



# Revitalizing Multilateral Governance at the World Trade Organization

Report of the High-Level Board of Experts on the Future of Global  
Trade Governance

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## 1 Preface

If international trade is not governed by rules, mere might dictates what is right. The World Trade Organization (WTO) serves as a place where trade policy issues are addressed, disputes arbitrated, legal frameworks derived and enforced. Through these functions, the WTO ensures that the rules of trade policy are inspired by fairness and reciprocity rather than national interest. It is more important than ever to vitalize the global public good that it represents against various threats that have been undermining it.

Therefore, the Global Economic Dynamics project of the Bertelsmann Stiftung has called into life a High-Level Board of Experts on the Future of Global Trade Governance. Composed of eminent experts and seasoned trade diplomats, it elaborated a series of feasible policy recommendations that will increase the effectiveness and salience of the WTO. We hope that this Report provides helpful suggestions in a time marked by increasing trade disputes and protectionism and instead contributes to stronger multilateral institutions and fora.<sup>1</sup>

The Bertelsmann Stiftung owes a debt of gratitude to Prof Bernard Hoekman, the Chairman of the Expert Board and author of this report. His invaluable expertise and experience, guidance and ability to bridge controversial opinions have been crucial in defining the work of the Board. We would also like to express our sincere thanks to all our Board Members, who generously contributed their expertise, time and networks. Without their dedication, this Report would not have been possible. Finally, we would like to thank Robert Koopman and Aik Hoe Lim of the WTO for their support throughout the whole process and Christian Bluth of Bertelsmann Stiftung for managing this common endeavour.

Aart De Geus

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<sup>1</sup> The analysis and suggestions made in this report reflect the dominant view among the members of the Expert Board. Members of the Board participated in meetings on a personal basis – the views expressed should not be attributed to any of the organizations Expert Board members are affiliated with.

## 2 Members of the High-Level Board of Experts on the Future of Global Trade Governance

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Hector <b>Torres</b>	Senior Follow CIGI, former Executive Director at the International Monetary Fund

### 3 Executive Summary

The trading system is in crisis. Urgent action is needed to revitalize its central organ, the World Trade Organization (WTO). Such action must come from its Members and be based on renewed multilateral dialogue on the use and effects of trade-distorting policies in both developed and developing nations. Dialogue is also needed to resolve conflicts regarding the operation of the WTO dispute settlement mechanism and to assess the functioning of the organization.

The fundamental consensus norm has been abused to resist multilateral discussion of new policy areas and concerns regarding the functioning of the organization. Members should reflect on whether WTO bodies provide them with the information they need to assess implementation of existing agreements and identify gaps where the rules need to be updated. Without discussing how the WTO operates, Members will not be able to create a framework for issues such as the governance of digital trade or how to enhance trade's contribution to societal goals.

All WTO members benefit from the rules-based trading system. Participating in mega-regional trade agreements offers a complementary vehicle for cooperation to countries willing to deepen integration of markets, but this is not a viable alternative for many developing countries and risks fragmenting the rules that apply to global value chains. Nor will such agreements discipline key trade-distorting instruments such as subsidies.

Safeguarding the WTO is particularly important for smaller countries. Only the multilateral trading system offers them the opportunity to influence the development of new trade rules.

Friends of the multilateral trading system can pursue four complementary avenues to revitalize the WTO as a forum for trade cooperation and conflict resolution:

**1. Policy dialogue.** WTO members need to establish a new work program to address both long-standing and more recent use of trade-distorting policies that are systemically important. Dialogue is necessary for WTO members to determine what those issues are and to agree on a road map for the future. Dialogue should include a focus on the functioning of WTO bodies – the Committees overseeing implementation of WTO agreements, the Appellate Body and the dispute settlement system more broadly. It should encompass a process of self-reflection by WTO bodies to identify (i) how to enhance their usefulness to their constituencies; (ii) the information needed to enhance their relevance; (iii) whether trade measures help economic development; and (iv) how trade can be more fully used as a tool to realize the sustainable development goals.

**2. Support open plurilateralism.** Members need to consider whether all Members must participate in the launch of every new negotiation or initiative. Greater pursuance by groups of WTO members of open, non-discriminatory plurilateral initiatives offers the opportunity to move forward on issues where concerns about free-riding do not exist or can be addressed. Such initiatives do not require consensus to start. Others can always join the discussion when they are ready to do so. Four subjects are already being discussed in plurilateral groups. Others may emerge from the suggested policy dialogue processes.

**3. Enhance the scope for the Secretariat to provide inputs.** The WTO is a 'member-driven' organization in which the Secretariat is given too little voice. Empowering the Secretariat to do more to support policy dialogue in WTO bodies and the work of WTO Members engaged in open plurilateral initiatives will bolster the trading system.

**4. Review WTO institutional performance.** The operation of the WTO as an institution is not subject to regular assessment. Establishing a review mechanism that incorporates self-assessment by WTO bodies can present Members with facts they may not be fully aware of, and information on working practices, Member engagement and outcomes.

A precondition for revitalizing engagement at the WTO is that its work program deal with matters of systemic import and does so without undercutting the scope for poor countries to pursue development policies. The recommendations are aimed at satisfying these desiderata.

Policy dialogue is critical to establish a new work program. Such a work program must include subjects that matter to all WTO members. In practice this will mean a mix of old and new topics. Long-standing subjects of great importance to many WTO members include eliminating tariff escalation, managing global overcapacity in specific industries, disciplining agricultural subsidies, and protection of intellectual property. New subjects are likely to include digital economy-related policies that may distort trade and investment in services, e-commerce regulation

and the development of (access to) new technologies. What is needed is a balanced work program that offers a credible prospect for addressing priority issues for all WTO members, whether developed, emerging or developing.

Self-reflection in WTO bodies can help to (re-)establish a common understanding of the strengths and weaknesses of existing agreements. It can identify opportunities to expand cooperation in a policy area and enhance economic development impacts. Many WTO members want emerging economies to make more extensive trade policy commitments while developing economies cite their need to address their development challenges. Greater differentiation in the rights and obligations of developing countries is a sensitive political issue but is essential if development concerns are to be properly addressed.

A committee-by-committee process of deliberation – including the Dispute Settlement Body – can help re-build the trust needed for constructive, good faith engagement on substantive policy questions based on solution-oriented proposals. To do so, deliberations must be inclusive and engage the whole membership. Regular assessment of the performance of the WTO as an organization – spanning both WTO members and the Secretariat – will enhance transparency and improve information on implementation of WTO agreements.

There is no presumption that what is needed is a new round of multilateral negotiations. Nor that every Member must engage on every element of the work program. Policy dialogue may identify opportunities for cooperation that are not of interest to all WTO members. In such instances open plurilateral initiatives provide a mechanism for subsets of the WTO membership to deepen cooperation. Such initiatives differ from preferential trade agreements by being both open to any WTO member and not discriminating between participants and non-participants in the application of benefits. This is nothing new for the WTO – examples include the Information Technology Agreement and the Telecom Reference Paper establishing regulatory principles for telecommunication services. WTO members can decide to apply these agreements if they wish to. Open plurilateral initiatives permit countries seeking to retain policy space for development reasons to do so – they need not participate.

Objective and timely information is vital for constructive deliberation. The heterogeneity of the WTO membership implies that knowledge about issues and international experience may vary substantially across countries. Ensuring that the WTO Secretariat, working in conjunction with other international organizations, can provide the required support to WTO members is important. This includes better monitoring and analysis of implementation and effects of WTO agreements, information on the experience with approaches that have been used in preferential trade agreements for a given policy area, and synthesis of extant knowledge of development effects and good practices.

If successfully implemented, the recommendations can help WTO members develop a road map to resolve current trade conflicts, clarify and improve the operation of the dispute settlement process, and move towards a trading system that entails greater use of open plurilateralism as a complement to the expansion of membership in mega-regional trade agreements. At the 2017 WTO Ministerial Conference in Buenos Aires the US called for WTO reform. In May 2018 President Macron did the same. Ideally, all large players, jointly with others, will work together to consider reforms to the WTO.

Due in part to the rise of global value chains and the success of the system, many more countries are today participating in international trade. This creates opportunities and incentives for groups of WTO members to take on a greater role. Different possibilities may exist to constitute a critical mass large enough to provide leadership. For instance, three of the four largest trading powers – China, the EU and Japan – account for more than one-third of world trade in goods and services and more than half of the WTO budget.

Leadership cannot come from large trading powers alone. Even more powerful would be if East Asia as a region played a greater role, with shared leadership between China, Japan and middle powers such as Korea and Indonesia (combined with ASEAN). A coordinated effort to invest more of their soft power to support reform initiatives could do much to change the dynamics.

Economies pursuing deep integration of markets are best placed to play a complementary, catalytic role. Examples include the members of the Comprehensive and Progressive Agreement on Trans-Pacific Partnership, the Pacific Alliance, the East Asian countries in the Regional Comprehensive Economic Partnership, and, more broadly, the WTO 'Friends of the System' group of smaller economies. Together with the EU these countries account for more than 75 percent of world trade. They constitute a critical mass that can help sustain multilateral cooperation and drive the trading system forward.

## 4 Revitalizing the WTO

The World Trade Organization (WTO) plays a central role in global trade governance.<sup>2</sup> An open world economy requires a governance framework that establishes ground rules for economic operators and governments. The mutually agreed rules embodied in the WTO agreements reduce uncertainty for firms regarding the policies that apply to their products in foreign markets. Preserving an effective multilateral trading system is vital to help countries cooperate in managing rapid structural change and transformation.

International trade is at a crossroads. The ongoing shift away from agricultural and assembly line manufacturing activities that are predominantly national in nature towards geographically dispersed international production networks and a rising share of total value added created by services activities calls for updating the prevailing governance framework. Efforts to undertake such updating have been stymied by disagreements among WTO members regarding the priorities for the multilateral trading system. These disagreements inhibit the scope for the organization to perform its role as a venue for deliberation and rule-making, monitoring and enforcement of mutually agreed policy commitments.

The failure to conclude the first multilateral round of trade negotiations held under WTO auspices, the Doha Development Agenda, has had serious consequences. These go beyond the significant opportunity cost of global welfare gains foregone from not disciplining the use of trade-distorting policies that have long been on the agenda of the WTO – such as agricultural support and tariff escalation. The Doha round failure has impeded WTO members from addressing new sources of policy tension and engaging in a collaborative effort to update WTO rules to reflect the changes that have occurred in the global economy in the 25 years since the WTO treaty was negotiated.

The difficulty in making progress in negotiating new agreements in the WTO has increased incentives for WTO members to negotiate preferential trade agreements (PTAs). The number of PTAs has been rising steadily since the early 2000s. More than 400 PTAs are in force today, some of which span more than one region of the world. Resort to PTAs reflects many motivations but a common element is a willingness of participating countries to engage in deeper integration than they deem desirable or feasible in the broader multilateral setting. Such agreements complement the WTO – and the WTO makes explicit provision for them – but they are at best only a partial substitute for globally welfare-enhancing multilateral cooperation on trade policy.

### Challenges

The effects of greater international economic integration are increasingly contested in high-income countries. Sustained high rates of economic growth in several large developing countries have resulted in major shifts in global output and trade shares. As average per capita incomes in these nations have risen, the global distribution of income has become less unequal. However, within most economies, the opposite has occurred: income inequality has increased as skilled workers and owners of financial assets have experienced higher rates of income growth than less skilled workers. The role of trade and trade liberalization as a driver of greater inequality and stagnation in average household incomes of the middle class in many countries is hotly debated. Empirical research demonstrating that trade is not the major driver of these trends – they are primarily the result of technical change and domestic policy choices – has had little impact on domestic political debates. Trade agreements have become a focal point for criticism.

Arguments against trade agreements and the trading system span a wide spectrum, including businesses, NGOs and citizens more generally. Protests against recent EU trade negotiations with Canada and the US as well as opposition in the US by leaders of both major political parties against the Trans-Pacific Partnership and the North American Free Trade Agreement demonstrate that the idea and value of rules-based trade is being questioned.

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<sup>2</sup> This report draws on several meetings by the board of experts and background papers and presentations by Robert Basedow, Aaditya Mattoo, Kamal Saggi, Hector Torres and Robert Wolfe. It has benefitted from suggestions by Robert Koopman and Aik Hoe Lim, numerous trade officials and participants in seminars and workshops at the EUI, the WTO Public Forum (2017), the Trade and Development Symposium (Buenos Aires, 2017), the Asian Leadership Conference (Seoul, 2018), the 2018 Shanghai Forum and the Global Solutions Summit (Berlin, 2018). Thanks are due in particular to Simon Evenett and Piotr Lukaszuk for generously sharing data from the Global Trade Alert initiative and to Benedikt Dengler for excellent research assistance.

There are deep-seated perceptions in major emerging economies such as China and India that the WTO is unbalanced and treats them unfairly. Conversely, many OECD member countries argue that China and other emerging economies engage in trade-distorting policy practices that skew competition in favour of national companies (Wu, 2016). Consumers and citizens worry about the fairness of trade and ensuring that national governments retain the autonomy to regulate economic activity to realize fundamental societal goals.

A basic question confronting the international trade community is how trust in the global rules-based trading system can be restored and reinforced. Sustaining an effective multilateral trading system is critical in helping governments address the concerns briefly enumerated above. Reversal of trade liberalization and rejection of trade policy commitments made in the WTO or in regional trade agreements is not a solution. Doing so will simply increase trade costs and raise prices of products for consumers. Instead of increasing domestic investment, employment or wages it is more likely to have the opposite effect.

All WTO members stand to gain from concerted efforts to cooperate on the trade-related policies that are of concern to stakeholders and that underlie the recourse of some countries to unilateral trade policy actions. This applies as much to the US as it does to China, India, other Asian nations, African countries, the EU or any other WTO member.

- Large OECD trade powers such as the EU, Japan and the US need a functioning multilateral trade regime because most of the concerns they have raised regarding foreign trade practices cannot be addressed effectively – or efficiently – on a bilateral basis. Any deal with one country will be eroded by a mix of market forces that drive investment towards other countries. Many trade practices that create negative spill-over effects are not unique to one country.
- Large emerging economies need a functioning multilateral trade system because they do not have bilateral or regional trade agreements with their main trading partners and have not participated in recent efforts to conclude deeper economic integration arrangements. The WTO provides the primary locus where they can participate in setting the rules for new areas of policy in which they have a great stake – such as e-commerce or digital trade and investment.
- Developing countries need a functioning multilateral trade regime because they have little market or negotiating power vis-à-vis large trading nations or blocs. The rules-based multilateral trading system provides the basic foundation for the effort that many developing countries are undertaking to integrate markets on a regional basis. An important example is the African initiative to create a continent-wide integrated regional market for goods and services.
- Citizens of countries concerned with ensuring that trade supports societal goals and sustainable development need a functioning multilateral trade regime that upholds and bolsters the ability of governments to take actions to achieve these objectives.

Unfortunately, recent developments regarding the multilateral trade system are troubling. The United States – a nation that played an important leadership role in the design and operation of the WTO and its predecessor the General Agreement on Tariff and Trade (GATT) – has become increasingly dissatisfied with the organization.<sup>3</sup> But the US is not alone. Many countries are frustrated. Some are strongly of the view that the organization needs to develop a new work programme that encompasses the unresolved policy agenda that was at the heart of the Doha round as well as new issues of increasing concern to businesses and consumers, such as e-commerce, subsidies and investment-related policies. Others, including many developing countries, insist that efforts to discuss ‘new’ (non-Doha) subjects can only be considered once the Doha agenda subjects that matter to them have been resolved.

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<sup>3</sup> At the 2017 Ministerial Conference in Buenos Aires the US Trade Representative laid out a WTO reform agenda spanning compliance with WTO obligations, notably notification requirements, clarifying the understanding of economic development within the WTO and more generally a joint reflection on the question whether playing by current WTO rules makes it harder to achieve economic growth, revitalizing standing WTO bodies to ensure they are focused on new challenges, and action to re-consider the current litigation structure. See <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2017/december/opening-plenary-statement-ustr>.

The problems go beyond the inability to conclude the Doha round. WTO monitoring efforts (WTO, 2017a) and the Global Trade Alert initiative<sup>4</sup> reveal that many countries use a wide variety of non-tariff policies to increase incentives for local production or exports (Evenett and Fritz, 2017a,b).<sup>5</sup> Often these do not violate the letter of WTO law but nonetheless may distort trade. Some threaten to undermine the system. The recent invocation of national security concerns for the imposition of tariffs and quotas on imports of selected products by the United States is a prominent recent example. Such measures create systemic risks given the prospect of tit-for-tat imposition of trade-distorting measures and greater use of national security justifications by WTO members for the imposition of protectionist measures. Such a development would be detrimental to all countries involved as well as the rest of the world. Nicita, Olarreaga and Silva (2018) estimate that a full-blown trade war in which all countries engage in tit-for-tat tariff setting would raise import duties facing the average exporter by 32 percentage points. Such a major increase in taxation would have significant negative effects on global demand and economic growth. Avoiding such an outcome is in the interest of all WTO members.

Another worrisome recent development is the US refusal to agree to appointments of new Appellate Body (AB) members as the term of sitting members expires. If this matter is not resolved, the Appellate Body will be down to 3 members in September 2018, the minimum needed to consider an appeal, and will cease to be operational at the end of 2019 when two more vacancies arise. This constitutes another systemic risk if it leads to unilaterally determined retaliation in cases where dispute settlement panel reports are not adopted.

Sustaining the WTO dispute resolution mechanism – generally held to be a major global governance innovation – is critically important for the organization. Numerous proposals have been made in the last 15 years by WTO members to improve and clarify the current conflict resolution system in the context of a review of the Dispute Settlement Understanding. However, the need for consensus and a desire by WTO members to make reforms to dispute settlement part of a larger “package deal” that encompasses other subjects (even though formally the dispute settlement review was not part of the Doha round) has impeded agreement on reforms.

The 11<sup>th</sup> Ministerial conference in Buenos Aires in December 2017 ended without a Ministerial Declaration and without agreement on the sole subject where a deal was potentially in reach – on disciplines on fishery subsidies. The former reflected disagreement on what in the past would have been considered innocuous ‘motherhood and apple pie’ language on economic development and multilateralism, while the latter ran aground on resistance from both ends of the subsidy spectrum – nations supporting large high seas fishing fleets as well those reliant on artisanal fishing – to banning fishery subsidies. The business community was missing in action. CEOs did not call their Presidents and Prime Ministers, nor did national leaders engage effectively with each other before the conference (Wolff, 2017).

Notwithstanding these factors, the Buenos Aires meeting had an important positive outcome that offers scope for some optimism for the future. Groups of WTO members agreed to launch talks on four policy areas: E-commerce; obstacles to trade confronting micro, small and medium-sized enterprises (MSMEs); investment facilitation; and domestic regulation of services. These initiatives provide an important signal that many countries – both developed and developing – are willing to pursue cooperation on trade policy matters in the context of the WTO. Noteworthy as well was that several developing countries played a leadership role in getting these initiatives launched.

## **Responding to the challenges**

The WTO has a central role to play as a forum and framework for countries to manage trade tensions and conflicts. The trading system is a key instrument for attainment of the Sustainable Development Goals – it is only through the WTO that agreements can be concluded to reduce policy distortions in world agricultural markets that negatively

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<sup>4</sup> See, e.g., Evenett and Fritz (2017a) and more generally <http://www.globaltradealert.org>.

<sup>5</sup> Between 2009 and April 2018, Brazil, China, India, Indonesia and South Africa implemented a total of 2,327 trade-distorting measures, accounting for 22 percent all such measures captured in the GTA database. India accounted for almost 40 percent of the measures undertaken by these 5 large emerging economies. Slightly more than half of the measures involved were subsidies or targeted investment; 13.5 percent involved import tariffs and 25.5 percent took the form of trade defense instruments such as antidumping.

affect developing countries, discipline the use of trade-distorting subsidies, remove barriers to trade in environmental products, or support integration of small-scale enterprises into value chains through global trade and investment facilitation in an increasingly digital economy.

Multilateral negotiations on rule-making are just one dimension of the WTO's functions. The WTO plays a vital role in fostering transparency of trade, monitoring the trade policies of members and providing a platform for deliberation. The Secretariat provides support services for regular interactions at technical level between members, as well as the adjudication of disputes. On most of these dimensions PTAs cannot compete. Indeed, it is not sufficiently recognized that the WTO provides the basic infrastructure of rules for PTAs, as these invariably refer to and generally build on WTO provisions. Weak institutionalization of PTAs means they often rely on WTO notifications and even dispute settlement.<sup>6</sup> Moreover, while there are exceptions, for example, the Comprehensive and Progressive Agreement on Trans-Pacific Partnership (CPTPP), which includes disciplines on e-commerce policies and state-owned enterprises, most PTAs do not deal with areas of policy that can generate global spill-over effects – such as the use of various types of subsidies.

Some observers have argued the trading system is like a bicycle (Bergsten and Cline, 1982) in that it needs to keep moving to stay upright: regular progress is required on rule-making on trade policies for countries not to revert to protectionism. Sceptics have contested this 'bicycle theory', arguing that, in a common law framework, new rules emerge through various forms of interaction and that the institutional framework provided by the WTO to monitor trade policies and to resolve trade disputes was robust. This 'tricycle' view sees the WTO as a more stable mechanism for cooperation. The inability to finish the Doha round, the stalemate on new Appellate Body appointments, and increasing use of trade-distorting policies in several WTO members implies that the tricycle is stuck. The challenge is to get it moving again and to steer it in a direction that is in the interest of all its members.

What the destination should be is a matter for WTO Members to determine. What is clear is that the destination is not 'free trade'. The Preamble to the WTO text states that the goal of organization is "raising standards of living, ensuring full employment (and) expanding the production of and trade in goods and services." To contribute to these objectives, it fosters "reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade." All these objectives are placed in the context of "allowing for the optimal use of the world's resources in accordance with the objective of sustainable development, seeking both to protect and enhance the environment."

It is insufficiently appreciated by both trade critics and advocates that the WTO is primarily a mechanism to govern national commercial policies: agreeing and implementing a body of rules and good trade policy practices to which members commit themselves. Agreements not to exceed certain tariff levels (so-called tariff bindings) and to abide by jointly agreed procedural rules make trade policies more predictable, transparent and less burdensome to traders. The associated reduction in uncertainty is the primary product of the WTO. This has significant value in and of itself, whatever the incremental reduction in applied trade barriers that may be agreed through periodic trade negotiations or accession to the organization by new members.<sup>7</sup>

It is fruitless to engage in finger-pointing or apportioning blame for rising trade tensions. The priority is to prevent escalation of trade conflicts and unilateral resort to trade restricting measures that damage all WTO members. The immediate need is to avoid further erosion of the WTO's credibility. This includes preventing backsliding by WTO members towards unilateral use of protectionist trade policies and ensuring that disputes are resolved effectively and efficiently. Other challenges centre on bolstering cooperation to leverage trade for sustainable development and adapting to the new realities of global production and trade in services and digital products.

Inertia and complacency reflected in a 'business as usual' approach to the daily activities of the institution ignore the serious threat of unravelling much of what has been achieved in recent decades. Continued cooperation cannot

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<sup>6</sup> Many specific rules embodied in PTAs are often copied and pasted from relevant WTO agreements. This is frequently the case for disciplines on the use of product standards and trade defence instruments.

<sup>7</sup> The economics literature has stressed the role that international agreements can play as a policy commitment device (Maggi and Rodriguez-Clare, 1998) and the associated effects of this in curbing uncertainty, and thereby supporting greater trade. The salience of the latter motivation increases in periods of economic distress (Carballo, Handley and Limão, 2018). Francois and Martin (2004) discuss the role that policy commitments in trade agreements can play in reducing uncertainty for firms (investment). Handley (2014) and Handley and Limão (2015, 2017) are recent papers that provide estimates of the economic effects of such uncertainty reduction.

be taken for granted, even if trade tensions end up being contained. The call by President Macron of France at the OECD ministerial meeting in May 2018 to launch talks on WTO reform is a positive development, which hopefully will be pursued by the WTO membership. The costs of a gradual erosion in the salience of the WTO will be significant, especially if this is associated with an increase in uncertainty and recourse to protectionist measures. Small countries that make up most of the WTO membership have the most to lose from a resurgence in the use of unilaterally determined trade policies in major export markets as they have little market power and benefit from multilateral rules as opposed to having to satisfy differentiated and potentially conflicting trade policies in major export markets. Beyond the losses from potential reversals in trade policies, the opportunity cost of the world losing the primary platform through which Members can collectively govern international trade relations is likely to be very high for all countries.

### **This report**

The main goal of this report is to make specific suggestions on how WTO members can revitalize the WTO. It is based on discussions among Board members, written contributions by several members, and meetings with trade practitioners.<sup>8</sup> The report does not take a view on the relative merits or importance of substantive policy issues that have been or should be the subject of rule-making efforts, although it will refer to specific subjects that have been or may become the subject of discussion as a result of changes in the structure of the world economy. A huge literature exists on the Doha round specifically, the effects of trade-related policies more generally, and priorities and options for multilateral cooperation. This is not re-visited here.<sup>9</sup> The focus is on what could be done to increase the effectiveness of the WTO as an institution through which countries can define priorities, address policy spillovers and cooperate for mutual benefit.

A premise is that WTO working practices diminish the effectiveness of the organization. Insistence that Ministerial mandates define what can be discussed in the WTO, that all developing countries must be treated equally in terms of special and differential treatment, independent of size, export capacity or per capita GDP, and a willingness to accept that consensus can be used to block the normal operation of the WTO are examples of working practices that have eroded the efficiency of the institution as a forum for trade cooperation and practical problem solving. These practices often reflect tactics in the service of negotiating strategies pursued by WTO members to achieve specific goals. Identifying better processes and approaches to help countries achieve their objectives is a necessary condition for improving the effectiveness of the WTO.

Previous reports on the WTO have recommended changes in the governance of the organization.<sup>10</sup> We refrain from suggesting major reforms to the existing governance framework. Proposals in earlier reports and the policy research literature on WTO governance have mostly been ignored. The lesson is that top down, external, ‘technocratic’ approaches seeking to redesign the basic governance mechanisms of the WTO are doomed to fail. The institutional framework that has been put in place over many years reflects the revealed preferences of the membership. This framework provides great scope for Members to pursue pragmatic and flexible approaches to improve the effectiveness and utility of the WTO as a mechanism to attain national objectives. A necessary condition for progress is a willingness by a plurality of members to engage in efforts to improve the operation of the organization and to reconsider some of its working practices.

Although the trading system is today under significant pressure, it is important to recognize that there are many positives. Much has been achieved by the WTO membership since the organization was established in 1995. The

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<sup>8</sup> The report draws on background papers prepared for this project (Basedow, 2017a and 2017b; Wolfe, 2018); as well as other analyses of the functioning of the WTO and the challenges it confronts. The latter include Torres (2017a,b), Steger (2009), Baldwin and Low (2009), Mattoo and Subramanian (2009), Draper et al. (2015), Elsig (2016) and Evenett and Fritz (2107b).

<sup>9</sup> Samans et al. (2016) summarize the recommendations of a major effort to identify priorities, options and opportunities for multilateral cooperation across a wide range of trade-related issues. Reasons for the demise of the Doha round have been analyzed extensively (e.g., Zedillo, 2007; Martin and Messerlin, 2007; Laborde and Martin, 2015; Wolfe, 2015). Views differ, but most observers point to a mix of the following factors: the choice of negotiating agenda and modalities, domestic politics – especially governments with very thin majorities, the boom in global trade during the first 7 years of the talks (before the 2008 financial crisis erupted), and extensive economic policy reforms implemented unilaterally by many countries that left mostly sensitive products with above average levels of protection to be negotiated.

<sup>10</sup> These include Sutherland (2004), Warwick Commission (2007) and Abu-Ghazaleh et al. (2013).

track record of dispute settlement cases brought forward by WTO members – over 500 to date – is quite good. Accession to the WTO of 36 new members since 1995 illustrates the value accorded to the system. The accession of China was a landmark development. The negotiation of a Trade Facilitation Agreement (TFA) in 2013 and a ban on agricultural export subsidies are two major achievements realized in the past five years. The TFA embodies extensive differentiation across developing countries, complementing previous WTO Agreements that treat developing countries differently based on income levels or export market shares, demonstrating the feasibility of differentiating between countries.<sup>11</sup>

A complementary initiative launched under WTO auspices has resulted in an expansion of development assistance to strengthen trade capacity ('aid for trade'). This includes the establishment of the Enhanced Integrated Framework to assist Least Developed Countries (LDCs), another significant achievement reflecting a recognition that to benefit from market access opportunities many developing countries need assistance to enhance supply capabilities. There have also been successful initiatives to reduce barriers to trade in specific products among a subset of the WTO membership, most notably the Information Technology Agreement (ITA), the coverage of which was expanded in 2015. These attainments illustrate that progress has been made on several important fronts. There is much to build on.

## 5 A changing global economic context

The global economy has changed substantially in recent decades. Growth in international trade, cross-border investment and knowledge flows has supported major reductions in global poverty, increasing real incomes of hundreds of millions of people in low-income countries. Households in richer nations have also benefitted greatly, as greater competition has driven down prices of goods, fostered innovation and increased the variety and quality of products. Trade liberalization and the associated integration of product markets is just part of the story. Structural transformation driven by technological change has been and will continue to be a major force affecting labor markets independent of trade. Rapid expansion of the digital economy, reflected in shifts to e-commerce, the servicification of manufacturing and associated cross-border flows of data, services and digital products is changing the demand for skills and the organization of international production.

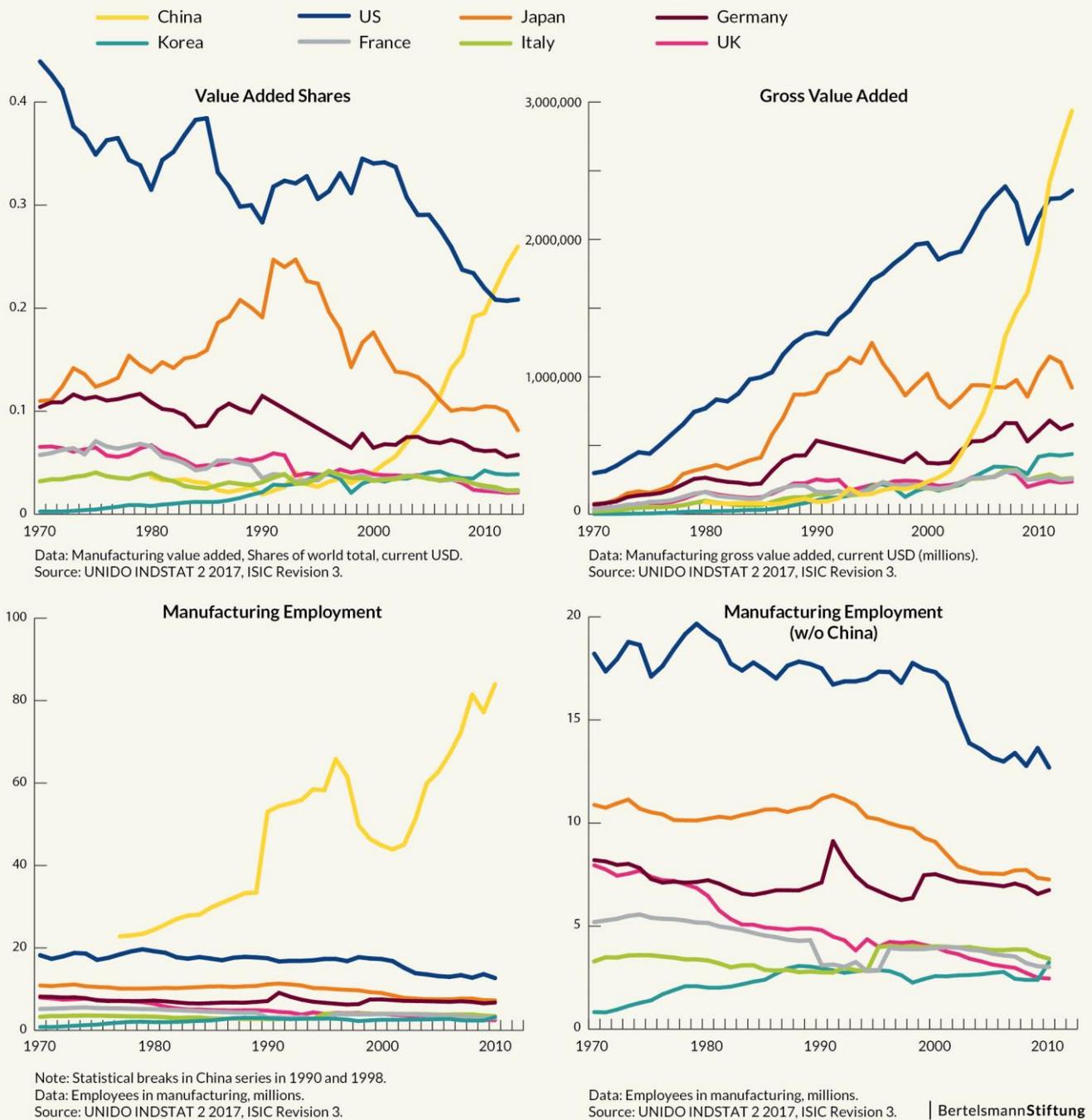
Developing and emerging economies have come to account for almost half of the value of global merchandise trade and global GDP. Reforms pursued by developing countries and transition economies have supported a major expansion in export-oriented manufacturing production in many of these countries. The corollary of this growth in manufacturing activities in emerging economies has been a decline in relatively unskilled employment in manufacturing in OECD member countries. Much of the growth in manufacturing output and employment has occurred in China (Figure 1), helping to explain why China has been at the centre of attention in debates about the distributional effects of globalization and the competitive implications of its rapid export growth. China has become a major trade partner for many countries around the world.

The rapid increase in China's share of global trade has given rise to increased scrutiny of China's economic policies and their consistency with WTO rules. In recent years China-related cases have accounted for most of the disputes brought to the WTO by the four largest trading powers against each other (Wu, 2016). Looking forward, one of the major challenges confronting the trading system is addressing tensions that have arisen because of gaps in the WTO rulebook that inhibit the ability of WTO members to determine whether certain types of policies distort competition.

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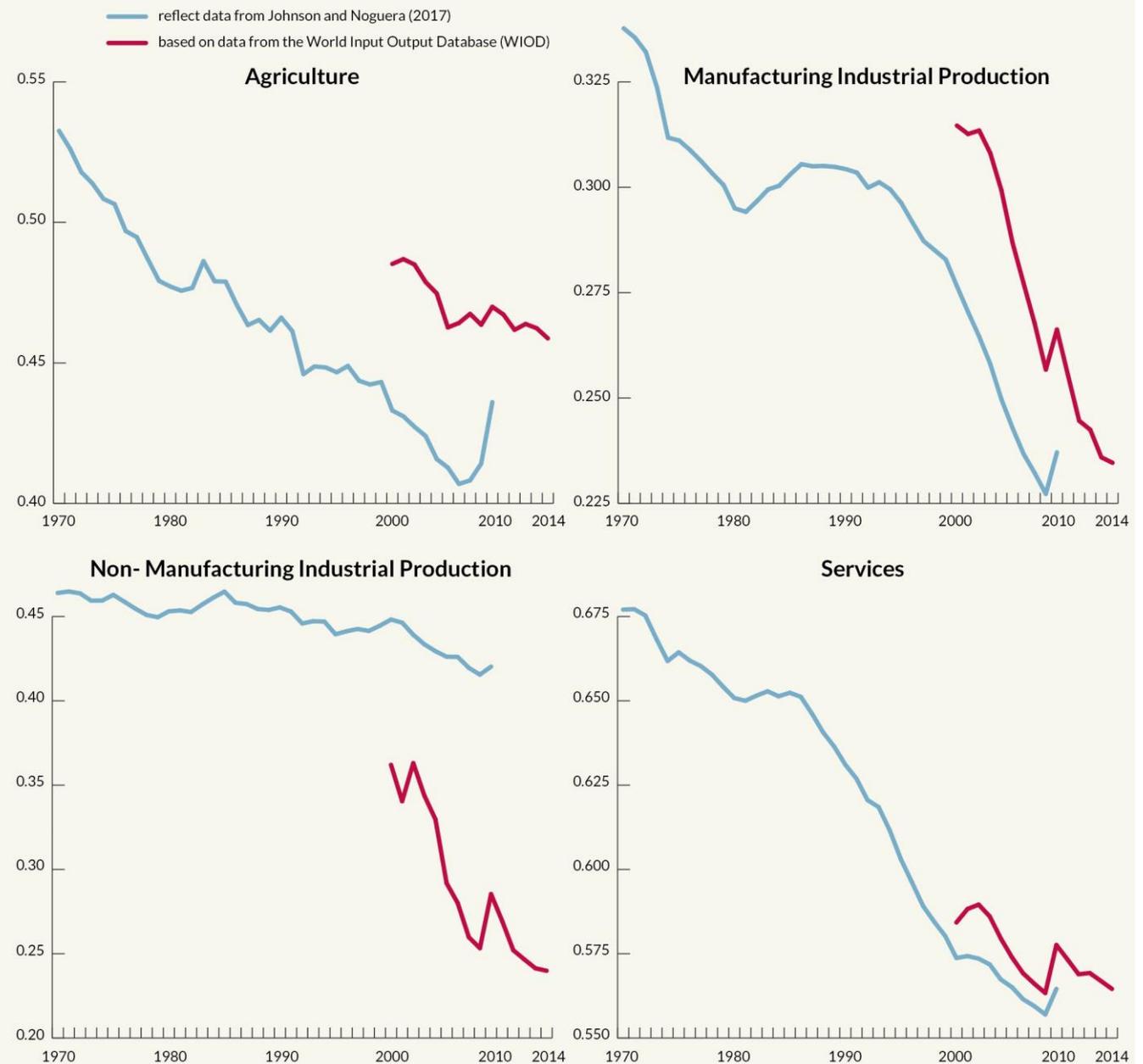
<sup>11</sup> As discussed below, an example is provided by the Agreement on Subsidies and Countervailing Measures.

FIGURE 1: China's rising share in global manufacturing output and employment



An increasing share of global trade comprises intermediate inputs, with value added generated in many countries (Baldwin, 2016). Supply chain-based production and trade has driven a steep fall in the ratio of domestic value added to total gross output in most countries, as an increasing share of value added embedded in products is imported. This is observed for all types of products, not just manufactured goods (Figure 2). The rise in the import content of domestic production reflects increasing specialization by firms. The associated reorganization of global production by companies to exploit the comparative advantages of different countries and locations has greatly increased economic interdependence.

FIGURE 2: Ratio of domestic value added to gross output



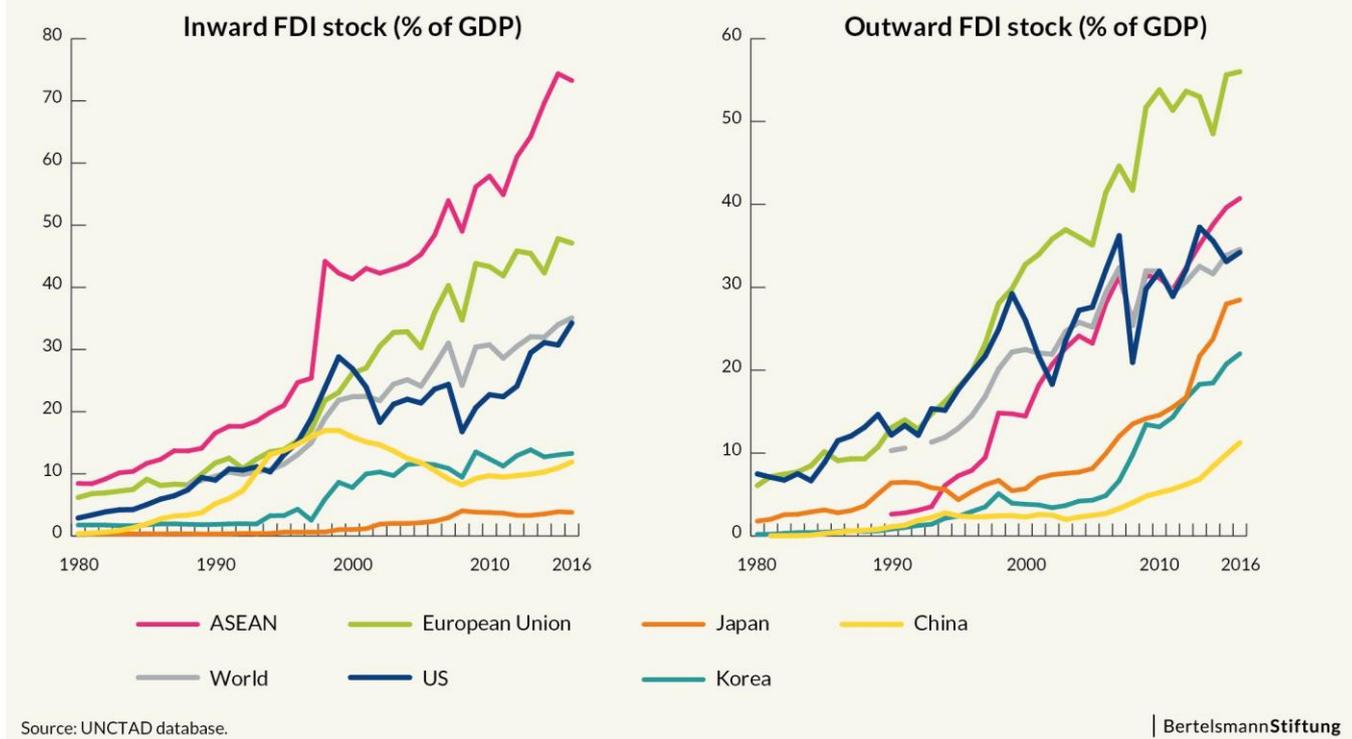
Notes: Blue lines reflect data from Johnson and Noguera (2017); red lines based on data from the World Input Output Database (WIOD). The data combine two different sources that are not strictly comparable. The more recent WIOD data indicate that the reversal in the declining share of domestic value added in total domestic output observed in 2009-10 was an artefact of the 2008 financial crisis-induced demand shock.

Source: Data files provided in Johnson and Noguera (2017) and 2016 WIOD release.

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A core feature of this process of specialization and rising mutual dependence reflected in multi-country supply chain-based production has been large flows of inward and outward foreign direct investment (FDI). In many countries a significant share of domestic production is now undertaken by affiliates of foreign companies (Figure 3), implying that national income and employment is in part generated by foreign-owned companies. FDI is a mechanism through which countries can acquire access to new technologies and knowledge, as well as to the distribution channels needed to sell products in export markets. Stocks of FDI are particularly large in ASEAN, the EU and the US – regions where the share of supply-chain-based trade is high. Inward FDI as a share of GDP is relatively low in China and has not increased substantially since the mid-1990s. This may in part reflect the policy stance towards FDI. China's outward FDI has been growing in the past decade, although it remains relatively low compared to higher income countries.

FIGURE 3: Inward and outward FDI



FDI is important for services providers to be able to supply services to foreign customers. Although services are rapidly becoming more tradable, to date establishing production facilities in a foreign market is often necessary for a firm to be able to supply services to foreign clients. The data in Figure 2 show that the extent of internationalization of the production of services is far below what is observed for manufacturing or agricultural production. The average ratio of domestic value added to the value of total production (gross output) in manufacturing is around 0.25, i.e., 25 percent. For services it is a bit less than 0.6. The ratio has been falling over time, but it is more than double what is observed for manufactured products. Looking forward, technological changes permitting services to be digitized and automated will permit an increasing share of total output to be sourced from other countries. While the extent of fragmentation of production of services that will emerge in coming years is not known, the data indicate that in principle there is great scope for internationalization of services. This calls for a governance framework to guide firm behaviour and activities and to ensure that domestic regulatory goals are met.

The far-reaching interdependence, specialization and fragmentation of production that is part and parcel of the process of globalization relies on firms being assured that the policy environment in which they operate is predictable. This is especially the case in industries where firms must make large investments with long time horizons. Actions to restrict trade, such as increases in tariffs on goods, or measures that constrain the scope for foreign investors to exploit their competitive advantages, will have effects on all firms and countries that participate in international production networks. The efficient operation of the value chains that drive trade today requires not just low barriers to trade but a stable and predictable policy framework. This extends beyond trade policy – the ability to enforce contracts and protect property rights, including intellectual property, matters for the feasibility of countries to participate in value chains and the willingness of firms to invest in them. The WTO provides a basic framework of rules for trade-related policies, but there also policy areas that are not, or only partially, covered by the WTO. Policies towards FDI and digital trade are two prominent examples.

## 5.1 Preferential trade agreements

An important trend affecting the economic landscape has been the growth in the number of PTAs. Such agreements are allowed for by the WTO. PTAs go further than the WTO in liberalizing trade: applied tariffs on substantially all

trade between partner countries must in principle be reduced to zero (although WTO rules do not require this to be the case for PTAs between developing countries). PTAs increasingly go beyond the removal of border barriers to cover matters not subject to the WTO. Examples include rules governing access for foreign investment, cross-border data flows, the digital economy, and dimensions of domestic regulation (e.g., competition policy; public procurement; regulatory cooperation). PTAs in North America (NAFTA), Europe and East Asia (e.g., ASEAN and related trade and cooperation agreements) have supported the pattern of specialization and rising 'foreign' content of domestic production illustrated in Figure 2.

Recourse to PTAs spans both developed and developing countries. Recent examples of 'mega-regional' PTAs include the CPTPP, ongoing negotiations on an East Asian Regional Comprehensive Economic Partnership (RCEP) that are due to be completed this year,<sup>12</sup> the effort to negotiate a Trade in Services Agreement (TiSA), and the recently signed African Continental Free Trade Area (AfCFTA). Such initiatives are complemented by a plethora of bilateral PTAs, including a large network of agreements negotiated by the EU. Notable recent initiatives that include far-reaching provisions to integrate product markets are the EU's PTAs with South Korea, Canada and Japan. Another important example is the trans-Tasman Single Economic Market established by Australia and New Zealand in 2009.

The steady expansion in the number and average depth of PTAs reflects continued strong interest in international trade cooperation by governments around the globe.<sup>13</sup> Such initiatives illustrate that rules can be agreed on for new issues (as was done in the CPTPP) and that PTAs may provide a catalyst for greater integration through consolidation and gradual expansion of membership. In order to play this role, deeper PTAs should have an open accession clause – that is, permit additional countries to negotiate participation.

PTAs are an important instrument for countries with an interest in reducing barriers to trade and pursuing deeper integration of product markets. They are also a mechanism through which countries may seek to address the structural changes and economic power shifts that have occurred in the last three decades. At the same time, PTAs are discriminatory by design and in effect, generating potential trade diversion as well as steering policy attention away from matters that call for multilateral cooperation. Measures to open regionalism by applying PTA commitments on a non-discriminatory, most-favoured-nation (MFN) basis, as has been done in the ASEAN context, would help ensure that PTAs benefit non-members. But PTAs can only deal with global externalities in a partial fashion. They cannot attenuate the negative economic spill-overs created by national policies of countries that do not participate in them.

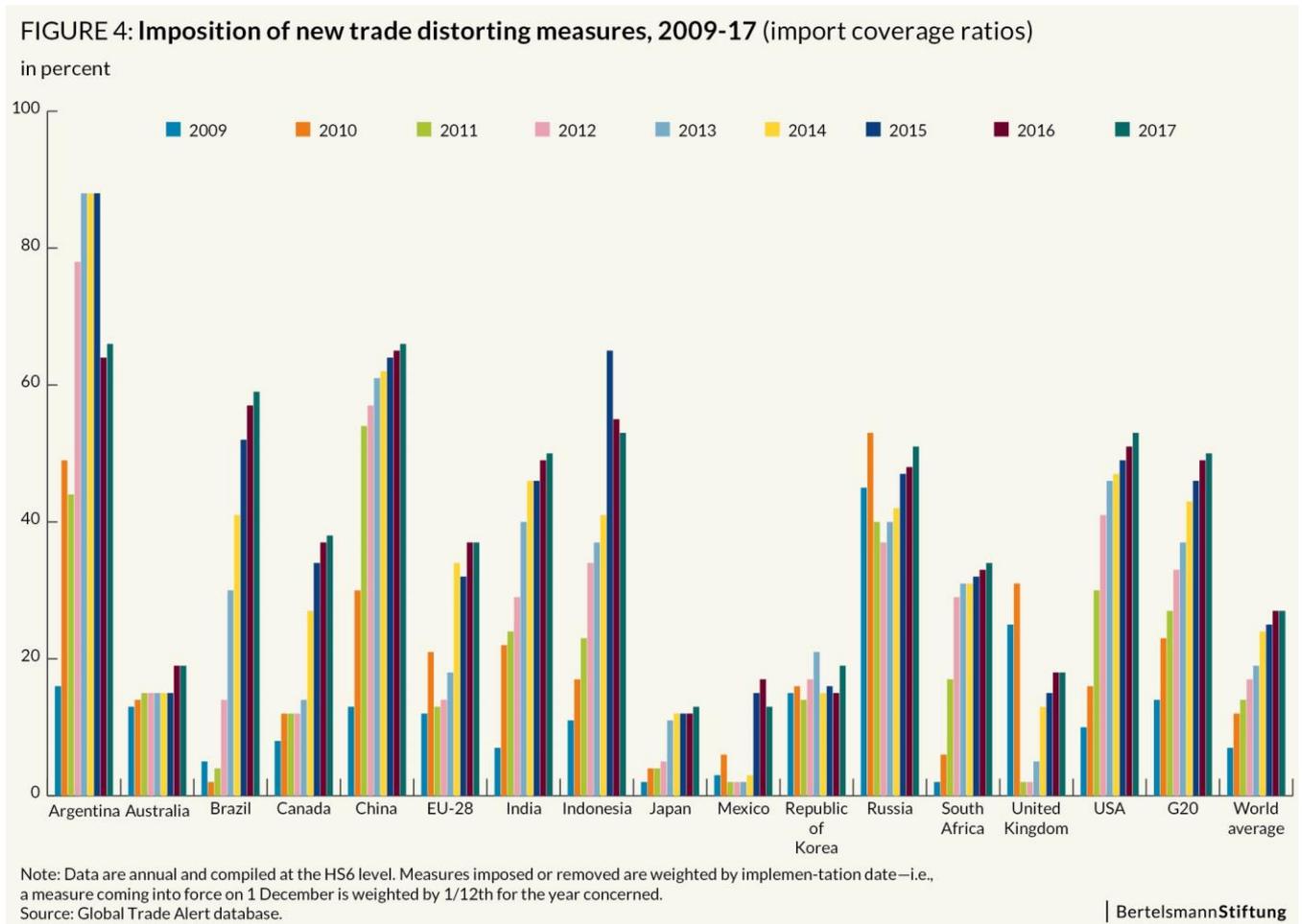
## 5.2 Rising use of trade-distorting policies

WTO trade policy review reports and the Global Trade Alert document the fact that many measures have been imposed by governments since 2009 that potentially distort trade. The trend is worrisome – a significant share of total imports is affected by such measures (Figure 4). Emerging economies and the United States have been the most prolific users of trade policy instruments in the post-2008 period. Other countries have been more restrained but the trend is upwards in many countries.

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<sup>12</sup> There is significant overlap in the membership of some PTA initiatives. For example, seven of the members of the CPTPP are also participating in the RCEP negotiations.

<sup>13</sup> Hofmann et al. (2017) provide a detailed assessment of the coverage of PTAs.



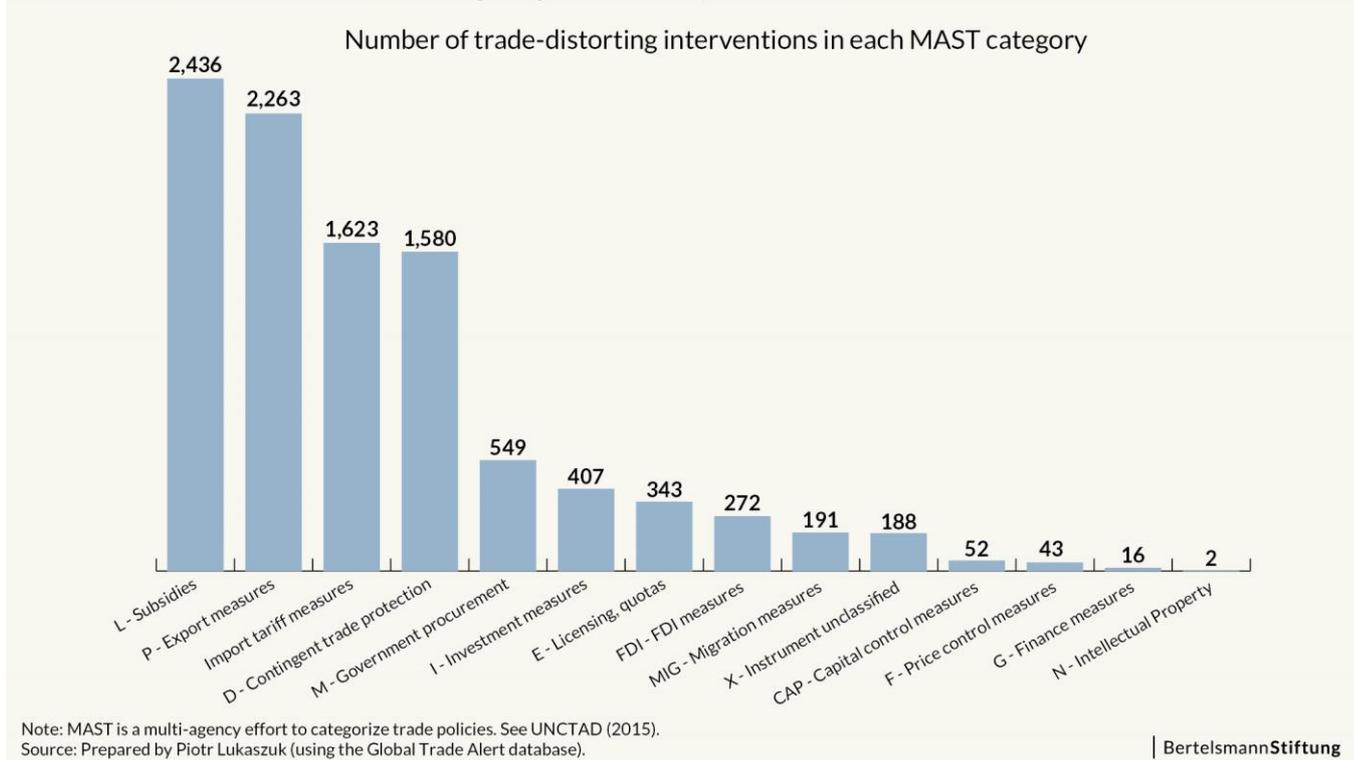
Most of the policy instruments captured in Figure 4 are non-tariff measures. Motivations for the use of such policies vary but a common factor is to support domestic economic activity. This need not be limited to measures that assist national firms. Governments also may seek to attract foreign-owned companies to their territories. Foreign companies are more likely to have high productivity, better technology and stronger innovative capacity than local firms. They also create demand for workers, both skilled and less skilled, thus stimulating local employment. Another motivation that is likely to be common to many countries imposing policies that distort trade – especially trade remedies such as anti-dumping and countervailing (anti-subsidy) duties – is to manage import competition. The use of such measures – the fourth most commonly observed instrument since 2009 (Figure 5) – is permitted by the WTO to respond to what has been collectively agreed (defined) to constitute injurious unfair trade practices.

About half of all trade measures imposed by governments since 2009 take the form of subsidization and support for exports through fiscal incentives of various types. These are only partially covered by WTO disciplines. The same is true for measures such as public procurement and investment incentives.<sup>14</sup> The data reported in Figures 4 and 5 suggest WTO members need to engage in a discussion regarding the international effects of both old and newer types of trade-related policy instruments and the potential need for updating the WTO rulebook. The agenda here includes ‘old’ trade policy instruments that featured on the Doha round agenda – tariffs, other border barriers and agricultural support measures. These instruments account for a significant share of observed measures and are important to many developing nations.<sup>15</sup> But the main message of Figure 5 is that various forms of domestic subsidies are among the most frequently used trade-distorting instruments.

<sup>14</sup> Members of the plurilateral Agreement on Government Procurement are subject to rules on procurement; other WTO members are not.

<sup>15</sup> Some policies that matter significantly for many developing countries – e.g., agricultural support policies and tariff escalation – would have become subject to more stringent disciplines if the Doha round had been concluded.

FIGURE 5: Global use of trade-related policy instruments, 2009-2017



### 5.3 Measures affecting digital trade

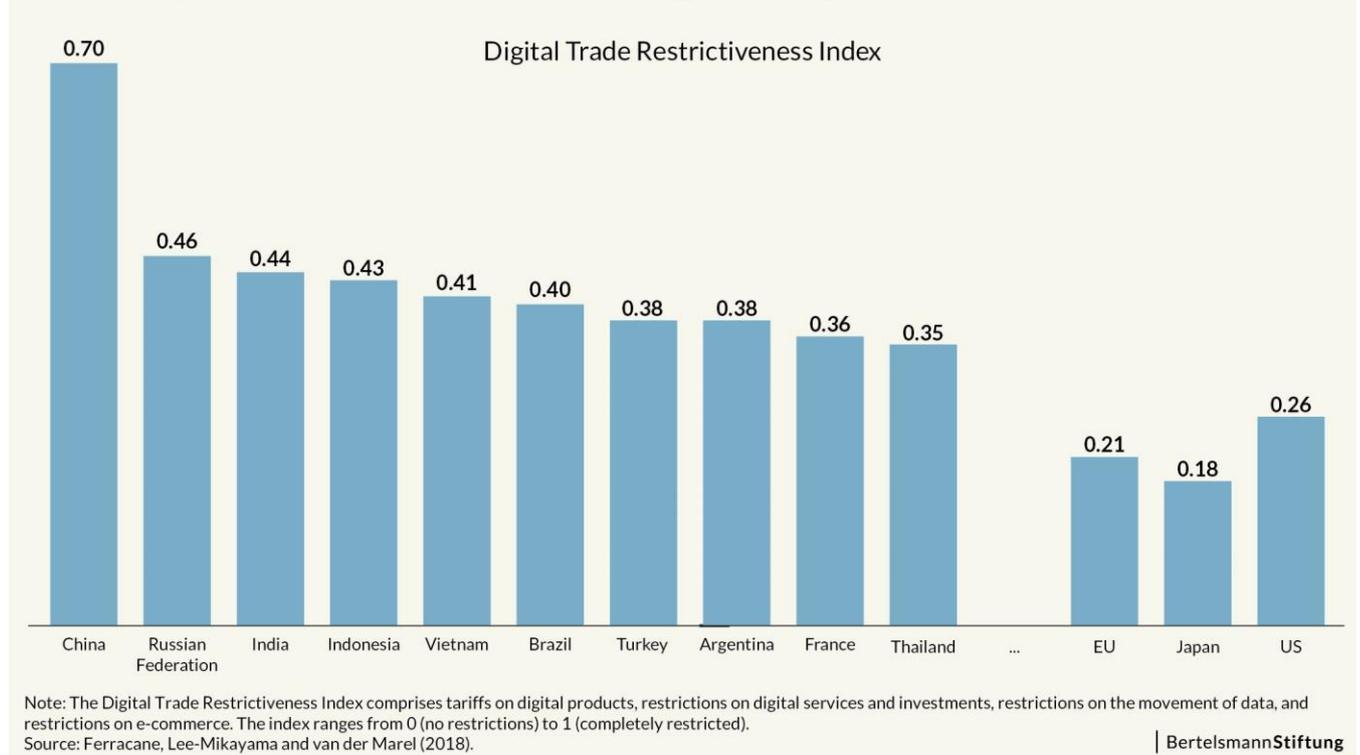
An area of trade policy that is of increasing salience is measures affecting trade in digital products and services. Cross-border digital transactions are growing rapidly and, going forward, will comprise an increasing share of global production and trade. The data on trade policy trends discussed above include many measures that affect digital trade but are oriented more towards policies that affect production and trade in goods. A recent effort to assess the policy stance of countries towards digital trade by Ferracane, Lee-Mikayama and van der Marel (2018) reveals great variation in the extent to which countries implement policies that inhibit digital trade. Large emerging economies maintain more restrictive policies than OECD member nations (Figure 6). Many of the policies concerned are only partially covered by WTO agreements. These policies can have significant negative spill-overs on trade and call for multilateral cooperation to devise efficient regulatory approaches that facilitate digital trade while attaining national objectives regarding consumer safety, data privacy and national security.

More generally, services account for upwards of three-fifths of GDP and employment in higher-income countries. On average, one third of the value of globally traded goods reflects services inputs. An implication is that the competitiveness of firms depends on the productivity performance of services sectors, which in turn is affected by prevailing services trade policies. Restrictions on trade in services are often higher than barriers against trade in goods (Borchert, Gootiiz and Mattoo, 2014). To date, the WTO has done very little in this area, as the priority was given in the Doha round to policies distorting trade in goods – a decision that arguably was a factor undermining the negotiations.<sup>16</sup> In the case of e-commerce and internet-enabled transactions WTO members have periodically committed not to impose customs duties on electronic transmissions, but little progress has been made on rules of the road for domestic regulation that negatively affects the efficiency of the digital economy and the ability of foreign

<sup>16</sup> One consequence of the decision to sequence the negotiations to put agriculture and non-agricultural market access issues first, little attention was given to services, reducing the incentives for firms accounting for most employment and economic activity in higher-income countries to lobby for a Doha Round outcome, including on agriculture. This led a subset of countries to decide in 2013 to engage in negotiations to establish a Trade in Services Agreement (TiSA) outside the WTO. These talks made substantial progress in developing an expanded set of rules for services policies but were put on hold in 2017 by the Trump administration.

firms to provide services. As the world economy becomes ever more interconnected because of the “Internet of things”, e-commerce and cross-border trade in services, cooperation on policies that affect digital trade and data flows will become more important for firms and consumers.<sup>17</sup>

FIGURE 6: Digital trade: Ten most restrictive countries, plus the EU, Japan and US



## 6 Adjustment pressures and differences in social preferences and economic systems

Trade expansion has supported rising average levels of national income, improvement in human development indicators and reductions in poverty headcount ratios. But not everyone has benefited equally and some have been adversely affected. The gains from trade are only realized because of painful adjustments incurred by firms that cannot compete with more efficient or innovative foreign enterprises. Workers in firms and industries that are not competitive must find alternative employment in more dynamic firms and sectors or accept lower wages. Such adjustment pressures are not just due to trade or globalization more broadly defined. New technologies continuously impact on labor markets by changing demand patterns and the organization of production. Some technologies may have negative impacts for workers in non-tradable jobs (e.g., domestic transport), others may make formerly non-tradable jobs subject to international competition. Looking forward, technical change may generate more “off-shoring” of tasks as products are digitized and exchanged cross-border as trade in services. This will generate new employment opportunities as digitally-enabled activities expand, but not all workers will be able to transition to new jobs without assistance.

<sup>17</sup> A feature of the Internet of Things, 3D printing and related technologies is that they blur the contours of regulatory framework applying to different services that may be provided using the same technology platform. This has implications for regulatory frameworks, calling for more cooperation amongst regulators from different countries.

The transitional costs of adjustment can be very significant for affected workers, households and communities.<sup>18</sup> There are strong reasons for governments to respond to such costs. The displaced workers who incur the costs of adjustment are producing the gains associated with policy change and technical change and for that reason warrant assistance. It is well understood that governments must put in place compensation mechanisms for market opening to make everyone better off. Such compensatory policies need not detrimentally affect national competitiveness vis-à-vis countries that do not so, if they are designed to enhance the ability of workers to meet the changing demand for skills by employers. In practice, estimates of the extent to which formal trade adjustment assistance and other transfer programs offset losses suggests that the offset is substantially less than complete (Claeys and Sapir, 2018).

Lamy (2009) has pointed to a 'Geneva consensus' that the focus of policy should be on domestic and international policies to "help translate more open trade into real, increased and perceived benefits" for citizens. From the perspective of the WTO and the global trade regime it is essential to note that compensation is a matter for domestic policy. Given that trade is just one source of adjustment pressure – technological change and macroeconomic fluctuations are more important – income insurance and appropriately structured active labour market policy are called for. Domestic social policies across countries vary in their effectiveness in providing safety nets and assistance to find alternative employment. In practice, most governments have relied on economic growth to generate jobs for those negatively impacted by globalization. Post-2008 such growth has been anaemic – in part because of the trade policy responses captured in the data discussed above (IMF, 2016). Slow growth has in turn helped to generate political opposition to trade agreements and the WTO as visible embodiments of globalization.

Disquiet about the effects of globalization is not a global phenomenon – most citizens in developing countries tend to be more positive about globalization (Bluth, 2018). In high income countries, drivers of discontent are varied. Many have little to do with the policy areas spanned by the WTO. Concerns relating to migration, tax avoidance by large multinational companies, financialization of the economy, the treatment of foreign investors (e.g., opposition to bilateral investment treaties that permit foreign investors to contest regulatory changes adopted by host governments) are all policy areas that are only partially covered by the WTO, if at all. Trade arouses less concern among citizens in developed and developing countries than do other dimensions of globalization (Bluth, 2018).

This does not mean trade and the trade regime do not raise concerns. Of increasing import are views that firms based in foreign countries with weaker regulatory standards or that benefit from competition distorting policies may engage in unfair trade. Such perceptions are not restricted to the context of trade between high-income and developing nations. They were a significant factor in mobilizing resistance in the EU against trade agreements with Canada and the US, i.e., countries with similar levels of per capita income and regulatory standards. They illustrate that consumer preferences are an important factor in the design of cooperation on trade-related policies.

The WTO leaves countries free to define for themselves the goals of their regulatory regimes, subject to measures being implemented on a non-discriminatory basis, not unnecessarily restricting (distorting) trade and conforming to procedural criteria that have been agreed by all Members (e.g., relating to transparency). Notwithstanding this, perceived threats to regulatory sovereignty and worries that governments may be constrained in their ability to enforce or change domestic health, safety, labour and environmental regulations underpin the concerns many civil society organizations have regarding the operation of the trade regime and efforts to deepen trade cooperation. They are also a factor underlying perceptions by businesses that they confront 'unfair' competition from firms located in countries deemed to have 'lower' standards.

Likewise, many developing countries fear that product standards and related regulatory disciplines applied in import markets may be used to create obstacles to their exports. This explains opposition to efforts to extend the reach of the WTO to encompass disciplines on political and civil rights, labour standards or protection of the environment – a direction of travel that is embodied in the trade strategies of many higher-income countries and reflected in recent PTAs these countries have negotiated. In the case of nonreciprocal trade preferences, linkages between duty-free access and social and environmental standards regulation are now common, viz. the GSP+ regime applied by the EU.

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<sup>18</sup> What follows draws on Hoekman and Nelson (2018).

Such linkage is a contentious matter in the WTO and has been the subject of decades of debate. Most developing countries have taken the view that the WTO, as a trade organization, is not the right place to negotiate on political, civil and social rights. Regarding their effects on competition, many developing countries also argue against this "burning the bridge after crossing the river" – noting that high-income country proponents were not subject to international disciplines when they industrialized. Concerns that "unfair competition" arguments are a disguised manoeuvre to deprive lower-income economies from benefitting from their comparative advantages have been a prominent feature of developing country perspectives on this matter. Thus, many countries have opposed efforts to agree to WTO rules pertaining to labour or environmental standards, although bodies have been created to discuss some such matters – e.g. the Committee on Trade and Environment.

Concerns about safety, sustainability or social conditions in workplaces where imported goods are produced have been augmented as a result of the spread of complex international value chains. These entail a need for national regulators to cooperate more with foreign counterparts. Similarly, worries about the way intangible products are produced and traded (transmitted) through global information and telecommunications networks call for cooperation to ensure efficient realization of national regulatory objectives. Such cooperation can lower trade costs for firms as a side benefit, but their primary driver is to achieve more effectively non-trade objectives. An important question is whether and how the WTO can help support such 'win-win' regulatory cooperation. This may only be feasible among subsets of the WTO membership – a matter we return to below.

The trade order embodied in the WTO presumes trade is undertaken by firms that operate on a commercial basis. No matter what type of economic system prevails in a country, firms may seek and obtain support from governments that distort competition and trade. This has led to the negotiation of rules to govern such assistance, reflected in different WTO agreements – e.g., the Agreements on Subsidies and Countervailing Measures and on Trade-related Investment Measures. The presumption, however, is that firms are free to operate their businesses as they see fit, that is, trade rules were designed to regulate relations between private agents that pursue only commercial interests. The accession to the WTO of countries where state-owned enterprises account for a significant share of economic activity tests this central presumption.

Whether and how the trade regime should govern the policies of countries where the State plays a significant role in the economy has become a prominent question for many WTO members. Although China is the primary focal point in this regard, other countries also have economies where State influence or control is substantial. More generally, governments use a mix of policy instruments that affect competition on markets – including subsidies or fiscal incentives to attract or retain investment. This is not a new question for the trading system or for trade agreements, but it is one that is particularly important to address to reduce current trade tensions. As discussed below, doing so requires policy dialogue with a view to identifying the magnitude of negative effects of specific policies and approaches that reduce potential adverse impacts on foreign producers and distortions to competition.

Differences in policy choices, preferences, standards and economic systems more broadly are not the only source of potential trade tensions. It is sometimes argued that macroeconomic policy stances are another factor that determine whether a country's trade relationships are equitable. Macroeconomic policies, including fiscal and monetary policies that impact on the government budget and influence patterns of saving and investment, may be reflected in trade and current account balances. Arguments that large bilateral trade imbalances are an indicator that a trading partner is engaging in practices that distort trade flows is misconceived. Countries have different comparative advantages. These give rise to the gains from trade.

Countries with comparative advantage in a specific industry will be net exporters of the products of that industry, and net importers of goods and services in which they have a comparative disadvantage. Adding up across all industries and products, this may result in bilateral surpluses or deficits. Views that fairness requires trade to be balanced across all bilateral flows or that to benefit from trade a country must have a bilateral trade surplus are misguided. Moreover, a country's overall current account balance is not affected by trade policies but by its macroeconomic policies and how these impact on national savings and investment. Countries that in the aggregate save more than they invest (or consume less than they produce) will run current account surpluses. The size and

sign of both bilateral trade balances and the overall trade balance is not informative about the welfare impacts of trade.<sup>19</sup>

## 7 Three specific trade governance issues

The open, rules-based multilateral trading system plays an important role in providing the supportive environment needed for firms to exploit international market opportunities, while at the same time establishing rules of the game that assure that governments can provide the public goods and services demanded by their citizens. As noted previously, the WTO does not have free trade as a goal. It is an instrument through which governments agree to rules of the game for trade policy. This extends beyond agreeing to upper bounds on permissible tariffs, providing information on applied trade policies, and treating foreign products in a non-discriminatory manner. A key motivation for agreeing to multilateral disciplines is to improve the access of firms to foreign markets, but more important from a welfare perspective is the role of the WTO as a governance and conflict management mechanism. A major focus of WTO provisions and processes is to enhance the transparency and predictability of applied trade policies, thereby reducing uncertainty for traders and other governments. Independent, compulsory dispute resolution takes power out of the equation.

A reversion towards unilateral use of trade policies that violate commitments made by countries in the WTO in conjunction with the possible demise of independent adjudication of trade disputes will raise risk premia associated with investments in tradable activities. This in turn may induce companies to shift away from a strategy of global sourcing to one that is anchored in specific regions where trade is governed by PTA disciplines. To some extent this may already be happening. OECD data indicate that the rate of return on FDI has been falling in the post-2008 period (OECD, 2017), which may be one factor inducing a shift towards reshoring of production and shortening supply chains.

If reshoring is driven by changes in relative costs, for example increasing real wages in countries where assembly operations occur, or technological change, for example the feasibility of substituting workers with robots, it will be efficient. This is not the case if it is induced by policy measures that are designed to increase trade costs. The data on post-2008 use of trade policies summarized above suggests there is a rise in trade-distorting measures used by governments. A reversal in global value chain-based business models that is driven by protectionist policies will reduce efficiency. It will result in higher costs of inputs and higher prices for consumers. As already noted, the costs of such a reversal will be greatest for developing countries.

The WTO agreements provide significant latitude for WTO members to use trade policy instruments, e.g., permitting action to be taken against dumped or subsidized imports that injure domestic industries. A key feature of WTO membership is that governments agree to follow negotiated rules and procedures. Examples include encouraging the use of relevant international standards to achieve health, safety and related objectives. Trade defence instruments such as anti-dumping, countervailing duties (measures to offset the effects of subsidies provided to foreign suppliers of an imported product) and safeguard actions play an important role in helping governments to manage the pressures that accompany globalization and technological change. All WTO Members have agreed that certain types of foreign trade, if it causes injury to domestic industries, may be countered with import tariffs on a temporary basis. However, this is subject to following specific procedures laid out in WTO agreements that have been negotiated over time with a view to preventing abuse of these instruments.

The data summarized in section 5.2 – in conjunction with increasing threats to take action against countries deemed to engage in unfair trade practices – illustrate the need for the WTO to reflect on whether and where the rulebook may need to be updated. Such updating, while challenging, is urgently needed and feasible. WTO members have demonstrated the ability to innovate and cooperate on trade matters. Examples include the expansion of product coverage of the ITA in 2015, the 2013 Agreement on Trade Facilitation, and the agreement to ban agricultural export subsidies. Outside the WTO one can point to the continued pursuit of PTAs to illustrate both willingness and ability of governments to deepen cooperation on trade-related matters.

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<sup>19</sup> See World Economic Forum (2018) for greater discussion of the various misconceptions that exist around trade imbalances.

WTO members vary in the importance they attach to efforts to define new or updated rules for different policy areas. Some issues – such as excess capacity in the steel industry – are sector-specific. Others are ‘horizontal’ in that they affect many industries – such as fiscal measures that promote exports or state aids (subsidies) that distort competition. A precondition for engaging in efforts to update or establish new rules for a policy area is that countries have established what matters to them. Not all countries have clarity on this question. In part this is because the focus of attention has been on the Doha agenda for the last 15 years. In part it is because poorer countries have less capacity to be fully informed. As discussed below, a process of deliberation under the umbrella of the WTO to assess the economic effects of different types of policies on trade and investment can help establish where policies raise legitimate concerns for trading partners.

Any effort to update the rulebook must confront three issues: (i) the implementation and operation of the Dispute Settlement Understanding; (ii) addressing economic development concerns (recognizing the extensive heterogeneity in circumstances and capacity across the membership); and (iii) some of the working practices of the WTO.

## 7.1 Dispute settlement

A fundamental feature of the WTO is the dispute settlement system. This is unique among inter-governmental treaties in comprising compulsory third party adjudication. It involves a two-step process. Panels of independent practitioners are tasked with assessing allegations of violations of WTO commitments by a WTO member. Parties to a dispute may subsequently appeal panel findings to an Appellate Body (AB). Over 500 disputes have been adjudicated since the establishment of the WTO in 1995, with judgments mostly implemented by the losing party (WTO, 2017a). If a WTO member decides not to comply with rulings, the parties that brought the case will be authorized to retaliate, up to a maximum amount of trade that is determined through an arbitration process.<sup>20</sup>

A key objective of many countries in acceding to the WTO (and accepting a significant expansion in the coverage of multilateral disciplines on trade policies, including services and requirements to protect intellectual property), was to reduce the prospects of confronting ‘aggressive US unilateralism’ (Bhagwati and Patrick, 1990). This was achieved — since 1995 the US has worked through the WTO to challenge foreign trade practices covered by the WTO agreements. Moreover, small countries have successfully challenged the policies of large nations. The track record of cases brought forward and compliance with rulings suggests that the system has been effective (e.g., Sacerdoti, 2017).

This achievement does not mean all countries are happy with the system. The United States has been particularly critical of how the Appellate Body functions (USTR, 2018).<sup>21</sup> This was reflected in the 2016 decision by the Obama Administration to oppose reappointment of an Appellate Body member. As noted previously, the Trump Administration has taken this approach further and to date has blocked all new appointments. Other members have also raised concerns regarding the consistency and coherence of Appellate Body rulings, as have assessments of the case law by scholars (e.g., Mavroidis, 2016b). In our consultations for this report several practitioners also pointed to the potential ‘chilling’ effect of WTO dispute settlement procedures – including reasoning by the Appellate Body – on the willingness of some WTO members to engage in deliberating new issues. How significant this is as a factor impeding dialogue is difficult to determine but it suggests there is value in an open discussion of its salience and what can be done to address such concerns.

The long-running review of the functioning of the Dispute Settlement Understanding (DSU), which commenced in 2001, has generated numerous proposals for improving and clarifying dispute settlement procedures and processes. The need for consensus has prevented any such proposals from being adopted. After more than twenty years there are lessons to be learned from the track record to date. Resolving the current conflict on the Appellate

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<sup>20</sup> See e.g., Mavroidis (2016a).

<sup>21</sup> One source of US dissatisfaction is that the Appellate Body has not adopted the deferential standard of review regarding the use of so-called zeroing methodologies in antidumping investigations that the US believes it had obtained agreement on at the end of the Uruguay round negotiations. Other concerns tabled by the US include disregard for the 90-day deadline for appeals, continued service by persons who are no longer Appellate Body members, issuing advisory opinions on issues not necessary to resolve a dispute, review of facts, and claims by the Appellate Body that its reports are entitled to be treated as precedent. See USTR (2018, pp. 22-28).

Body is an urgent challenge confronting the WTO membership that should be placed in the context of a broader debate on improving conflict resolution procedures as well as other ways to address tensions without invocation of formal dispute processes. The various WTO bodies offer a venue to discuss concerns and find solutions without recourse to formal litigation – this has been done to good effect in committees dealing with product regulation. Even abstracting from the current crisis pertaining to the Appellate Body, the WTO dispute settlement system is already under considerable strain. More attention is needed to utilizing other mechanisms to prevent and resolve disputes outside the DSU.

## 7.2 Economic development

An important factor underlying the difficulties experienced in using the WTO as a platform for negotiations and efforts to update its rulebook is insistence by many developing countries that provisions in WTO agreements aimed at promoting economic development are implemented. Specifically, these nations want to be able to use trade policies to promote economic growth, even if these have adverse consequences for trading partners. The engagement of many developing nations in the WTO has been premised on ‘special and differential treatment’ (SDT). This entails less than full reciprocity in trade negotiations and acceptance that developing nations should be less constrained in the use of trade policies than high-income countries.

The rules of the game for trade policy embodied in the WTO are motivated by the objective of reducing the negative effects of protectionist measures for trading partners. A large body of economic analysis suggests that reducing trade barriers will benefit primarily consumers – including firms – in the country that liberalizes, in addition to exporters in foreign countries. But many countries are of the view that sheltering domestic industries from international competition may be necessary for some time, permitting firms to learn from experience, become efficient and bolster their capacity to contest the market. They argue that (more) space to use trade policies is needed for their economic growth and industrialization. Opponents argue this will do little to achieve development objectives and that other policies are needed. This debate on the utility of ‘policy space’ to use trade-distorting measures to pursue economic development objectives is relevant to all WTO members, given trends noted in Section 4.2 of this report.

There is an inherent tension between the national welfare benefits that accrue from making binding (enforceable) trade policy commitments in the WTO and the associated constraints on the ability of governments to assist domestic industries by restricting imports of goods and services or supporting exports of domestically produced goods. A loss in ‘policy space’ is the price that WTO members pay for other countries to undertake trade policy commitments and to comply with the procedural disciplines that have been negotiated over time. If countries could freely (re-)impose trade barriers or increase their support to domestic exporters there would be no value in WTO membership. The multilateral disciplines that constrain the use of trade policy are particularly important for small countries that do not have the power to prevent large economies from shifting the terms of trade in their favour by restricting imports or subsidizing exports. Reducing the policy space of large trading powers is a core dimension of the value added generated by the WTO for small countries. Such constraints benefit all countries, large and small.

A central feature of SDT is that it applies to all developing countries. The WTO, following precedent set under the GATT, does not define what constitutes a developing country, leaving it to members to self-determine their status. Outside the group of 47 (UN-defined) LDCs, the only distinct group of developing countries identified in the WTO, there are no criteria that allow differentiation between developing countries. In general, upper middle-income countries that have become competitive exporters, and nations that have large and rapidly growing economies, can claim the same SDT privileges as small lower-income countries that are not classified as LDCs. That said, in practice differentiation has been agreed on an issue-specific basis. An important example is the classification of developing countries based on per capita GDP and export competitiveness in Article 27 of the Agreement on Subsidies and Countervailing Measures. As part of the Doha round negotiations, several draft texts made distinctions between developing countries and included different categories for SDT.

All WTO members agree differences in economic capacity and levels of development should be recognized in the design and application of trade policy commitments. But many WTO members also argue that greater differentiation is needed between developing countries. The fact that some developing economies constitute (very) large markets and have become export powerhouses – most notably China – has led many Members to argue that SDT should not apply to more advanced developing economies. The latter do not necessarily oppose more obligations for

themselves but reject efforts to re-define or establish categories of developing country members that “graduates” them in effect out of the developing countries categorization. This is regarded as a sensitive political issue.<sup>22</sup>

As noted by Lamy (2013), the challenge is to “find a new balance between reciprocity and flexibility in a multidimensional membership [to be able] to deliver on multilateral trade opening.” Such a balance needs to differentiate between policies applied at the border (traditional trade policy instruments) and policies of a regulatory nature – so-called behind-the-border policies. There is extensive evidence and research demonstrating that the latter types of policies and associated institutions matter greatly from a development perspective. Behind-the-border policies will play a major role in determining whether firms have access to the intermediate inputs they need and whether and how foreign companies decide to invest in production facilities.

An inability to satisfy international product quality standards or to obtain certification of production processes may be a binding constraint impeding export growth. Policy coordination failures may impede investments needed to connect domestic firms to global value chains or result in higher transactions and operating costs for firms, reducing their international competitiveness. There are good arguments that addressing these types of factors should be prioritized. To support development, policies must address specific market failures that impede or distort investments. Examples of such market failures are capital market imperfections, coordination failures that result in missing input markets, agglomeration externalities and information asymmetries that preclude trade from taking place.

There is an extensive literature that makes a compelling case for government action to address such market failures by supporting processes of ‘self-discovery’ (Hausmann and Rodrik, 2003) by innovative firms to learn whether ideas they have for new products are viable, to allow the realization of dynamic economies of scale through learning by doing and identify potential opportunities in export markets. Policy instruments that may help do this include effective exchange rate management (Rodrik, 2008), a supportive investment climate, targeted subsidies for domestic investment (including inward FDI), creation and operation of export development zones where the government provides infrastructure (Moran, 2014) or export promotion activities that help firms sell to new markets (Olarreaga, Sperlich and Trachsel 2017).

Some of these policies are subject to WTO rules. Others are not. The focus of the WTO is on measures that affect products when they cross borders. Such measures – trade policies – generally will do little to address the types of market failures prevailing in low-income countries. These call for domestic interventions targeting the source of the market failure. This presumption has become stronger in light of the changes to the organization of the global economy discussed in Section 4.1. Imposing high(er) barriers to trade makes little sense from a development perspective in a world of international production networks as it raises the costs of imported intermediates needed to be able to export products. The constituent elements of SDT date back to the mid-1960s and were designed for a world economy that no longer exists.

The challenge today is to identify and implement policies that promote economic development in a world of global value chain-based production, e-commerce and digitalization where small firms can become micro-multinationals by using electronic platforms and exploiting mobile information and communications technologies. Capacity constraints that impede the scope for poorer developing countries to identify, implement and benefit from such policies are an important dimension of this challenge. Such policies will not revolve around tariffs but centre on measures that enhance access to finance, technologies, cross-border payments systems and efficient logistics.

Changes in the structure of global production have made traditional trade barriers much less effective instruments to assist domestic firms – helping to explain why other types of policies increasingly are being used by countries (viz. Figures 5 and 6). An implication is that attention should be given to understanding the effectiveness of such policies in attaining their objectives and determining to what extent they give rise to significant negative spill-over effects for trading partners and should be subject to multilateral rules. This is something that concerns all WTO members. All countries have disadvantaged regions where the incidence of poverty is higher than average or where employment opportunities are scarce.

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<sup>22</sup> Concerns about special and differential treatment do not split neatly into developed vs. developing countries or traditional North-South lines. For example, middle-income countries that do not benefit from the type of duty-free access to OECD member country markets accorded to the LDCs are negatively affected by tariff escalation that impedes their ability to add value to their exports.

This does not mean that trade policies are not relevant to economic development. Specific Doha round agenda items are legitimately regarded by countries as very relevant from a development perspective – tariff escalation in large import markets that constrains movement up the value chain is an important example; subsidies for agricultural production that distort international competition another. Developing countries have a strong case for insisting on stronger multilateral disciplines on such policies. But this should be complemented by a willingness to re-think SDT. Rather than continuing to fight old battles, it would be more productive to do more to identify where specific WTO rules impede the implementation of policies that would enhance their economic welfare and engage in a process to identify good practices and policies to address market failures. This should be complemented by provision of assistance where needed. An important step forward on the latter front was the launch of the Aid for Trade initiative in 2005 and the Enhanced Integrated Framework to assist the LDCs. These programs reflect a common recognition that more needed to be done to bolster supply side capacities and capabilities of firms in developing countries to benefit from trade opportunities

As discussed subsequently, deliberation on how WTO rules affect economic development could commence at the level of the various WTO committees, under the overall auspices of the Committee on Trade and Development. This will require both open and constructive policy dialogue, something that all governments arguably have an interest in. The building blocks for a renewed approach towards economic development are already largely in place. WTO members already pursue issue- and agreement-specific approaches to addressing specific development concerns. These have included agreement to exempt certain developing countries or to differentiate between developing economies. Examples include the Agreement on Subsidies and Countervailing Measures, negotiating texts that were on the table in the Doha round on agricultural and non-agricultural market access, and the TFA.

The flexible approach taken in the TFA towards scheduling of commitments by developing countries and the opportunity it offers for developing countries to link implementation to technical assistance. In such cases, TFA provisions cannot be invoked in dispute settlement proceedings until such assistance has been received and the relevant provisions have been fully implemented. The TFA experience suggests an issue-by-issue approach aimed at building a common understanding on what types of policies make sense (constitute good practice) is in principle feasible. This is a core feature of the TFA – all WTO members agreed on its substantive provisions, reflecting the outcome of a long process of dialogue that was informed by national experiences and inputs from specialized international agencies such as the World Customs Organization.

### 7.3 WTO working practices

A common denominator underlying the failure of the Doha round, the inability to launch discussions on new policy areas, and the impasse on appointments to the Appellate Body is a basic WTO working practice: consensus. The WTO is founded on the principle that all members are equal in rights and obligations. While consensus is primarily a practice and not a formal rule – the WTO makes provision for voting – in practice voting does not occur, reflecting a widely held view this would undermine the legitimacy of WTO decisions.<sup>23</sup> Consensus is deeply ingrained and strongly supported by the membership. It is part of the culture. Countries – large and small – rely on the consensus practice as a guarantee that they cannot be forced to accept obligations which they do not deem to be in their interest. Consensus ensures that all WTO members have an equal opportunity to make their points and can withhold support until they see their interests and concerns accommodated.

Many proposals for WTO reform have focused on the consensus norm, based on the diagnosis that consensus is a source of inefficiency and deadlock, impeding a majority from moving forward on an issue and giving excessive scope for a small minority to block a decision (e.g., Steger, 2009). At the same time, there are strong arguments

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<sup>23</sup> There are WTO provisions in which consensus is specified as the decision-making rule, e.g., Art. X:9 on amendments to include new Annex 4 Plurilateral Agreements. Art. IX WTO specifies that if voting occurs, unanimity is required for amendments relating to general principles such as non-discrimination; a three-quarters majority is needed for Interpretations of provisions of the WTO agreements and decisions on waivers; and a two-thirds majority for amendments relating to issues other than general principles. Where not otherwise specified and consensus cannot be reached a simple majority vote is sufficient. Art. X provides that a member cannot be bound by a vote on an amendment that alters its rights or obligations and that it opposes. In such instances the Ministerial Conference may decide to request that the member concerned withdraw from the WTO or to grant it a waiver.

why this is a beneficial working practice when it comes to the negotiation of new commitments, given the very large asymmetries in size and power across WTO members and vast differences in per capita incomes, capacity and economic interests. Consensus is a mechanism to ensure that the eventual results of negotiations are acceptable to all members, ensuring the legitimacy and ‘ownership’ of the WTO by governments and domestic polities of members. Developing countries are particularly strong supporters of the consensus practice as it provides them with some assurance that they will not be confronted with decisions that may be detrimental to their interests.<sup>24</sup>

A downside of consensus is that it also applies to the normal operations of the WTO, i.e., activities that have nothing to do with negotiations. Such normal operations include agreement on the agenda of Committee meetings, proposals to have a discussion on a trade policy-related matter, or suggestions to invite independent experts to provide inputs on a subject that is directly relevant to the implementation of a WTO agreement. The consensus practice may allow even a small minority to try to block a majority that supports such suggestions. This is detrimental to the credibility of the organization.<sup>25</sup> While it can be argued that it can be a problem if consensus is used to stop a majority from moving forward to adopt new rules on a matter, it is a much more serious problem that consensus can be (and is) used to preclude discussion and deliberation, such that even exploratory discussions on matters of interest to some members are opposed by other members. This is dysfunctional and creates incentives for proponents of new ideas to negotiate PTAs, fragmenting the trading system. Blocking substantive deliberation is inimical to the collegial spirit that should prevail in international cooperation (Torres, 2017a,b).

Efforts to fundamentally change the governance of the WTO have no chance of success, whatever one’s views of their desirability. At the same time, it must be recognized that the consensus practice has impeded the effectiveness of the WTO as an institution. Given differences in preferences and priorities across countries, not all issues are of interest to all WTO members. Cooperation among groups of WTO members on an issue-specific, incremental basis where the intent is to apply whatever may be agreed to all WTO members offers a partial solution to the current malaise. It constitutes a potential mechanism for proponents to cooperate on policy areas where free riding is not a concern – i.e., subjects where it does not matter to participants if agreement to adopt certain policy disciplines or practices is not adopted by countries that decide not to sign on to them. Insofar as a subset of the WTO membership is willing to incur additional commitments and apply these to all WTO members on a non-discriminatory basis, there is no need for consensus. The group of WTO members concerned can simply incorporate what is agreed into their GATT schedules and/or their commitments under the General Agreement on Trade in Services (GATS) (Hoekman and Mavroidis, 2017).

In what follows we shall refer to such non-discriminatory agreements between a subset of the WTO membership with the term open plurilateral initiatives – open because the presumption is that any WTO member can participate if it desires to, whether as part of the group that initially agrees to pursue cooperation on a matter, or after the establishment of an agreement.<sup>26</sup> Such initiatives should be distinguished from formal ‘Annex 4’ Plurilateral Agreements such as the Agreement on Government Procurement. The latter apply only to signatories and require the approval of all WTO members to be incorporated into the WTO. In what follows the term open plurilateral initiatives spans only arrangements where there is no discrimination against non-participating countries.

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<sup>24</sup> Four types of proposals have been made in previous reports and the trade policy literature to address the downsides of consensus as a working practice. The first is to introduce procedural changes that would require Members blocking adoption of a measure in instances where the majority is in favour of proceeding to explain why they are doing so (Sutherland, 2004). A second is to adopt a plurality criterion, described as “a practice where countries refrain from blocking consensus when a critical mass of countries supports a proposed change. This critical mass of countries could be expressed as an overwhelming majority of countries and an overwhelming amount of the trade weight in the world, such as 90 percent of both of these factors” (Jackson, 2001: 74-75). A third proposal is to create an Executive Board or Committee and emulate the management structure of the IMF or World Bank, in which a Board of 20 to 30 representatives is given decision-making powers. The fourth suggestion is to create an advisory, consultative body to engage in strategic thinking and help to set priorities to further the mandate of the WTO (Blackhurst and Hartridge, 2004; Sutherland, 2004; Steger, 2009).<sup>24</sup> None of these proposals have attracted much support. As noted in Lamy (2009), there is a consensus about consensus among WTO members.

<sup>25</sup> Prominent examples include the United States refusal to approve new Appellate Body appointments and the July 2014 decision by India to block adoption of the Protocol incorporating the TFA into the WTO, despite having agreed to the TFA six months earlier at the 2013 Ministerial conference in Bali. India took this action to generate pressure on WTO members to address its concerns regarding WTO rules on agricultural production support policies. Such ‘hostage-taking’ erodes trust and undermines incentives for good faith efforts to engage on substantive dialogue on matters of common concern.

<sup>26</sup> Open plurilateralism as an organizing concept is an element of the Government of New Zealand’s trade policy strategy. See Vitalis (2018).

In thinking about the scope for open plurilateral approaches to rule-making it is useful to distinguish between national policies that differentiate between national and foreign products (producers) and those that in principle apply equally to domestic and foreign economic actors. Discriminatory policies generate negative spill-overs on trading partners by design. Examples are import tariffs and services investment restrictions. Efforts to reduce such barriers are likely to be affected by free riding concerns and require that many countries participate in an agreement to reduce them – a ‘critical mass’. Experience suggests that countries accounting for 80-90 percent of total trade in the associated products may need to participate for a subset of the WTO membership to agree to liberalize trade in cases where free riding is a concern.

Policies that apply on a non-discriminatory basis, no matter the origin of a product or producer, may also generate negative spill-over effects, but this will mostly be unintentional. Examples include health, safety, consumer protection, competition and data privacy regulation. There are many such policies. Some are politically sensitive and reflect strong social preferences – e.g., labour standards. But many are essentially technical. International cooperation on the latter offers opportunities to reduce trade costs without affecting the realization of underlying policy objectives. Possibilities include countries agreeing to adopt certain procedures that enhance transparency, exchanging information to reduce duplication of compliance costs for firms, or recognition of the equivalence of regulatory regimes. Such initiatives reduce regulation-related costs for firms without impacting on attainment of regulatory objectives. Such cooperation, which could build on the WTO Agreement on Technical Barriers to Trade (TBT), has the potential for improving national policies and outcomes, independent of what other countries do.

There are several objections that can be made against pursuit of open plurilateral initiatives in the WTO. One is that countries that decide not to participate will not have obligations but nonetheless may have an interest in what is agreed to constitute good practice. In part this is because they may want to participate later, and in part this is because their firms may have to comply with whatever policies are adopted by a plurilateral group. Another issue that is likely to arise is that some countries may not be able to participate despite being interested in doing so because of weaknesses in institutional capacity and capabilities. The first objection can be addressed by proponents of open plurilateral initiatives focusing on international standards or norms and cooperating with relevant international organizations and entities. This is a basic element of the approach taken in the WTO towards product regulations and standards and was also an element of the process of negotiating the TFA, which drew extensively on practices that had been the subject of extensive deliberation in the World Customs Organization. The second concern can be addressed by including commitments and establishing mechanisms to assist countries to satisfy regulatory preconditions for participation (Hoekman and Mavroidis, 2015).

A basic question is what types of policies lend themselves to open plurilateral initiatives and thus do not need consensus. This is discussed further in Annex 1. A necessary condition is that countries can identify policy practices/areas where cooperation among a group of WTO members to address negative international spill-overs is feasible and beneficial even if benefits are extended to other WTO members. This is likely to span a relatively limited set of policies. Agreeing on disciplines for instruments such as domestic support for agriculture is likely to require participation by many countries because of free riding concerns, although it has been argued that this may not be true – see e.g., Stoler (2014).

For policy areas where free-riding is a concern and open plurilateral agreements are not feasible (the participation constraint binds), cooperation requires an agenda that permits trade-offs across issues. This is the traditional bread and butter of the GATT/WTO. It calls for careful preparation of a negotiating agenda that is broad enough to create a landing zone that is big enough to make all the major players better off than they are in the status quo ante. This is not a trivial matter as is illustrated by the experience of the Doha Round, where it turned out that this necessary condition was not satisfied (Evenett, 2014). But it is the only way to make progress on issues of this nature.

## 8 Recommendations

A presumption of the recommendations that follow is that the existing institutional framework provides sufficient flexibility for WTO members to do much more to leverage the normal business pursued at the level of Committees and similar technical bodies. This flexibility should be used by the membership to reflect on factors that affect the performance of WTO bodies, learning from the differences in working practices across WTO Committees and experiences obtained in PTAs on subjects that fall within the purview of WTO bodies. Greater engagement and

deliberation on the effects of policies and the operation of the WTO is a precondition for mobilizing political support for additional rule-making and the compromises and trade-offs needed to forge consensus. It is also necessary for developing a new consensus on addressing development concerns and the functioning of the DSU.

## **8.1 Policy dialogue on nontariff measures affecting competitiveness**

Escalation of the bilateral conflicts that give rise to 'retaliatory' unilaterally determined trade policies constitute a serious threat to a rules-based trade regime. Resolving current trade tensions requires the major players to use the WTO for what it was created: a forum for discussion, negotiation and dispute resolution. It is in the interest of all WTO members to engage in a concerted effort to revisit the current rulebook and working practices – including the dispute settlement mechanisms. The situation that has arisen with new appointments to Appellate Body members is one, urgent, example illustrating the need for open and frank dialogue on perceived problems and suggested solutions. The WTO dispute resolution system plays a vital role in sustaining cooperation between WTO members. Dealing with concerns regarding how the system functions without undermining the operation of the dispute settlement process must be a priority for the WTO membership.

The same applies to issues such as the trade-distorting effects of agricultural support policies; tariff escalation that constrains developing country firms from moving up the value chain; ensuring there is a level playing field for competition between firms in markets where the State may play a significant role in supporting (some) domestic companies; managing instances of global sectoral over-capacity; competition distorting effects of investment incentives; or the use of subsidies to support local production or exports. An important function of the WTO is to provide a platform for open and candid discussion of policies that countries perceive to be creating significant negative spill-overs. This platform is not being used sufficiently.

Such deliberation must be informed by factual assessments of the specific features of policies or situations giving rise to concern, and analysis of the magnitude and incidence of negative effects they generate. This is best done through working groups, supported by the Secretariat with relevant information and objective analysis. Secretariat support is important as in practice on most complex issues only a small group will engage. Good information is a critical input into this process. Moreover, greater transparency as an input into better understanding of an issue area is a public good.

The prospects for discussion and serious engagement to find an accommodation will be a function of the willingness to engage in multilateral cooperation – the *raison d'être* of the WTO – and the magnitude and incidence of a breakdown in cooperation. The current situation confronting the trading system may be unexpected but it is not unprecedented. There are parallels with the 1980s, which were characterized by extensive recourse by many OECD member countries to trade-distorting measures in response to a rapid rise in exports from East Asian economies. This was a motivation for the launch of the Uruguay Round in 1986. What is called for is a process to establish an agenda for negotiating a resolution on the specific areas of greatest concern and relevance to the WTO membership from a systemic perspective. Any such agenda goes beyond the issues that underlie the imminent threat of a trade war. There is broader set of policies of interest to all WTO members. Some of these are part of the Doha Round. Others have long been a source of debate and concern – such as subsidies of different sorts. Some are new for the trading system, notably matters that relate to governance of trade in digital products and services.

It is critical that dialogue encompass matters of importance to developing countries. Efforts to block deliberation on non-Doha issues arise not because countries do not see the salience of non-Doha policy areas for the WTO but because of a desire to see progress on policies that are priorities for many developing countries – such as tariff escalation in agricultural and natural resources sectors. Thus, balance across topics matters.

Some policy areas that are of concern to WTO members lend themselves to open plurilateral agreements. Others do not and call for a broader negotiation. Preparing the ground for this is important – a preparatory process to document the facts and help countries assess priorities is needed. A first step is for proponents of considering specific matters in the WTO to request that such a process be undertaken by WTO Members, supported by the WTO Secretariat. A precedent from the GATT period for the type of work that is needed was the process of national

studies undertaken after the 1982 GATT Ministerial meeting to better understand the extent of trade in services and the set of policies that affects such trade.

Such policy dialogue should encompass the operation of the DSU. There have been 15+ years of discussions in the framework of the DSU Review exercise that have not led to any outcomes, in large part because consensus is required to make changes. Consensus is now being used by the US to generate pressure to resolve its concerns with the Appellate Body. What has been lacking is an open discussion of concerns raised and a willingness by WTO members to accept that reforms may improve the system. The membership should engage in a broader process aimed at agreeing on specific reforms to dispute settlement procedures. Absent an agreement, conflict resolution will revert back to the pre-WTO situation in which panel reports can remain unadopted if the losing party does not agree with the panel's findings – with attendant risks of escalation in the use of unilateral trade policies. A necessary condition for resolving the dispute on dispute settlement is a willingness to draw on the review of the DSU and engage in a broader examination of the dispute resolution mechanism.

Geopolitical tensions and associated national politics may preclude a consensus on launching the needed dialogue and eventual negotiations. It must be recognized that geopolitical considerations have been a factor impeding substantive discussions in the WTO. It may not be possible to engage all WTO members in a good faith effort to address differences regarding the use of specific policies or to resolve disputes regarding the operation of WTO bodies. WTO members should not permit consensus to be a constraint in launching a process of policy dialogue. In many areas it may be feasible to proceed on a plurilateral, critical mass basis. This may be a stepping stone for an eventual agreement with broad membership, but it may also be the best approach for some types of issues – e.g., instances where there are significant differences in social preferences or societal goals.

A willingness to revisit WTO working practices, notably consensus, may be needed to resolve some issues. This may be the case for dispute settlement. If a consensus solution to the current stand-off on the working practices of the Appellate Body cannot be found, consideration can be given to developing alternatives that will apply to those WTO members that agree to implement them. As discussed subsequently, a critical mass of 'friends of the multilateral trading system' exists that accounts for some 75 percent of global trade. These countries have a strong interest in supporting both dialogue and proposing solutions.

## 8.2 Foster substantive deliberation in WTO bodies

It is often noted that the WTO is a 'member-driven' organization. There are numerous WTO bodies, both standing and *ad hoc*, including a set of Committees charged with overseeing the implementation of specific WTO agreements. There are currently twelve issue/agreement-specific Committees that cover different dimensions of trade policies affecting merchandise trade that report to the Council for Trade in Goods, two committees that report to the Council for Trade in Services, and five that cover cross-cutting issues and report to the General Council. In addition to these committees there are two working parties that operate under the aegis of the Council for Trade in Services (on GATS rules and on domestic regulation), a working party that reports to the Goods Council (on state-trading enterprises) and working groups on trade and technology transfer and on trade, debt and finance (see Annex 2). The working parties are deliberative bodies charged with exploring approaches for further developing provisions in the relevant WTO agreements.

While day-to-day activities are undertaken by delegations based in Geneva, Committee and other meetings may also involve officials from capitals. However, the extent of capital-based participation varies substantially across Committees and working parties/groups. The Secretariat supports the work of all WTO bodies with specific inputs prepared at the request of the Chairperson or WTO members that participate in them, preparing minutes of meetings and circulating documents submitted by WTO member representatives.

Many of the committees operate in two modes – one to deal with normal business and one in so-called special session. The latter are negotiating sessions that center (centered) on subjects (goals) established by the Doha Development Agenda. The Committees are the primary venues in which WTO members discuss the operation of the agreements they oversee. The working groups and working parties are mechanisms to discuss specific matters they have been mandated to consider and explore potential modalities for cooperation/agreement. The special

sessions and working party-based efforts to develop new rules/agreements attract most attention from policymakers and the press. Devoting more attention to the regular work of the Committees could help to revitalize the deliberative function of the WTO.

**Self-reflection: Do Committees have the information they need?** Transparency is essential for reducing uncertainty and is one of the main tasks of the WTO. Focusing on its performance in generating relevant information at the level of Committees and specific WTO agreements is consistent with learning about its performance more generally. Better information is not simply a public good, although that is an important output and a key rationale for the various transparency and surveillance mechanisms included in the WTO. Information is primarily beneficial for countries themselves – a necessary input for understanding national policies. A useful role that WTO bodies can play is providing a venue for members to learn about their own policies as well as those of others and to identify where policies may be having negative international effects and using regular meetings to promote discussion of policies that limit adverse trade effects while attaining underlying regulatory goals.

A first step could be for each Committee to ask themselves what is needed to become more relevant to the constituencies / stakeholders that have a direct interest in the policy areas covered. Is the Committee dealing effectively in helping to attain national objectives in their area? An important element of this self-reflection is to determine what information is needed to fulfill both the mandate/objectives established in the relevant WTO agreements and the concerns of the government officials and agencies in capitals that deal with their issue areas. Are these well-understood? Do Committee members have the information they need? What information is needed?

Questions that arise in this connection concern the quality and comprehensiveness of the information provided to (by) the WTO in terms of allowing analysis of whether it is attaining its objectives (listed in the Preamble); helping economic actors navigate the system; or helping citizens to see inside the system. Is WTO data comprehensive? Of high quality? Tracking emerging issues? Is information a burden or a benefit? Are members willing suppliers of information (statistics, notification) in one area but reluctant in another? Why? Is this a matter of differences in perceived legitimacy of the WTO Secretariat across committees? Does it reflect resource constraints? Why are some committees more successful in generating relevant information than others? Are there any common good practices? Could technology be used more effectively? And of the information that is being provided, for instance, though notifications, could better use be made if its content?

Answers to these questions can help to enhance transparency and enable better information provision, including how to ensure timely and satisfactory notifications by members and inform decisions whether the secretariat should be given a mandate to collect more information itself, working with other international agencies and stakeholders, on matters of relevance to the different WTO bodies. Alternatively, it may be that provision of assistance would help improve the ability of developing country members to collect and provide information. The point is for members to ask themselves in each committee if they have the information they need to do their job and, if not, what can be done to ensure they obtain it.

This process of self-assessment by Committees is not the same as recognizing that Members are not living up to notification obligations and calling on them to do better in abiding by the many notification requirements embodied in the WTO. There is a general recognition that WTO notification obligations are not being fully adhered to by many members. Instead of engaging in negative finger-pointing, we suggest a positive approach – asking WTO members in each Committee what specific types of information are needed. As argued by Wolfe (2018), it may well be that many of the notification requirements contained in WTO agreements are not deemed to be useful. Conversely, WTO members may be missing information that does not have to be notified at present.

The aim here is to shift the focus from a “business as usual” approach centered on defending long-standing positions to one that focuses on what each WTO body’s activities should be – and based on the answer to this, an assessment of what information is needed to fulfil those tasks. This goes beyond the question whether members are living up to notification obligations embedded in the WTO agreements. It entails reviewing these and considering if they should be revised or simplified given changes in the organization of global production discussed earlier in this report. Such self-assessment of WTO information provision, on a WTO committee-by-committee basis, could feed into an annual synthesis report (a “Trade Policy Review of the System”) that could be discussed in the General Council as part a broader review of the functioning of the WTO (see recommendation 8.5 below).

**Focus on salience for economic development.** In addition to self-reflection on how to enhance the effectiveness and relevance of the normal operation of each committee and other WTO bodies, a parallel process of

policy dialogue (open, non-committal deliberation) on whether and how the provisions of WTO agreements support sustainable development goals could be launched. The aim would be to identify good policy practices and their relationship with each of the subject areas covered by the agreements overseen by a committee. This should include sharing of national experiences and be supported by analysis by the Secretariat and other international organizations. Such a process could become the basis for incrementally addressing the tensions that surround the invocation of SDT.

A development-focused policy dialogue in the various WTO bodies could consider factual questions: What kind of SDT could help countries develop world class industries in sectors where they have comparative advantages? What kind of SDT would support better insertion in GVCs? Practical case studies of countries that have developed world class industries could inform such deliberation. Many such studies already exist – there is no need to commission them. Did SDT provisions contribute to success? Was SDT a factor in attracting foreign investors? Could there be situations where SDT actually prevents development? Does the private sector benefit from derogations from general WTO rules? What could the WTO and the Secretariat do to assist governments and economic operators address coordination problems and other market failures that impede investment? Are development agencies providing aid for trade that addresses such constraints? A corollary benefit of such substantive deliberation on policy matters is that it may help WTO Members to extend the approach reflected in the TFA to other areas (i.e., agree on a set of good practices complemented by credible commitments by higher income members to assist developing countries to implement). A basic focus of such discussion should be on identifying the scope for greater differentiation among developing countries.

**Learning from PTAs.** Another useful focal point for deliberation at the Committee level is the operation and implementation of PTAs in the policy areas covered by each Committee. This would complement the focus of the Committee on Regional Trade Agreements on the legal content (provisions) of the PTAs that have been implemented by WTO members. This Committee does not discuss the experience of how PTAs are implemented or assess the economic effects of different approaches that may be taken in PTAs towards a given policy area. Discussion of implementation experience in the areas covered by the various WTO bodies is best done in the respective bodies as these will bring together officials from capitals responsible for the specific areas covered by each WTO agreement. This has been done in the past on an ad hoc basis – making this a regular agenda item, with preparation of background documentation by the Secretariat would support a more structured and regular process aimed at learning from PTA experiences.

PTAs may encompass innovative approaches to attenuate the market-segmenting effects of regulatory policies that other countries might usefully emulate. All WTO Members have a strong interest in understanding what innovative PTAs do and achieve. Documenting alternative approaches used in PTAs would not only improve transparency but, more important, potentially inform a process of learning about what works and what does not and identify options that might eventually be multilateralized through initiatives under the WTO umbrella.<sup>27</sup>

**‘Ownership’: connecting better to constituencies.** A general precondition for the process of self-reflection and policy dialogue proposed here to be feasible is that it is not blocked by the consensus practice. A necessary condition for this is to credibly address concerns that issues tabled for discussion may give rise to eventual negotiations. Fears that this is the ‘end game’ of policy dialogue may induce some members to take tactical positions to oppose deliberative activities. The rationale for doing so is not compelling given that consensus implies that countries can always refuse to engage in negotiations to establish new rules for a policy area. If a WTO member insists on blocking open-ended discussion, there is nothing that prevents a group of WTO members from pursuing this outside the WTO. This is very much a second-best outcome however, as it is important that the Secretariat can support such deliberations and is able to ensure there is transparency vis-à-vis WTO members that do not participate in them.

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<sup>27</sup> A Committee-centric discussion of relevant elements of PTAs can address the reasons for the failure of the Nairobi Ministerial mandate directing the Committee on Regional Trade Agreements to discuss the systemic implications of PTAs highlighted in Wolfe (2018). Some committees have made steps to implement what is being proposed here – an example is the Committee on Trade and the Environment, which has discussed environmental provisions in regional trade agreements based on presentations by Members and a background paper by the Secretariat (WTO, 2017b).

The practice of interpreting consensus as an unlimited capacity to exercise veto power has been a factor impeding the effectiveness of the operation of the WTO. There is no easy solution to the problem given the consensus that exists on consensus (Lamy, 2009). This suggests the focus should be on reducing the scope for WTO members to engage in hostage-taking by increasing the costs of such behavior, or, equivalently, reducing the return that can be achieved. The latter can be done through subsets of WTO members pursuing a matter through open plurilateral initiatives where these are feasible. The former can be pursued by doing more to engage with constituencies at the national level that have a strong interest or stake in making progress in each policy area.

Some of the WTO committees work effectively as bodies through which government officials based in national capitals and/or representatives of national regulatory agencies interact and cooperate. Three examples where this is the case are the Committees on Technical Barriers to Trade (TBT), Sanitary and Phytosanitary (SPS) measures and Government Procurement (the latter is an Art. II.3 Plurilateral Agreement that applies only to signatories – see below). The TBT and SPS committees have been characterized as technical expert-driven catalysts for multilateral dialogue, providing a forum for the development of guidance on good practices and collective peer review of proposed national policy measures (Wijkström, 2015), motivated by finding solutions for problems of concern to the business community.<sup>28</sup> All three of these bodies have gradually expanded their remit and activities.

A prominent example is the use of so-called specific trade concerns (STCs) as a vehicle for a WTO member to raise questions and concerns about proposed new product regulations in the TBT or SPS committee. Close to 550 STCs have been raised in the TBT Committee and only 16 ended up in formal disputes. The majority have disappeared, presumably resolved, sometimes with modifications to regulations following discussions around the STC process. The TBT Committee has also as part of regular committee work adopted decisions that have proven influential such as the TBT Committee Six Principles for the development of international standards. The Government Procurement committee has established and is implementing a work program of different dimensions of public procurement that essentially involves identifying good practices. It does so through several working groups in which subsets of GPA members take a leadership role and that are open to all GPA signatories. Other WTO committees and bodies demonstrate less in the way of such initiative or activity, although the Agriculture, Market Access and Council on Trade in Goods, among others, have created opportunities for discussion of implementation questions and answers raised by Members.

A common factor underpinning the pro-active and constructive engagement between WTO members observed in these committees is that they connect a specific constituency – officials responsible for achieving regulatory objectives – with trade officials who are interested in reducing trade costs. The ‘ownership’ resulting from the value added that is generated for participants in these committees reduces the incentives to engage in hostage-taking behavior.<sup>29</sup> Necessary conditions are that work programs are relevant to what officials are responsible for, and that the activities of the Committee can be justified to parliaments, businesses and citizens as delivering useful results. Determining if and how the various WTO Committees and related bodies connect to specific groups in and outside national government – and how to do so more effectively – may both improve the usefulness of their work and the support by economic operators and national interest groups for WTO engagement.

In practice, connecting to relevant stakeholders in each WTO member will be costly, but recent advances in information and communications technologies permit more use of video conferencing. The first step is to identify the constituencies that have an interest in the work of a Committee and reflect on how to better engage them. This includes the relevant regulatory communities at both national and international level whose work impacts on the policy area covered by a WTO agreement. Interacting with these regulatory communities, including regulatory agencies that have indirect impacts on trade costs (trade facilitation objectives), can assist Committees identify how they can help achieve national regulatory objectives more efficiently and effectively.

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<sup>28</sup> One useful innovation that has been implemented by the WTO secretariat is ePing, a system through which the WTO can push relevant information from notifications to firms, providing them the basis if necessary to raise any concerns with their government, which in turn can raise a specific trade concern in the TBT or SPS Committee.

<sup>29</sup> This does not necessarily mean that it is easier to obtain agreement on expanding the scope of a Committee’s activities. In the case of the SPS Committee it has proven difficult for example to agree to launch a work program on private (voluntary) standards, a subject that has been put forward for deliberation by several developing countries.

Changes in the modus operandi of Committees may help increase participation and ‘ownership’ of activities. One possibility in this regard is to provide more support for Chairpersons of Committees by creating a steering group or bureau of three or four WTO member representatives who are appointed for several years. In existing practice, the chairpersons, except for those of Special sessions, stay only for one year, which causes problems of continuity. The practice of establishing a steering group has been adopted in some of the joint initiatives launched in Buenos Aires. This approach is used in other international organizations such as the OECD, where each Committee has a ‘bureau’ comprising a small group of member country Ambassadors who help guide the implementation of work programs. This helps to ensure continuity, follow-up and engagement. An ancillary benefit of broadening the management of Committees is that it can reduce the use of consensus to prevent a majority from moving forward in engaging in a specific activity. Assuming the steering group or bureau is representative and unified on a proposed course of action, this raises the reputational costs for a member to block initiatives as well as reducing incentives to do so.<sup>30</sup>

Other practical steps can also be considered to facilitate policy dialogue of the type advocated here. Adding items to a standing agenda can be problematic as it implies taking time from other issues. The processes suggested here will also have resource implications raising potential concerns of resource diversion. Such concerns can be addressed by holding informal or thematic sessions alongside regular Committee meetings, with sponsors of an issue put forward for informal dialogue providing additional funding, where needed.

Finally, and importantly, it is vital that policy dialogue is framed as an open process with a view to consider whether there is a problem and to learn from experience as opposed to starting from the premise that this reflects a search for rules. The latter may well be a solution, but first it is necessary for there to be a common understanding of an issue and whether and how rules are needed to address it. The process should not be framed as a prelude to negotiations, as this is a key factor why some WTO members have opposed policy dialogue on new matters in the first place. As noted, such concerns are misplaced as consensus ensures that countries can always block the launch of a multilateral negotiation process that spans all WTO members.

### 8.3 Open plurilateralism: initiatives among groups of WTO members

Taking as given that consensus will continue to be WTO working practice, this should not be permitted to preclude subsets of WTO members from pursuing cooperation on specific issues through open plurilateral initiatives. The types of deliberation proposed above could eventually become the basis for discussion on agreements to incorporate new elements of good practice into the commitments of WTO members that see a benefit from doing so on a concerted basis. This could take the form of a Reference Paper along the lines of the telecom reference paper to which countries seeing this as beneficial sign on. Alternatively, it could take the form of codes of conduct to be followed in instances where a group of WTO members may consider engaging in a more far-reaching open plurilateral initiative on an issue covered by a specific committee or WTO body.

Such initiatives are already being pursued. One of the results of MC11 was the launch of initiatives on e-commerce, investment facilitation, MSMEs and domestic regulation of services by different groups of WTO members. WTO members that joined these groups demonstrated that consensus cannot be used to prevent groups of countries discussing issues of common interest.<sup>31</sup>

Two types of mechanisms can be used by subsets of WTO members to collaborate on a policy area: so-called critical mass agreements (CMAs) and Plurilateral Agreements under Article II.3 WTO. CMAs are open plurilateral initiatives under which a group of countries agree to specific trade policy commitments they inscribe into their WTO schedules and apply on a non-discriminatory basis to all WTO members. A major example is the Information Technology Agreement (ITA), which abolishes tariffs on information technology products. This was re-negotiated in 2015

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<sup>30</sup> The focus here is on normal work programs of Committees, not negotiations that may alter the rights and obligations of members.

<sup>31</sup> Participation in these groups spans a broad cross-section of the membership. The EU participates in all four groups. The US is part of one (e-commerce). China participates in all groups except the one on e-commerce. India as well as many African countries decided not to participate in any of the groups.

to expand the number of products covered. The ITA has increased global trade substantially in electronic products and improved access to key technologies that underpin the digital economy.<sup>32</sup> CMAs have also been concluded for services sectors – an example is an agreement on basic telecommunications that was appended as a protocol to the GATS in 1997, with 69 WTO members signing it. The benefits of the agreement apply to all WTO members, including those that did not sign it. The basic telecom agreement includes a so-called Reference Paper that establishes regulatory principles (good regulatory practices) that signatories commit to apply.<sup>33</sup>

A key feature of CMAs is that disciplines are negotiated among a subset of interested WTO members and apply only to countries that sign on to them, while the benefits must be extended on a most-favoured-nation basis to all WTO members, including those that do not participate. Such agreements do not require consensus to be incorporated into the WTO – if Members decide to join a CMA they can inscribe the provisions of the agreement into their schedules of commitments under the GATT and/or the GATS. The agreements become part of the WTO and are serviced by the WTO Secretariat. Members interested in discussing possible future CMAs can request WTO Secretariat support for the process.<sup>34</sup>

Art. II.3 Plurilateral Agreements differ from CMAs in that they may be applied on a discriminatory basis – that is, benefits need not be extended to non-signatories. Because of this, Plurilateral Agreements require consensus to be incorporated into the WTO. Two such agreements currently exist – the Agreement on Civil Aircraft and the Government Procurement Agreement (GPA). Because Article II.3 WTO Plurilateral Agreements may be applied in a discriminatory manner, they are subject to the approval of all WTO members, including those that have no intention of joining. Art. X.9 of the Agreement Establishing the WTO stipulates that the Ministerial Conference of the WTO may decide to add a new Plurilateral Agreement to the existing ones ‘exclusively by consensus’.

WTO members have devoted much more effort and resources to the negotiation of PTAs than to open plurilateralism in the WTO but there has always been interest in pursuing cooperation on a critical mass basis. Aside from the expansion of the ITA in 2015, examples include negotiations on a possible Environmental Goods Agreement. These commenced in July 2014 and span the EU and 16 other WTO members. As mentioned above, at the 2017 Ministerial Conference in Buenos Aires different groups of WTO members launched four joint initiatives on micro, small and medium-sized enterprises, e-commerce, investment facilitation and domestic regulation of services.

As discussed above, the scope for open plurilateral initiatives – i.e., CMAs – is likely to be limited to issues that are either insensitive to free riding concerns or policy areas where many WTO members can be induced to participate so that benefits are mostly internalized by signatories (as was the case for the ITA). The types of subjects that may lend themselves to such initiatives therefore do not include policy areas such as industrial policy or subsidies. However, there may be much more scope for open plurilateral cooperation than is often assumed, especially for technical issues where cooperation may reduce trade costs. There are potentially many such policy areas.<sup>35</sup>

At a minimum, open plurilateral initiatives provide an opportunity to insert new oxygen into the system. They offer a mechanism for groups of WTO members to engage on matters of interest to them and to determine whether there is potential scope to agree on what constitutes desirable policy. They can serve as experiments and laboratories to identify areas where cooperation is feasible and demonstrate that the WTO need not be hamstrung by its consensus practice in providing a platform for cooperation. Even where no agreement proves possible, the associated deliberations are useful as they will help inform decisions on the set of issues that could be considered as part of a broader effort to construct a forward-looking agenda to update rules that will apply to all WTO members. This could be supplemented with a transition-oriented approach that may combine elements of TFA and the telecom reference

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<sup>32</sup> Over time, the ITA has been estimated to have had a large positive effect on trade in information technology products – see Henn and Gnutzmann-Mkrtchyan (2015) for estimates.

<sup>33</sup> The GATS also includes a protocol on financial services that applies only to WTO members that signed it, with benefits applying to the membership as a whole.

<sup>34</sup> There are different views on Secretariat support for CMA initiatives such as the ongoing EGA negotiations. Some members such as India have expressed reservations on the provision of (potential) secretariat support. For the new initiatives on e-commerce, MSMEs and investment facilitation, there are also different views on whether the secretariat should provide such support.

<sup>35</sup> Examples include using the scope under the GATS to make additional commitments (Adlung and Mamdouh, 2017), extending the ITA to encompass digital trade (Lee-Mikayama, 2011), or agreement on standards for using block chain technology to facilitate trade under the TFA.

paper, i.e. a phase in of obligations linked to some pre-accepted criteria from a list of obligations that combine mandatory and voluntary options.

The likelihood that the WTO membership will be willing to accept new Article II.3 WTO Plurilateral Agreements – i.e. agreements such as the GPA that permit discrimination – is very low, given that their incorporation into the WTO requires consensus. Some observers have argued that it is in the interest of all WTO members to be more willing to let countries negotiate such agreements. Refusal to consider this essentially means that countries that want to engage in deeper integration in areas where free riding is a concern must do so outside the WTO framework. In practice this implies (mega-regional) PTAs. These are important instruments for deepening trade cooperation, and, in the case of services, offer a potential mechanism for WTO members to pursue reciprocal liberalization of markets – as illustrated by the TiSA negotiations – but such PTAs not only give rise to the discriminatory features of Art II.3 Plurilateral Agreements but are less transparent. They are not subject to WTO monitoring and dispute settlement will occur outside the WTO.

It would be beneficial for the WTO membership to engage in a discussion on concerns that exist regarding WTO Art. II.3 Plurilateral Agreements and work to clarify and strengthen the ground rules that should apply to such agreements through a Reference Paper or a code of conduct.<sup>36</sup> In practice, however, small group agreements will have to take the form of open plurilateral initiatives that apply on a non-discriminatory basis.

Careful choices need to be made in pursuit of such initiatives. Ideally, the focus should be on matters of importance to influential constituencies and ones that stimulate engagement/support from the private sector and other stakeholders. The WTO is best served by initiatives that ‘move the needle’. Much depends on what will happen with the joint initiatives that emerged from MC11. All have a large potential set of stakeholders and all address subjects that are very relevant for the trading system.

An important question with respect to open plurilateral initiatives is whether any specific conditionality that is included in an agreement could violate the MFN rule. The benefits of such initiatives among a subset of countries will need to be extended to all WTO members, including those that do not participate in the agreement. However, such benefits may be subject to satisfying specific preconditions that relate to the quality or capabilities of regulatory institutions and frameworks. In this respect, the situation may be akin to mutual recognition agreements for conformity assessment of product standards. WTO rules require these to be accessible (open) to any WTO member that is interested in participating in an extant agreement, but this does not nullify the need to satisfy the conditions that are necessary for mutual recognition. Similar approaches will need to apply to open plurilateral initiatives that involve regulatory cooperation.

## 8.4 Bolster the support function of the Secretariat

The WTO is a member-driven organization in which the Secretariat is given very little voice. WTO practice has been to interpret the ‘member-driven’ motto as depriving the Secretariat from being able to take initiatives to support the work of WTO bodies. This needs to be reconsidered. Member-driven means members are responsible for conducting the WTO (i.e. taking decisions) but it need not translate into a monopoly on the right to express voice and supply relevant information to WTO members. Policy dialogue should not be limited to trade issues that fall under current WTO agreements; the Secretariat may need to assist such dialogue by providing information and analysis on the potential spillover effects or domestic policies, regardless of whether they fall under current WTO obligations.

A core task of the Secretariat is to provide background material and analytical support to WTO members. Such support is vital for informed policy dialogue and deliberation. For certain functions (e.g. some negotiations and committees and councils), this information provision role generally works well. In other cases, e.g. in politically sensitive negotiations, the Secretariat may not be permitted to provide such services. The same applies to new issues that are pertinent for the trading system. Restricting the scope for the Secretariat to provide information to members implies a significant opportunity cost from a systemic perspective given differences in capacities across

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<sup>36</sup> Lawrence (2006), Nakatomi (2013) and Hoekman and Mavroidis (2015) discuss this matter at greater length.

WTO members. Granting the Secretariat greater discretion to develop and table information and analysis, while leaving to members to decide whether and how to utilize this, would be a step forward. Developing guidelines or a code of conduct for the exercise of such discretion to ensure neutrality and independence of the Secretariat could help address potential concerns of WTO members about giving the Secretariat greater scope to support the work of the organization. One part of this effort could be to append the factual comments by Members on the Secretariat's information or analysis papers to get a more comprehensive perspective on the issues concerned.

There are many policy areas where WTO members need accurate and up-to-date information, not only regarding applied policies – which is a critical function of the organization – but on the effects and effectiveness of policies in attaining their objectives. The latter calls for both knowledge on how policies are implemented and analysis of their impacts. Committees and working groups need information synthesizing current knowledge on developments in a range of areas that are relevant from a trade perspective. Some of the inputs that Committees may identify as being needed as part of the self-assessment process suggested above may be difficult for members to provide because of resource constraints. Using the Secretariat more effectively by permitting it to provide more support for the normal work of Committees and other WTO bodies will raise the rate of return on the investment of resources WTO members contribute to the organization. Knowledge and analysis is particularly needed for 'new' policy areas and the type of cooperation that can be pursued via CMAs centering on identification of good (regulatory) practices and the distillation of knowledge regarding the lessons of experience with/results of implementing associated policies.

Empowering the Secretariat to do more to demonstrate that the WTO is an asset for WTO members can help counteract claims that the system of rules has adverse welfare effects or benefits only a few. A key area of concern for many citizens is the distributional effect of trade integration. While improving equity of domestic outcomes and assisting workers and firms manage adjustment costs are matters for national policy, much more can and should be done to monitor and assess the economic effects of WTO membership.

The extent to which distributional effects of globalization are due to trade policy commitments is not something on which the WTO has much to say. There is much *ex ante* academic analysis of the potential benefits of greater trade and much *ex post* analysis of the specific costs incurred by negatively affected industries. The former is generally discounted by trade critics and proponents alike. The latter tend to ignore the positive side of the equation, mostly because this is more difficult to attribute to the trading system in a scientifically acceptable way. What is missing is compelling analysis of the value of a rules-based trading system. The World Trade Report has become a flagship publication of the organization and is invaluable in providing an objective and informative 'big read' on a specific trade topic. It should be complemented by more regular analysis of the effects of implementation of WTO agreements.

The Secretariat has an important role to play in supporting the greater deliberation that is advocated in this report. Enabling it to provide more information can make it more useful to the constituencies that have a stake in the performance of different WTO bodies. These constituencies play a critical role in sustaining political support for the organization. They are mostly located in the capital cities of WTO members. Enhancing the capacity of the Secretariat to engage with these groups may help change perceptions at the national level on the utility of the organization.

Greater engagement with stakeholders in WTO members will require resources and depends on the Secretariat having the skill-mix to permit substantive engagement with national counterparts on subject areas covered by WTO agreements and other areas of policy of interest to groups of Members. On the resource side, there is scope to reallocate technical assistance funds from training seminars focused on helping "government officials of WTO members gain a better understanding of WTO rules and the multilateral trading system" (WTO, 2017b, p. 16) towards the provision of services to members that request it and to support the engagement of – and with – counterparts in national government agencies and broader regulatory constituencies with an interest in trade-related policy areas.<sup>37</sup>

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<sup>37</sup> The funds contributed by donors currently are deposited into the Doha Development Agenda Global Trust Fund, but activities are not limited to Doha negotiations support activities. Contributions to this fund have been declining over time, from an average of CHF 17 million during 2009-11 to some CHF 7-8 million during 2015-17. Consideration should be given to re-naming and revising the terms of reference of this trust fund to support a broader set of activities.

There is of course only so much the Secretariat can do and care should be taken that it does not duplicate what other organizations do. More cooperation with other international organizations dealing with different aspects of trade policy and related regulation, as well as increasing engagement with international business organizations, sectoral regulatory communities and representative NGOs, can leverage Secretariat capabilities to provide information and analysis that is relevant to WTO bodies and constituencies.<sup>38</sup>

## 8.5 Review of organizational performance

Periodic assessments of the WTO's institutional performance can foster learning about what works well and what does not. Formal review mechanisms can act as a mirror for members, presenting them with facts they may not be fully aware of, as well as provide information that is useful in considering what might be done to improve performance. Review can foster learning and incentivize constructive engagement by members.

The WTO is unique among international organizations in not having either an independent evaluation office or an internal review mechanism that assesses the operation of the institution. The WTO has an Office of Internal Oversight responsible for conducting internal audits, investigations and “any other assessment deemed necessary to strengthen accountability, internal controls, compliance, value-for-money and governance in the WTO Secretariat.” The director of this office is part of the Secretariat and, as such, she/he is appointed by the director general, after consulting the Committee of Budget and Financial Administration. The Office of Internal Oversight can perform evaluations, but it reports to the director general, not to the General Council (WTO members) and is mostly devoted to internal audits and investigations.

Assessing the performance of the different parts of the WTO can help to identify both good practices and reasons why performance in some areas may be below what it could be. Two options can be considered: an internal process or an independent, external evaluation mechanism. External evaluation is used in many organizations as an efficient way of facilitating learning. Prominent examples are the World Bank Independent Evaluation Group and the IMF Independent Evaluation Office.<sup>39</sup> Putting in place an external evaluation function could help identify weaknesses that may not emerge through internal reflections and generate ‘hard facts’ that some WTO members might prefer to ignore (Torres, 2017a,b). Great care will be required in designing an independent external evaluation office to ensure that it has a mandate that is agreed by all WTO members, is accountable and that its work is performed by experienced and knowledgeable individuals who have an excellent understanding of the goals and operations of the WTO. In practice, this is something that will require substantial preparation to attract the necessary consensus. An internal reflection process, in contrast, may be put in place more easily.

Internal review could build on the model that has been put in place at the OECD. This involves a small internal unit that works with each Committee's ‘bureau’ but drafts its own report on the operation of the relevant Committee. Thus, there is no independent external evaluation (and evaluators) – the process relies on delegations supported by a small number of OECD staff (Wolfe, 2018). A feature of the process is that it encourages learning across Committees and helps identify potential ‘silo problems’ created by the issue-specific focus of Committees and that preclude a more holistic focus on a problem area. The OECD structure is not dissimilar to the WTO in that it relies heavily on working groups and committees that report to an overarching Council and a Ministerial Conference.

Considering whether the issue-specific focus of WTO bodies results in policy areas being addressed in a too piecemeal fashion and identifying areas where more regular interaction between WTO bodies can fill gaps and exploit

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<sup>38</sup> There are examples of such efforts already in the WTO. For example, in 2016, the Council had sessions to discuss national experience in intellectual property-related education and diffusion, sustainable resource and low-emission technology strategies, and regional innovation models. See WTO (2017b).

<sup>39</sup> The World Bank's Independent Evaluation Group aim is to promote a stronger internal culture for results, accountability, and learning. It has two goals: (i) to deepen the evidence about the results of the World Bank Group towards the achievement of its goals of accelerating poverty reduction and boosting shared prosperity; and (ii) to generate evidence on the early implementation experience of the World Bank Group Strategy to help shareholders and managements make necessary mid-course corrections. See <http://ieg.worldbankgroup.org/about-us>. The mandate of the IMF Independent Evaluation Office EO is to conduct independent and objective evaluations of Fund policies and activities. It has three goals: (i) enhance the learning culture within the Fund, (ii) strengthen the Fund's external credibility, and (iii) support Institutional governance and oversight. See <http://www.ieso-imf.org/ieso/pages/IEOHome.aspx>.

synergies can help ensure the WTO is responsive and remains relevant. The need for cross-cutting approaches is increasing as a result of production processes that span many sectors and are affected by many different policy instruments.

There is substantial scope for cross-Committee learning, including on working practices. An important dimension of what the WTO does is compiling information on new trade measures, largely based on notifications by members. As is well known performance on notification leaves much to be desired, as is reflected inter alia by WTO monitoring of trade policies, annual reports on notifications by WTO members (e.g., WTO, 2017b) and the Global Trade Alert data. But performance varies widely, with some Committees doing a much better job than others in inducing notifications. The notification record of the TBT and SPS Committees swamps that of other WTO bodies. While this is in part a function of the types of policy measures concerned and the extent to which Committees are connected to national constituencies (see recommendation 8.2 above), differences in performance may be related to procedures used by these committees to develop and implement work programs that may be transferable.<sup>40</sup> A review of the regular work of these Committees can help identify differences in performance and reasons for them, and inform assessments of whether successful practices might be emulated in other areas.<sup>41</sup>

At present there is too little focus on operation and performance of WTO bodies. Any WTO-wide review should involve the Committees and draw on the bottom-up committee-by-committee self-assessments of WTO information provision suggested above. It should go beyond this to also report indicators of participation by Members and engagement with stakeholders. The WTO annual report includes some measures of participation – e.g. the number of questions raised by developed vs. developing countries on notifications made to Committees; number of specific trade concerns raised in Committees; contributions to the Global Trust Fund; and participation in the DSU. More such specific information on metrics that are salient from the perspective of the operation of the institution would help to assess performance of WTO members.

The goal here should not be to engage in a bean-counting exercise but to collect and present information that helps to inform delegations and business and other groups at home. Examples could include the number of proposals put forward by individual members; the number of joint papers/proposals made; support requested and provided by the Secretariat; the number of agenda items addressing thematic issues as opposed to narrow implementation of WTO agreements; how long specific proposals for deliberation on an issue have been on the table without consensus being possible; measures of capital-based engagement in meetings;<sup>42</sup> and indicators to measure interactions with and participation by non-governmental entities (international organizations, business representatives, NGOs).<sup>43</sup>

The compilation of such information would complement the annual reporting by subsidiary bodies and the proposed internal review of the operation of subsidiary bodies to inform an annual discussion in the General Council as part of its broader appraisal of the functioning of the trading system. As part of its oversight function, the WTO General Council already conducts a year-end review of WTO activities, based on annual reports of its subsidiary bodies. However, the latter are largely limited to summaries of meetings and topics discussed. There is little substantive

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<sup>40</sup> One procedure that may play a role in this regard is the adoption by the Committees of the ‘specific trade concern’ procedure that encourages members to flag concerns they have on proposed or existing product standards. This has generated over 800 issues being raised between 1995 and 2015. This process is widely regarded as being a useful mechanism to address the concerns raised – about 40% of specific trade concerns relating to sanitary and phytosanitary measures reportedly were resolved (Karttunen, 2016).

<sup>41</sup> An example is services where domestic regulations impact on the scope for firms to supply and consumers to buy products connected to/using “the cloud” (data localization requirements, etc.) The focus of the working party on domestic regulation has not been on mapping out and learning about the operation and effects of policies that WTO Members are pursuing. A recent joint venture with the World Bank to maintain and update a database on policies that restrict trade in services is a good first step but needs to be expanded to cover additional policies that may affect services trade.

<sup>42</sup> One benefit of this indicator is to help identify the investments governments are willing to make in sustaining WTO day-to-day processes and where technical assistance resources could be allocated.

<sup>43</sup> There is significant variation across WTO bodies in their interaction with non-governmental organizations. The Committee of Trade and Environment, for example, is quite active in this regard. In 2016 it invited the Secretariat of the Basel, Rotterdam and Stockholm (BRS) conventions on protection of human health and the environment from the harmful effects of chemicals and hazardous waste, to present its work. Other organizations that did so included UNIDO, CITES, FAO, UNEP and UNCTAD.

deliberation in the General Council on the operation and performance of subsidiary bodies.<sup>44</sup> The suggestions made here would make this process more meaningful and informative.

## 8.6 Outreach and communication strategies

Following on previous recommendations, consideration should be given to re-thinking how the WTO community – the DG, politicians, business representatives, trade scholars – describe the operation and the value added of the multilateral trading system. Too often public outreach and advocacy are framed in terms of the additional exports and jobs that will be generated by a new agreement. Usually this is based on simulation models that can easily be criticized and that increasingly have become a target for groups that oppose international cooperation and greater integration of product markets. Matters are made worse if criticism of models drives advocates to engage in debates on technicalities and try to document why the critics are making incorrect claims. This is counter-productive as it is a debate that will not be understood by voters and can result in a further erosion of perceived credibility.

The objectives of the WTO range far beyond trade policy disciplines. The preamble of the WTO Agreement mentions improvement of living standards, preservation of natural resources, and attainment of sustainable development, among other goals. Communication strategies should be based on what the WTO does (has done) to attain these common objectives – and where it has failed to do so. Given that a key function of the WTO is to provide a platform for its members to establish rules and to enforce them, greater attention should be given to the role played by the organization in reducing uncertainty for firms and providing a mutually agreed governance framework that helps governments pursue welfare-enhancing policies. This extends far beyond the narrow interest of exporters – it benefits all citizens. Systemic stability and transparency about what governments do both in terms of national policies and of engagement in the WTO matters for citizens as well as firms.

Several of the recommendations made above will generate the type of information and data points that can feed into more effective and outreach strategies. What is missing is rich knowledge (evidence) on the ‘system at work’; how the procedural rules intended to reduce uncertainty for traders do so; how this affects actual investment decisions by specific firms; what the WTO system does to help members address trade concerns raised by firms; what it does to give consumers access to better products and greater choice; etc. Such an exercise can leverage the review and self-assessments advocated above to also highlight what is not working well and to do more to point out areas where WTO members could do more to support operation of the organization.

Some WTO members have begun to go down this track, although most continue to put too much emphasis on exports as the primary lens to motivate participation in the organization.<sup>45</sup> The OECD-WTO initiative to measure trade in value added has been important in documenting that imports matter for exports and that services are a major part of the value that is embodied in traded products. Moving from this ‘macro’ perspective to a focus on specific firms that rely on both imports and exports in specific communities across a range of WTO members can help make the case for trade policy rules more tangible.

The focus of attention regarding the performance of the WTO is appropriately on governments – the members. But governments can be assisted by actors that have a great stake in ensuring the continued viability of the rules-based trading system. Businesses especially have been missing in action and arguably been either too complacent or too risk-averse in supporting the institution. All businesses have an interest in lobbying governments for changes in policies that will benefit them and many do so, either directly or through trade or industry associations. This is a normal and desirable dimension of the political process in every country. Business has been disappointed by the inability of the member-ship to conclude the Doha Round and, starting in the mid- to late-2000s, many industries shifted more (most) of their attention to PTAs and mega-regional initiatives. Exceptions to this observation are the

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<sup>44</sup> The review by the General Council of the activities of subsidiary bodies as summarized in the WTO Annual Report is primarily focused on the trade policy matters covered by each body. There is no evidence of effort to reflect on lessons or transferability of approaches from one committee to other bodies.

<sup>45</sup> The European Commission has a Market Access Partnership that includes a focus on identifying success stories where specific trade impediments are removed and case stories are prepared that illustrate how this benefits specific firms and their workers.

ITA and the TFA, where there was pro-active engagement to support the associated negotiations in capitals and through advocacy efforts.

What has been missing is vigorous public defence of the trading system. While international business has been active in engaging with G20 leaders through the B20 and international institutions such as the WEF and ICC, greater investment in public advocacy for the multilateral trading system would help demonstrate to governments and national polities that they have a strong interest in safeguarding and improving operation of the institution. Adopting the terminology introduced by Hirschman (1970) to describe potential responses to dissatisfaction by actors regarding the performance of an organization, the business community – as the core stakeholder in the system – has a choice between exit, voice, loyalty and neglect.<sup>46</sup>

Arguably, business has engaged in neglect – the reallocation of support and attention to other venues (PTAs), in turn reducing government incentives to engage in the WTO. No government has chosen the exit option yet, but it is nonetheless something that can be exercised. The US position towards the Appellate Body is not something that has been concocted by the US government – it reflects long-standing concerns and advocacy by segments of the US business community. They have an interest in supporting the United States to engage in a constructive dialogue aimed at resolving the matter as opposed to letting a situation arise that leads to the US into a WTO exit scenario. Loyalty and voice – supporting the system and identifying areas for improvement and reform – are necessary conditions for sustaining the viability of the WTO.

Clearly CEOs and corporate boards must do what they deem best for their businesses, workers and shareholders.<sup>47</sup> But that requires at least that a conscious decision is made which of Hirschman's options to exercise vis-à-vis the WTO. It is not clear that the survival of the WTO is a matter that has risen to the level of boardrooms and corporate strategy. Undoubtedly, the Trump Administration's approach towards trade policy has greatly increased the attention being given to the consequences of a sharp reversal towards protectionism in the United States and retaliatory responses for the viability of international supply chains. But this has not translated into a concerted defense of the rules-based trading system and a call to deal with the sources of deadlock that prevail currently. To date business has not been very vocal about the need for governments to use the WTO to address the global rise in protectionism or the need to reconsider WTO working practices that have impeded its effectiveness.

Reaching out to business leaders along the lines of the Director General's 'Trade Dialogues' initiative – which aims at providing stakeholders, including business, labour organizations, and consumer bodies with the opportunity to discuss trade-related matters – is useful but ad hoc and not very demanding upon business. These dialogues for the moment remain closed door events and little is known about how any conclusions are taken up and how they relate to WTO members, which reduces their effectiveness. Making business and other stakeholders a more integral part of the WTO 'production function' may help raise the visibility of the organization and sense of ownership in board rooms.<sup>48</sup> Such engagement need not occur through WTO-organized activities – businesses can and should engage directly with their national parliaments and local communities – but the WTO can support such engagement by involving business representatives more in its deliberations.

In doing so, the focus should be on documenting the local benefits of their international supply chains – identifying their local suppliers and the total employment that is generated by their activities because of the mix of imports and export activity that occurs in their production networks. Many policymakers and citizens may not understand how the mutual dependence that is part and parcel of supply chain-based production depends on a web of contracts and investments. These are premised on a functioning system of rules – the WTO. They can unravel quickly, at

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<sup>46</sup> The option of neglect was added by Withey and Cooper (1989).

<sup>47</sup> One action that CEOs can take is to do more to make the case to their workers and suppliers why the WTO matters to their livelihoods. They need to tell governments and parliaments the same thing. This extends beyond multinational enterprises – SMEs and MSMEs need to be part of this equation given that they are the source of most employment. But it is the largest companies that have the greatest capacity to engage. Unfortunately, many have substantially reduced or eliminated their capacity to engage in trade policy matters in recent years.

<sup>48</sup> In 2013, the WTO surveyed some 300 business representatives about their perception of WTO. An interesting finding was that a majority (56%) thought private sector representatives should participate in WTO training and technical assistance activities, and 90% were of the view that business should be involved in WTO training and capacity building for parliamentarians. The survey, from 2013, was limited to firms producing goods. It revealed, not surprisingly, that 95 percent of respondents think the WTO is important for business and economic growth. Businesses are less impressed with WTO performance: only three-quarters (72%) regarded the WTO as an effective mechanism for control of protectionism, while just three-fifths (62%) thought the Doha Round could deliver benefits to businesses. See [https://www.wto.org/english/res\\_e/booksp\\_e/survey13\\_e.pdf](https://www.wto.org/english/res_e/booksp_e/survey13_e.pdf).

great cost. There is a public good dimension associated with what is suggested here as it will generate information on the employment dimensions of their trade relationships that only firms have regarding their value chains. Such data and the associated stories and examples can be used by the politicians, the WTO Secretariat and journalists to make a more compelling case for why the system matters than one that stresses export volumes and growth in exports.

One action that the WTO membership can consider to encourage greater engagement with businesses is via the normal business of the Committees and other WTO bodies – including critical mass-based deliberative groups. This already happens to a small extent in some of the Committees. Thus, the Committee on Rules of Origin held two information sessions on non-preferential rules of origin in 2016 where business representatives explained how such rules affected their operations. Other Committees have organized workshops with the private sector – e.g., the ITA Committee allowed industry representatives to raise concerns regarding standards for recognition of test results, e-labelling and energy efficiency that could be the subject of work (WTO, 2017b). Although not present in the TBT Committee, the private sector has engaged in informal thematic sessions which are held back to back to Committee meetings. Such interactions help delegations to better understand the concerns of business and vice versa. More such initiatives can put business to work in helping the WTO stay relevant for the global trade community collectively.<sup>49</sup>

## 9 Leadership

Citizens of WTO members generally recognize that the WTO is an important global institution. A recent Bertelsmann Stiftung survey demonstrates that this view is particularly strong in emerging market economies (Figure 7). More than 60 percent of respondents in emerging economies believe that the WTO is an important institution. The percentage is above 70 percent in India and Mexico and rises to more than 80 percent in China. However, only one-third of respondents in the US had a positive perception of the WTO. On average, slightly more than 40 percent of respondents in developed market countries thought the WTO was important. The differences in perceptions suggest that citizens in major emerging economies recognize that the multilateral trading system matters for them and that governments of emerging market economies will have domestic support if they invest greater effort to safeguard the trading system.

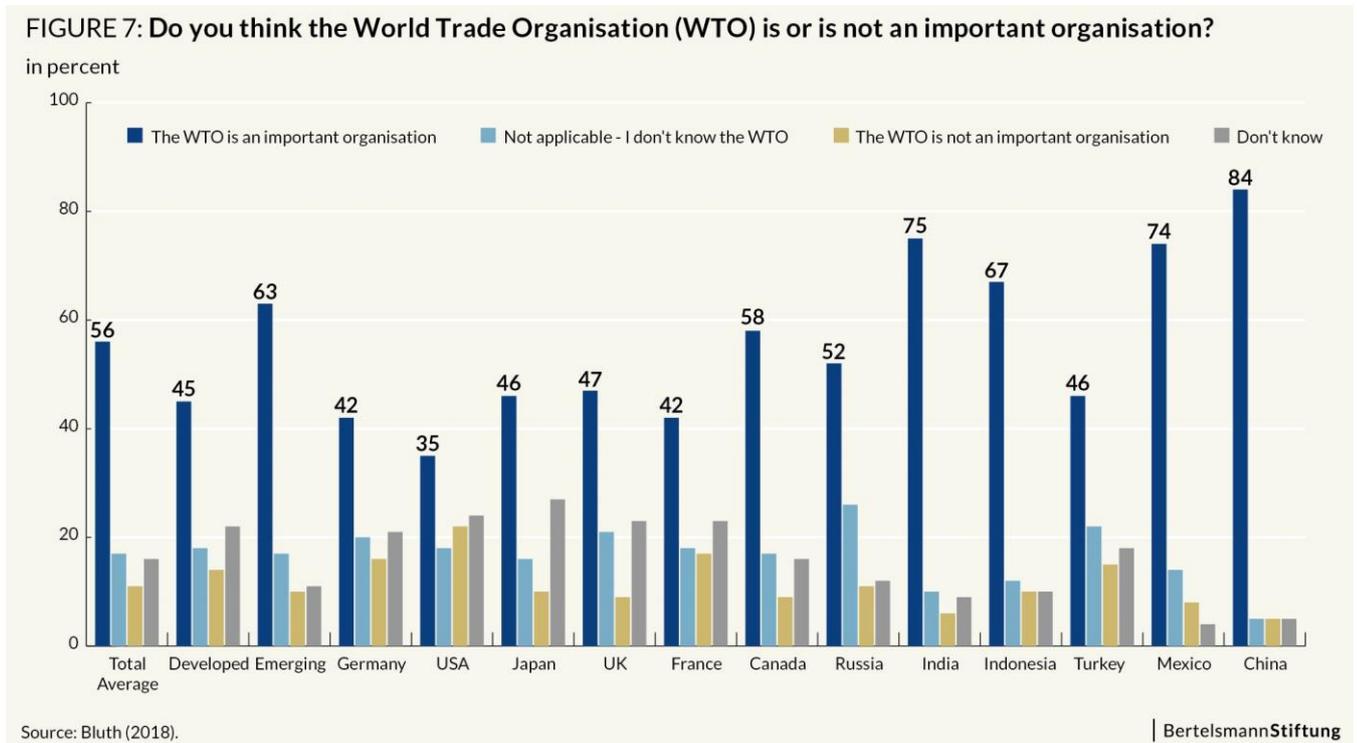
The success of the multilateral trade regime in the post-Second World War period was attributable in large part to US leadership and the fact that the organization was dominated by broadly like-minded countries. Today, it is unclear whether multilateral rule-making remains the central focus of US external trade policy. The US is participating in the joint initiative on e-commerce and is active in the normal WTO committee work, but it is casting itself in a different role than it has in the past, calling for the WTO membership to pursue a WTO reform agenda. It laid out its view of key elements of such a reform agenda at the 11<sup>th</sup> WTO Ministerial Conference in Buenos Aires, stressing a need to focus on compliance with WTO obligations, for greater differentiation among developing countries, and action to ensure that litigation is not used as an alternative to negotiation.

The multilateral trade regime remains a fundamental pillar of the trade strategies of other high-income large trading powers (the EU, Japan) and many smaller OECD member and East Asian economies. Less clear is the position of developing and emerging economy members. These countries have not stepped forward to take up the slack. The Bertelsmann Stiftung's survey data suggest citizens of large emerging economies recognize the WTO's importance but this is not reflected in the stances taken by their governments in the WTO, although a number of members have expressed a need for a stronger multilateral trading system. Safeguarding what has been achieved is important for these countries but perhaps more so is that only the multilateral context offers them the opportunity to influence the

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<sup>49</sup> Other Committees, e.g., TRIMs, SCM, and Import Licensing, three bodies that directly affect many industries, and working groups – e.g., the Working Party on State-Trading Enterprises – do not appear to have much engagement with the business community.

development of new trade rules. What is needed is greater engagement by the emerging economies and smaller countries, developed and developing, in signalling a willingness to confront the challenges that face the WTO.



A noteworthy development in this regard was the call by President Macron of France in May 2018 for the largest trading powers to launch talks on WTO reform, to agree on what is wrong with the current system and to develop a roadmap for new rules that address the distorting effects of subsidies and industrial development policies and measures to attain non-economic objectives.<sup>50</sup> A coordinated effort by large trade powers to invest more of their soft power to support initiatives that are priorities for many WTO members can change the dynamics.

Prospects for this scenario to materialize will be enhanced if China complements its focus on implementing its own vision for plurilateral cooperation, centred on the Belt and Road Initiative and associated project funding mechanisms, with greater engagement in the WTO. This will need to encompass a willingness to discuss measures to address concerns regarding distortions to competition in its markets to level the playing field for foreign companies to participate in – and contribute to – China’s growth.

In Buenos Aires the US made clear that it advocates WTO reform. It is a major economy and a key player in the WTO. Jointly, China, the EU and Japan account for more than one-third of world trade in goods and services. They contribute 56 percent of the WTO budget. Together they can do much to respond to the challenges confronting the organization and revitalize the WTO. Even more powerful would be if East Asia as a region played a greater role, with shared leadership between China, Japan and middle powers such as Korea and Indonesia, together with ASEAN. Leadership cannot come from large trading powers alone. Safeguarding the WTO is particularly important for smaller countries, not least because only the multilateral trading system offers them the opportunity to influence the development of new trade rules. Smaller countries have played a catalytic role in re-invigorating trade cooperation in the past. They need to do so again.

<sup>50</sup> May 30, 2018. See <http://www.elysee.fr/declarations/article/speech-by-the-president-of-the-french-republic-to-open-the-oecd-s-annual-ministerial-council-meeting/>.

Economies pursuing deep integration of markets are best placed to play a complementary role. Examples include the eleven members of the Comprehensive and Progressive Agreement on Trans-Pacific Partnership, the Pacific Alliance countries, the East Asian countries in the Regional Comprehensive Economic Partnership, and, more broadly, the WTO ‘Friends of the Multilateral System’ group of smaller economies.<sup>51</sup> Taken together with the EU, these countries collectively account for over 75 percent of world trade. They constitute a critical mass that is more than large enough to sustain multilateral cooperation and drive the trading system forward.

## 10 Concluding Remarks

The credibility of the WTO is under serious threat, reflected in rising trade tensions between major economies. These are not being addressed in Geneva. WTO members must act to assure the continued relevance of the institution as a platform for States to jointly govern their trade relations. Preserving the multilateral rules-based trading system requires members to address gaps in the rule book that have become increasingly obvious. The ongoing shift towards a global interconnected digital economy calls for international cooperation in a range of new policy areas. Preferential trade agreements cannot fill the gap. They offer partial solutions at best in establishing rules to govern trade and investment flows. Moreover, such agreements depend on the strong foundation of basic rules provided by the WTO and are threatened by the erosion in support for the multilateral trading system.

The WTO must become better attuned to new forms of trade and production that are associated with the growth of emerging economies and the ongoing rise of the digital economy. Increasing cross-border flows of services, data, knowledge and capital call for international rules of the road to provide both producers and consumers with the predictable and effective regulatory framework such transactions require. For this to happen, WTO members must learn, evolve and adapt. WTO rules and working methods need updating. This can be done without changes in the WTO treaties. The WTO provides extensive flexibility for members to engage with each other to discuss perceived problems and explore potential solutions.<sup>52</sup> What is required is leadership, willingness to engage in candid, substantive discussion of perceived problems and possible solutions, and greater engagement by the economic actors for whom preserving and improving the rules-based system is critical and who can no longer take it for granted. Sticking to status quo modes of operating is a recipe for the institution’s gradual demise.

This report identifies avenues that could be pursued by WTO members to foster both incremental and larger changes that would allow the WTO to evolve and adapt to new challenges and new forms of trade while, at the same time, being more responsive to economic development needs and differences in preferences and priorities across members. The underlying premise is that inertia and complacency constitutes a danger for WTO survival. The suggestions focus on ways in which WTO members can use the existing institutional framework to unlock the deliberative function of the organization to consider solutions to systemic policy conflicts that call for updating the multilateral rulebook.

Some of the recommendations made in this report imply a reconsideration of basic approaches that have guided multilateral trade governance for some time. They do not imply changes to the WTO treaties or structure, but they do constitute changes in modus operandi and may not be uncontentious. The basic premise underlying the recommendations is that deliberation – policy dialogue – is critical to prevent trade tensions and disagreements on the functioning of the dispute settlement system resulting in a systemic crisis.

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<sup>51</sup> The Friends of the Multilateral System, comprises Albania; Argentina; Australia; Bangladesh; Benin; Canada; Chile; Colombia; Costa Rica; Dominican Republic; Ecuador; El Salvador; Ghana; Guatemala; Hong Kong, China; Iceland; Israel; Kazakhstan; Republic of Korea; Lao People’s Democratic Republic; Liechtenstein; Malaysia; Mexico; Montenegro; Moldova; Myanmar; New Zealand; Nigeria; Norway; Pakistan; Panama; Papua New Guinea; Paraguay; Qatar; Russian Federation; Singapore; Sri Lanka; Switzerland; Chinese Taipei; Thailand; The former Yugoslav Republic of Macedonia; Tonga; Turkey; Ukraine; Uruguay; Vanuatu; Viet Nam. Together these countries account for some 40 percent of global trade.

<sup>52</sup> Many of the policies giving rise to trade tensions and debates today can be ‘mapped’ to one or more already existing WTO bodies overseeing implementation of WTO agreements or as established to discuss a given issue. Matters such the distortions to competition arising from the behavior of state-owned enterprises; policies on technology transfer; or domestic regulation of services activities can be discussed in existing WTO bodies dealing with closely related subjects. Some WTO bodies that have become inactive – e.g., groups dealing with trade and investment; trade and competition; and transparency in government procurement – could be resuscitated and used to engage in policy dialogue.

The foregoing has not engaged in any depth with the question what the priorities for action are or should be. This reflects a view that this cannot be prejudged but should emerge from dialogue between WTO members. Clearly addressing the stand-off on the Appellate Body is a priority from a systemic perspective. Arguably another priority from a systemic view is to assess where the rulebook needs to be updated to provide a stronger foundation for digital trade and assuring a level playing field for companies operating internationally.

Dialogue is needed both to identify the relative size of negative spill-over effects of different types of national policies that are only partially covered by WTO rules, and for countries to identify good trade practices that will promote sustainable development. Cooperation on the latter – an important part of the agenda for global trade governance – does not necessarily require a single undertaking-based negotiation with issue linkages and trade-offs. Other forms of cooperation may be more appropriate. Discussion on the magnitude of the spill-overs of different policy choices is important to identify which ones matter most. To date, the WTO has limited itself to monitoring new trade restrictive measures. This is insufficient. The large number of potentially trade-distorting measures that have been imposed since the 2008 financial crisis and the policy conflicts that have arisen between the largest trading powers call for a more proactive stance by WTO members.

Efforts to revitalize the WTO should include a focus on bolstering the regular operations of the WTO. This requires a willingness to reflect and assess on a committee-by-committee basis what is needed to fulfil their functions – starting with asking what information is required and learning from experience within and without the organization how best to obtain it. Considering whether WTO agreements constitute good practices and a dialogue on what would promote economic development can help determine whether a new consensus can be crafted on how to address development concerns. This must encompass areas of policy that are of great importance to many developing countries, such as agriculture subsidies and tariff escalation, as well as sustaining the aid for trade initiative to provide support to address supply side constraints.

Pursuit of open plurilateral initiatives is part of the solution to the deadlock that characterizes the status quo. These need not be restricted to further reductions in tariffs along lines of the ITA or a prospective Environmental Goods Agreement. They can also involve deepening disciplines and/or the development of guidance to better implement policy areas already subject to WTO rules or that have yet to be covered by international disciplines. The launch by groups of WTO members of four joint initiatives at the 11<sup>th</sup> Ministerial Conference in 2017 on a variety of subjects is a very positive development for the trading system. Such initiatives are not a panacea. But neither are bilateral, regional or even mega-regional PTAs.

Scepticism has become a feature of attitudes in some countries towards multilateral trade cooperation. Care must be taken that the baby is not thrown out with the bathwater. While some PTAs have addressed subjects that have given rise to disagreement in the WTO – competition policy, public procurement transparency and access, and investment-related policies – several recent efforts to negotiate deeper PTAs have also confronted political difficulties. All countries, large and small, have a major stake in an effective, rules-based multilateral trading system. In Buenos Aires, the US called for WTO reform; this has been echoed more recently by President Macron. What is needed is to launch a process of open dialogue to discuss what reforms are desirable.

Recognizing the shortcomings of the trading system as it stands today is a first step. The inability of WTO members to update the rules has put pressure on the WTO dispute resolution mechanisms and resulted in imbalances and gaps. The world economy has evolved, as have domestic policies of in major WTO members. There is a corresponding need to re-balance the rules to ensure that prevailing policies are subject to multilaterally defined disciplines that reduce the scope for trade and competition distortions. Such re-balancing should extend to past commitments – including instances where countries acceding to the WTO were requested to take on stronger disciplines than those applying to incumbent members. Determining how to create real level playing conditions for companies operating in foreign markets is an important part of the agenda.

There are several necessary conditions for the ideas put forward here to make a difference. One is that China and other emerging countries recognize the value of a functioning multilateral trade regime to themselves and the threat to the system associated with a business as usual stance. A key dimension of this is readiness to engage in efforts to clarify and extend existing rules to ensure greater equality of competitive conditions. Another necessary condition is to ensure that the advantages of special and differential treatment in all its forms are directed towards countries that most need it – and that such WTO provisions actually support sustainable development.

Willingness to support greater reflection on the effects of national trade-related policies and the performance of the WTO is critical for revitalizing the institution. Pessimism can easily become a self-fulfilling prophecy. Launching processes centred on policy dialogue and institutional learning is a first step to re-establishing an environment that supports constructive engagement and regenerates the trust needed to revitalize the WTO negotiation function. Progress will be incremental and will require pragmatism. While the trading system is undergoing a serious stress test, the current crisis offers an opportunity. Hopefully it will become a step in a transition towards a multi-lateral trade regime that is more adapted to the world of today.

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## 12 Annex

### 12.1 Annex 1: Alternative Instruments for Trade Cooperation under the WTO

The table below maps types of issues where international cooperation may be beneficial against instruments that can be used in the context of the WTO. Four types of issues and associated objectives are listed in the left-hand column. The first comprise national policies that apply equally to domestic and foreign products or firms. Examples are product standards and sector-specific regulation. Differences in policies across countries may generate transactions costs for international firms because of duplicative, redundant testing and certification requirements, or because of uncertainty in how policies will be applied. More generally, trade costs may arise because policy in a country increases entry costs for new competitors or new products, whether foreign or domestic. Efforts to attenuate the scope of such spill-overs can take the form of open plurilateral cooperation that centres on determining good practices in the relevant policy area.

ANNEX TABLE 1: Alternative Instruments for Trade Cooperation

		Instrument		
		Small group cooperation		Large group cooperation
		Non-discriminatory application	Applied on a conditional basis	Non-discriminatory application
Types of issues/objectives	Reduce trade costs caused by differences in policies ('trade facilitation')	CMA (E.g. MC11 E-commerce group)	Mutual recognition; regulatory cooperation (E.g. EU-US aviation)	Multilateral agreement (E.g.: TFA)
	Reduce differences in social norms and standards ('social preferences')	CMA (E.g. regulatory coherence)	Deeper (unilateral) trade preferences (E.g.: EU GSP+)	CMA (Committee on Trade & Environment)
	Address negative effects of a discriminatory/anti-competitive policy ('market access')	CMA (E.g. Telecom Reference paper)	Plurilateral agreement (Article II.3 WTO) (E.g., GPA)	CMA (E.g.: ITA; EGA)
	Address negative effects of several discriminatory policies (> 1 'market access issue')	N.A.	Preferential trade agreement (E.g. CPTPP, TISA)	Multi-issue package deal ('single undertaking') (E.g.: Doha round)

Notes: N.A.: not applicable. CMA: critical mass agreement. GSP: Generalized system of trade preferences for developing countries. EGA: Environmental Goods Agreement (under negotiation). ITA: Information Technology Agreement. TISA: Trade in Services Agreement (under negotiation).

Source: Hoekman and Sabel (2018). | BertelsmannStiftung

A feature of such agreements is that their application benefits all countries. However, the scope for non-discriminatory application of an agreement is limited if a precondition is a minimum level of regulatory quality. This constraint arises for product standards, where cooperation may take the form of mutual recognition agreements that allow products to be imported without additional testing or conformity assessment. Such agreements ensure that each country has a regulatory framework that assures the others that products conform to regulatory requirements. Countries that do not have such regulatory frameworks will not be able to benefit from mutual recognition or equivalence arrangements. Benefits are conditional. In the case of product standards, WTO rules require such arrangements be open to any country that wishes to participate once an agreement has been established. Extending this principle to any CMA that aims at reducing regulatory externalities will ensure that countries not part of an initial arrangement can join subsequently if they desire to and have the capacity to implement that regulatory framework.

The second category relates to social preferences and norms. Many such norms have been agreed multilaterally in other fora, and cover human rights, political and civil rights, labor standards and measures to protect the environment. Such norms are not specific to products. There are long-standing debates among WTO members regarding the benefits of including such norms in WTO agreements. Proponents of doing so argue that this will increase political support for the WTO by supporting the realization of what has been agreed internationally to constitute minimum standards and address claims that trade between countries with very different levels of social standards constitutes 'unfair competition' or is simply ethically unacceptable. In the case of nonreciprocal trade preference programs, preferential access has been conditioned on the implementation of certain labor standards or environmental regulation – an example is the GSP+ regime applied by the EU. This is possible because the

design trade preference schemes are not subject to WTO rules – the only constraint is that a scheme applies to all developing countries.

Long-standing views of most developing countries are that the WTO, as a trade organization, is not the right place to negotiate these political, civil and social issues. Concerns that “unfair competition” arguments are aimed at depriving lower-income economies from benefitting from their comparative advantages have been a prominent factor underlying opposition to proposals that the WTO agree to rules pertaining to labour or environmental standards, although bodies have been created to discuss some such matters – e.g. the Committee of Trade and Environment. CMAs offer a vehicle for those WTO members that want to discuss avenues for cooperation on these issues to do so. The Joint Declaration on Trade and Women's Economic Empowerment that was supported by 119 WTO Members illustrates the potential that may exist.<sup>53</sup>

A third type of situation is where a policy is designed to benefit domestic economic actors and this may generate adverse effects for trading partners. This is essentially the core market access agenda that is the bread and butter of the WTO. It encompasses policies such as tariffs, subsidies, local content restrictions and export support, as well as sector-specific regulation that gives domestic incumbents a competitive advantage. What characterizes cooperation in such instances is that agreements on trade-distorting measures (discriminatory policies) must encompass all major trading nations or it must be possible to restrict benefits to signatories of a deal. Countries will be unwilling to give a trade concession to another country if, by doing so, third countries can free ride. The WTO MFN rule requires any concession to be applied to all trading partners.

Unlike in the case of domestic policies considered in row 1, where the MFN rule does not impede cooperation because the policies concerned apply on a non-discriminatory basis, free-riding concerns mean that cooperation must either permit non-participants to be excluded or span a critical mass of countries. GATT and WTO experience suggests that in the case of tariff negotiations where concessions must be implemented on a most-favored-nation basis, critical mass requires countries accounting for some 80-90 percent of total trade in the relevant products to participate. If this cannot be achieved, Article II.3 WTO Plurilateral Agreements are an alternative as these allow WTO members to agree to rules for a single issue and restrict the benefits to signatories. However, as discussed previously, such discriminatory Plurilateral Agreements require the approval of all WTO members.

The final category concerns situations where it is not possible to agree on an issue-by-issue basis. Cooperation then requires multiple issues to be bundled into a package. WTO Members have two options in such cases. They can either negotiate a PTA or pursue a multilateral, multi-issue negotiation under WTO auspices. A PTA is inherently limited as it will only span some countries, but benefits will be restricted to signatories. In the case of a multilateral WTO round, the MFN constraint binds. The rationale for a multi-issue negotiation may not be limited to the fact that there is no scope to agree to CMAs on an issue-by-issue basis (along ITA lines) because some countries will lose out from whatever is being tabled. Some countries may support a multi-issue negotiation because of a perception that the overall potential gains will increase by putting more issues on the table. Whatever the case may be, issue linkage is a core feature of negotiations that span multiple policy areas.

Cooperation centred on good regulatory practices to facilitate trade is relatively insensitive to free riding considerations. Because the primary focus is on identifying policies that are in the self-interest of countries to implement, there is also no need for issue linkages. Indeed, efforts to link different issues may impede agreement by shifting the focus away from defining good practices towards quid pro quo bargaining that characterizes negotiations on subjects where changes in policies give rise to political costs for governments. Nor is it necessary that all major trading powers are part of an agreement. While broad membership increases overall benefits, all that is necessary for cooperation is that enough countries are part of the process to justify participation costs. Given that free-riding concerns are not a binding constraint for policy reform, the ‘critical mass’ required to make cooperation on regulatory policies beneficial is much smaller than in cases where countries impose discriminatory policies that create significant adverse effects on trading partners.

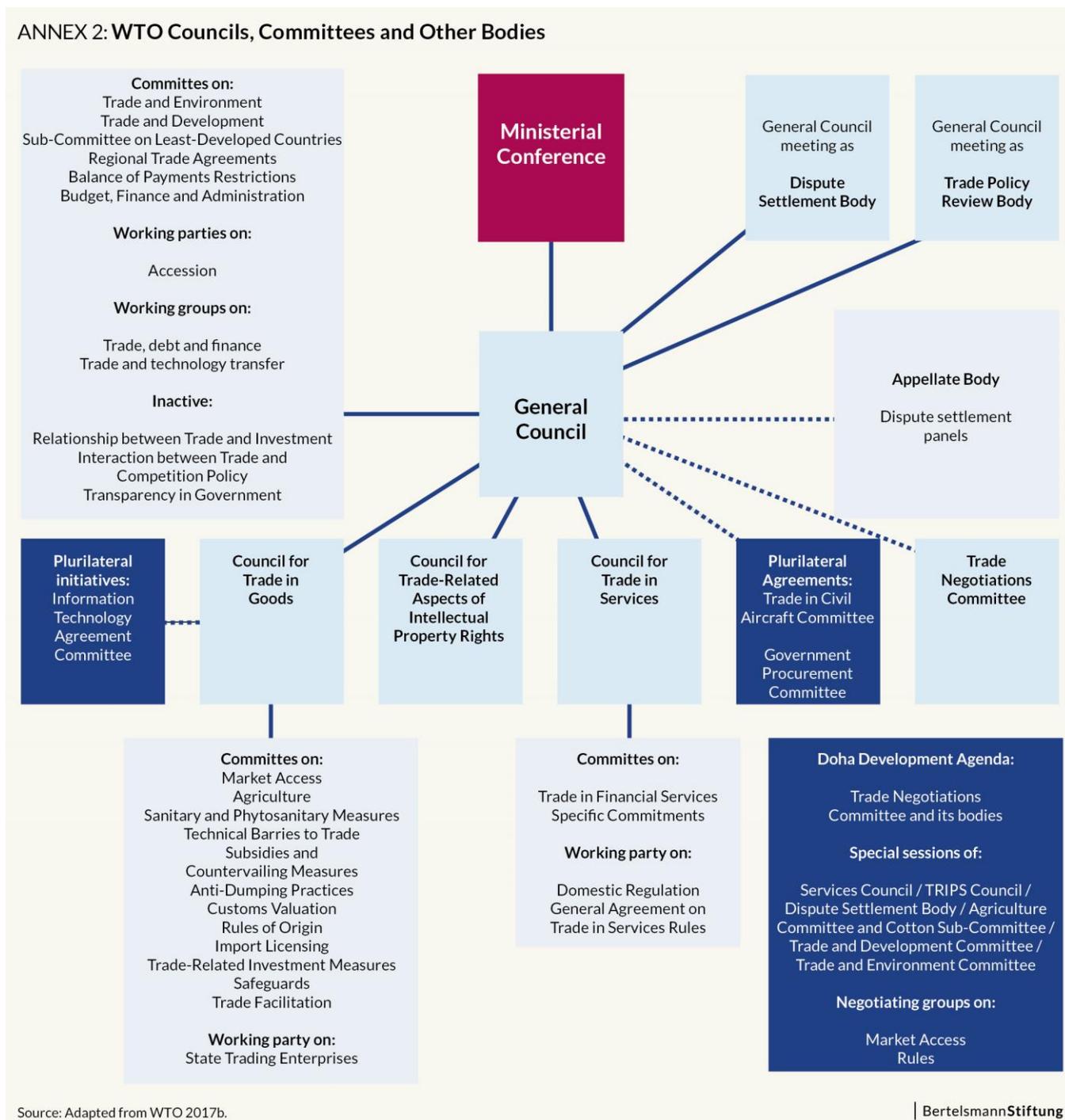
Moreover, cooperation that centers on identifying good policy practice does not need to constitute ‘hard law’ – there is less need and, indeed, less scope, for binding dispute settlement procedures where the ultimate sanction is the

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<sup>53</sup> Joint Declaration on Trade and Women's Economic Empowerment on the Occasion of the WTO Ministerial Conference in Buenos Aires in December 2017. At: [https://www.wto.org/english/thewto\\_e/minist\\_e/mc11\\_e/genderdeclarationmc11\\_e.pdf](https://www.wto.org/english/thewto_e/minist_e/mc11_e/genderdeclarationmc11_e.pdf).

threat of withdrawal of trade concessions (retaliation). If a country no longer applies what was agreed to be good practice it makes no sense to respond by doing the same – both because this will at most have only a small effect on the trading partner and, more important, doing so will be costly as the practice by assumption is beneficial to apply – otherwise it would not have been adopted in the first place. In situations where a party to an agreement decides no longer to apply an agreed practice the appropriate response is to assess the reasons for this decision. If it reflects political economy forces in the partner country driven by rent-seeking behavior by vested interests, this is not a reason to change one's own policy. Alternatively, if the change can be justified as enhancing national welfare, there may be reason to revisit the presumption that the policy constitutes good practice. In principle, however, situations where a party comes to believe there is a better way of regulating should give rise to discussion between parties to an agreement.

## 12.2 Annex 2: WTO bodies





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