders and hampers trade. Transparency and the fair application of trade regulations are therefore part of the basic rules on market access examined in Chapter 5.<sup>153</sup> Non-tariff barriers to trade, such as customs formalities and practices of government procurement, are, for many products and in many countries, more important barriers to trade than customs duties or quantitative restrictions. The rules on many of these non-tariff barriers are examined in chapter 5.<sup>154</sup>

### 1.3.2.3. *Rules on unfair trade*

WTO law, at present, does not provide for general rules on unfair trade practices, but it does have a number of detailed rules that relate to specific forms of 'unfair' trade. These rules deal with dumping and subsidised trade.

Dumping, i.e. bringing a product onto the market of another country at a price less than the normal value of that product, is condemned but not prohibited in WTO law. However, when the dumping causes or threatens to cause material injury to the domestic industry of a Member producing a 'like' product, WTO law allows that Member to impose anti-dumping duties on the dumped products in order to offset the dumping.<sup>155</sup> The rules on the imposition of these anti-dumping duties are examined in chapter 6.

Subsidies, i.e. financial contributions by governments or public bodies that confer a benefit, are subject to an intricate set of rules.<sup>156</sup> Some subsidies, such as export subsidies, are, as a rule, prohibited. Other subsidies are not prohibited but, when they cause adverse effects to the interests of other Members, the subsidising Member should withdraw the subsidy or take appropriate steps to remove the adverse effects. If the subsidising Member fails to do so, countermeasures commensurate with the degree and nature of the adverse effect may be authorised.<sup>157</sup> If a prohibited or other subsidy causes or threatens to cause material injury to the domestic industry of a Member producing a 'like' product, that Member is authorised to impose countervailing duties on the subsidised products to offset the subsidisation. Subsidies relating to agricultural products are subject to different (more lenient) rules.<sup>158</sup> The rules applicable to subsidies and countervailing duties are examined in chapter 6.

### 1.3.2.4. *Trade liberalisation versus other societal values and interests*

Apart from the basic rules and principles referred to above, WTO law also provides for rules that address the conflict between trade liberalisation and other

<sup>153</sup> See below, pp. 460–70.

<sup>154</sup> See below, pp. 470–6. Technical barriers to trade and the lack of protection of intellectual property rights can also be seen as forms of 'other non-tariff barriers', but since the rules on these barriers are quite specific in nature, they are discussed separately in chapter 8 of this book. See below, pp. 741–884.

<sup>155</sup> See Article VI of the GATT 1994 and the *Anti-Dumping Agreement*.

<sup>156</sup> See Articles VI and XVI of the GATT 1994 and the *Agreement on Subsidies and Countervailing Measures* (the 'SCM Agreement'). <sup>157</sup> See Article 7.9 of the *SCM Agreement*.

<sup>158</sup> Articles 6–11 of the *Agreement on Agriculture*.

societal values and interests. These rules, which are commonly referred to as 'exceptions', allow WTO Members to deviate – under specific conditions – from basic WTO rules and disciplines in order to take account of economic and non-economic values and interests that compete or conflict with free trade. The *non-economic* values and interests include the protection of the environment, public health, public morals, national treasures and national security. The relevant rules can be found in, for example, Articles XX and XXI of the GATT 1994 and Articles XIV and XIV *bis* of the GATS. The *economic* interests include the protection of a domestic industry from serious injury inflicted by an unexpected and sharp surge in imports, the safeguarding of the balance of payments and the pursuit of regional economic integration. The relevant rules can be found in, for example, Articles XII, XIX and XXIV of the GATT 1994, Articles V, X and XII of the GATS and the *Agreement on Safeguards*. The WTO rules allowing Members to take into account economic or non-economic values and interests that may conflict with free trade are examined in detail in chapter 7.<sup>159</sup>

Recognising the need for positive efforts designed to ensure that developing-country Members, and especially the least-developed countries among them, are integrated into the multilateral trading system,<sup>160</sup> WTO law includes many provisions granting a degree of special and differential treatment to developing-country Members.<sup>161</sup> These provisions attempt to take the special needs of developing countries into account. In many areas, they provide for fewer obligations or differing rules for developing countries as well as for technical assistance. The rules on the special and differential treatment of developing-country Members are examined in detail throughout this book, but particularly in chapter 7.<sup>162</sup>

### 1.3.2.5. Rules promoting harmonisation of national regulation

A final group of substantive rules of WTO law that deserves separate attention are the rules promoting harmonisation of national regulation contained in the *TBT Agreement*, the *SPS Agreement* and the *TRIPS Agreement*. The *TBT Agreement* sets out rules on technical regulations, standards and conformity assessment procedures. The *SPS Agreement* contains obligations applicable to sanitary and phytosanitary measures. The *TRIPS Agreement* lays down minimum requirements for the protection of intellectual property rights. The rules in these three agreements have in common that they go far beyond the usual trade liberalisation rules and venture into 'behind-the-border' regulatory areas to a greater extent than other WTO agreements dealing with 'other non-tariff barriers' to trade. In addition to the usual WTO disciplines, they promote regulatory harmonisation around international standards. These rules are discussed in chapter 8.<sup>163</sup>

<sup>159</sup> See below, pp. 615–95. <sup>160</sup> See *WTO Agreement*, Preamble, second paragraph.

<sup>161</sup> For example, Article XVIII and Part IV of the GATT 1994 as well as the Enabling Clause. See below, pp. 723–31. <sup>162</sup> See below, pp. 723–31. <sup>163</sup> See below, pp. 741–884.



### 1.3.2.6. Institutional and procedural rules

All basic rules and principles referred to above are substantive rules and principles. However, the multilateral trading system also includes, and depends on, institutional and procedural rules relating to decision-making and dispute settlement. The rules regarding the institutions and procedures for the formulation and implementation of trade rules are discussed in detail in chapter 2. The rules and procedures regarding the settlement of trade disputes are dealt with in chapter 3.

#### Questions and Assignments 1.9

What are the basic rules and principles that make up the multilateral trading system? What is the most fundamental principle of WTO law? Does WTO law take into account the special situation of developing countries? Does WTO law address the conflict between trade liberalisation and other economic and non-economic societal values and interests?

## 1.4. SOURCES OF WTO LAW

WTO law is, by international law standards, a sprawling and complex body of law. This section reviews the sources of WTO law. Not all sources of WTO law reviewed below are of the same nature or are on the same legal footing. Some sources provide for specific legal rights and obligations for WTO Members that these Members can enforce through WTO dispute settlement.<sup>164</sup> Many other sources, reviewed below, do not in and by themselves provide for specific, enforceable rights and obligations. They are nevertheless sources of WTO law as they ‘clarify’ or ‘define’ the law that applies between WTO Members on WTO matters.<sup>165</sup>

The principal source of WTO law is the *Marrakesh Agreement Establishing the World Trade Organization*, concluded on 15 April 1994 and in force since 1 January 1995. Other sources of WTO law include WTO dispute settlement reports, acts of WTO bodies, agreements concluded in the context of the WTO, customary international law, general principles of law, other international agreements, subsequent practice of WTO Members, teachings of the most highly qualified publicists and, finally, the negotiating history.

### 1.4.1. The Marrakesh Agreement Establishing the World Trade Organization

The *Marrakesh Agreement Establishing the World Trade Organization* (the ‘WTO Agreement’) is the most ambitious and far-reaching international trade agree-

<sup>164</sup> I.e. Members can claim the violation of these rights and obligations before WTO dispute settlement bodies.

<sup>165</sup> Arguably, the respondent Member in a dispute could invoke rules ‘generated’ by these sources of WTO law in defence of a claim of violation. This is, however, controversial. See below, pp. 53–9.



ment ever concluded.<sup>166</sup> It consists of a short basic agreement (of sixteen articles) and numerous other agreements and understandings included in the annexes to this basic agreement.

## Agreement Establishing the World Trade Organization

### ANNEX 1

#### ANNEX 1A: Multilateral Agreements on Trade in Goods

General Agreement on Tariffs and Trade 1994

Agreement on Agriculture

Agreement on the Application of Sanitary and Phytosanitary Measures

Agreement on Textiles and Clothing

Agreement on Technical Barriers to Trade

Agreement on Trade-Related Investment Measures

Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994

Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade 1994

Agreement on Preshipment Inspection

Agreement on Rules of Origin

Agreement on Import Licensing Procedures

Agreement on Subsidies and Countervailing Measures

Agreement on Safeguards

#### ANNEX 1B: General Agreement on Trade in Services and Annexes

#### ANNEX 1C: Agreement on Trade-Related Aspects of Intellectual Property Rights

#### ANNEX 2: Understanding on Rules and Procedures Governing the Settlement of Disputes

#### ANNEX 3: Trade Policy Review Mechanism

#### ANNEX 4: Plurilateral Trade Agreements

Agreement on Trade in Civil Aircraft

Agreement on Government Procurement

On the relationship between the *WTO Agreement* and its Annexes as well as on the binding nature of the Annexes, Article II of the *WTO Agreement* states:

2. The agreements and associated legal instruments included in Annexes 1, 2 and 3 (hereinafter referred to as 'Multilateral Trade Agreements') are integral parts of this Agreement, binding on all Members.

3. The agreements and associated legal instruments included in Annex 4 (hereinafter referred to as 'Plurilateral Trade Agreements') are also part of this Agreement for those Members that have accepted them, and are binding on those Members. The Plurilateral Trade Agreements do not create either obligations or rights for Members that have not accepted them.

<sup>166</sup> The official version of the *WTO Agreement* and its Annexes is published by the WTO and Cambridge University Press as *The Results of the Uruguay Round of Multilateral Trade Negotiations: The Legal Texts*. The *Legal Texts* are an indispensable instrument for international trade law practitioners and scholars. The *WTO Agreement* and its Annexes are also available on the WTO website: [www.wto.org](http://www.wto.org).

While the *WTO Agreement* consists of many agreements, the WTO Appellate Body in one of the first cases before it, *Brazil – Desiccated Coconut*, stressed the ‘single undertaking’ nature of the *WTO Agreement*.<sup>167</sup> All multilateral WTO agreements apply equally and are equally binding on all WTO Members. The provisions of these agreements represent ‘an inseparable package of rights and disciplines which have to be considered in conjunction’.<sup>168</sup>

Furthermore, Article XVI:3 of the *WTO Agreement* provides:

In the event of a conflict between a provision of this Agreement and a provision of any of the Multilateral Trade Agreements, the provision of this Agreement shall prevail to the extent of the conflict.

Most of the substantive WTO law is found in the agreements contained in Annex 1. This Annex consists of three parts. Annex 1A contains thirteen multilateral agreements on trade in goods; Annex 1B contains the *General Agreement on Trade in Services* (the ‘GATS’); and Annex 1C the *Agreement on Trade-Related Aspects of Intellectual Property Rights* (the ‘TRIPS Agreement’). The most important of the thirteen multilateral agreements on trade in goods, contained in Annex 1A, is the *General Agreement on Tariffs and Trade 1994* (the ‘GATT 1994’). The plurilateral agreements in Annex 4 also contain provisions of substantive law but they are only binding upon those WTO Members that are a party to these agreements.

Annexes 2 and 3 cover, respectively, the *Understanding on Rules and Procedures for the Settlement of Disputes* (the ‘DSU’) and the *Trade Policy Review Mechanism* (the ‘TPRM’), and contain procedural provisions.

#### 1.4.1.1. *General Agreement on Tariffs and Trade 1994*

The GATT 1994 sets out the basic rules for trade in goods. This agreement is, however, somewhat unusual in its appearance and structure. Paragraph 1 of the introductory text of the GATT 1994 states:

The General Agreement on Tariffs and Trade 1994 (‘GATT 1994’) shall consist of:

- a. the provisions in the General Agreement on Tariffs and Trade, dated 30 October 1947, annexed to the Final Act Adopted at the Conclusion of the Second Session of the Preparatory Committee of the United Nations Conference on Trade and Employment (excluding the Protocol of Provisional Application), as rectified, amended or modified by the terms of legal instruments which have entered into force before the date of entry into force of the WTO Agreement;
- b. the provisions of the legal instruments set forth below that have entered into force under the GATT 1947 before the date of entry into force of the WTO Agreement:
  - i. protocols and certifications relating to tariff concessions;
  - ii. protocols of accession (excluding the provisions (a) concerning provisional application and withdrawal of provisional application and (b) providing that Part II of

<sup>167</sup> See Appellate Body Report, *Brazil – Desiccated Coconut*, 177.

<sup>168</sup> See e.g. Appellate Body Report, *Argentina – Footwear (EC)*, para. 81. In *Korea – Dairy*, the Appellate Body explicitly agreed with the statement of the Panel in that case that ‘[i]t is now well established that the *WTO Agreement* is a “Single Undertaking” and therefore all WTO obligations are generally cumulative and Members must comply with all of them simultaneously’. See Appellate Body Report, *Korea – Dairy*, para. 74.