Trade Politics



International, Domestic and Regional Perspectives

Edited by
Brian Hocking and Steven McGuire

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Trade politics

Trade politics is becoming increasingly complex. There have long been disputes about free trade and protectionism, but changes in economic activity and the rise of large trading blocs have made international negotiations over trade a much more difficult process.

This book explores changes in trade politics such as linkages with human rights, the importance of cultural distinctiveness and the erosion of national boundaries, taking a multidisciplinary approach. It is divided into three parts. The first is concerned with the evolving trade environment and the growing diversity of issues it now embraces. The second examines the patterns of dependence, interaction and conflict amongst governments, firms and non-governmental organizations (NGOs). The third looks at the major geographical areas of the global economy and the particular issues they face.

Trade Politics provides a comprehensive survey of the changing world trade environment. It contains insights and considered analysis that will be invaluable to students wishing to make sense of a complex and fast changing situation.

Brian Hocking is Professor of International Relations at Coventry University. **Steven McGuire** is Lecturer in International Management at Royal Holloway College, University of London.

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Preface

Books about international trade focus for the most part on the negotiation of various forms of trade agreement, particularly successive 'rounds' of multilateral negotiations within the General Agreement on Tariffs and Trade. The stories recounted become more intricate as the years move on and the issues involved become more complex, but they are concerned primarily with trade policies: that is to say, the objectives pursued by national governments and the strategies deployed in the attempt to achieve them. Such stories have provided valuable insights into what is recognized to be one of the most significant areas of international relations. But it has become increasingly clear that the trade agenda is changing in ways that are fundamentally altering the environment in which policies are fashioned—whether at the subnational, national or international levels. One way of expressing such developments would be to suggest that a greatly expanded cluster of political activity is emerging around the shaping of trade policy. Politics and trade, of course, are no strangers to one another. Debates concerning the merits and demerits of free trade and protectionism reflect fundamental political choices confronting policy makers and their domestic constituencies. The changing agenda of trade itself provides part of this transformational landscape, reflecting the rise of 'new' trade issues such as financial services and intellectual property. However, onto these are being grafted issues with which trade negotiators of half a century ago would have had little experience or direct concern. Thus trade policy has now acquired both human rights and environmental dimensions which, whilst they certainly add new facets to the conduct of trade diplomacy, appear to do more than this. At one level, they are helping to create a situation in which the very nature of what was a relatively closed area of public policy has become opened up to a range of influences articulated by a growing diversity of actors.

This can be viewed as one facet of the growing integration of the global economy which has diminished the relative significance of border trade issues in favour of those which strike at the very heart of social and cultural distinctiveness amongst national communities. Few have become so emotive, or pose challenges to the right of communities to maintain differing standards (notably in the context of trans-atlantic trade relations) than those which might be designated as 'food politics'. As a result, what would once have been regarded as matters of personal or collective preference in food regulation have now become issues of the highest significance to trade diplomacy. Looked at more broadly, as a result of these and other related developments, the nature of foreign economic policy is changing in several important respects. This involves a

gradual erosion of boundaries marking off significant aspects of the policy processes as a result of issue-linkage, the growing patterns of interaction between governmental and non-governmental actors and the visible intermeshing of subnational, national and international political arenas in ways that erode traditional assumptions as to the points of interaction between them. Taken together, these developments have produced a much more intricately textured, multilayered environment for trade politics within which distinctions between domestic and international policy processes have become increasingly eroded.

The central aim of this book is to explore these changes. In so doing, we have sought to bring together specialists from several disciplines, each focusing on a specific dimension of the emerging trade environment. Taken together, the three parts provide a multidimensional perspective on the changing trade politics milieu. Thus the focus of Part I is, first, the evolving environment in which trade is conducted and, second, the growing diversity and complexity of issues which the trade agenda now embraces. Part II explores the patterns of interaction between the dominant actors generated by these issues and the patterns of dependence and conflict between business and government and, increasingly, non-governmental organizations. The aim of the third part is to explore the character of trade politics in the major geographical areas of the global economy, analysing the characteristics of the region, the key issues within it and the implications of the trends discussed in the first two parts. Overall, then, we have attempted to provide readers with a reasonably comprehensive picture of the emerging patterns of trade politics and the challenges that these present to national governments, subnational actors and to international institutions, principally the World Trade Organization.

The book has taken far longer to emerge than we originally anticipated. Perhaps this is inevitable given the number of contributors involved in the project, each having many other commitments. Our thanks are due, therefore, to all who have contributed, some at very short notice in the latter stages of production, and, particularly, to those whose chapters were submitted early on for their continuing patience. Several authors—and other colleagues—have, additionally, offered general and specific advice for which we are grateful. Other debts incurred are to Dominic Kelly, Research Fellow at Coventry University, for his editorial assistance, and to Kath Wright, whose assistance in preparing the final manuscript was invaluable. We also wish to thank members of the Routledge editorial staff, particularly Victoria Smith and Mark Kavanagh, for their patience and advice as the original proposal took shape and, despite last minute hitches, finally saw the light of day. And, by no means least, we owe a great debt of gratitude to our families for their support and understanding in yet another project which impinged on time that is as much theirs as ours.

Brian Hocking
Steven McGuire
May 1999

Abbreviations

ACP	African, Caribbean and Pacific
AEC	African Economic Community
AFTA	ASEAN Free Trade Area
AMS	Aggregate Measurement of Support
APEC	Asia-Pacific Economic Co-operation
ASEAN	Association of South-East Asian Nations
ASEM	Asia-Europe Meeting
BGMEA	Bangladesh Garment Manufacturers and Exporters Association
BITS	Bilateral Investment Treaties
C^3I	Command, Control, Communications and Intelligence
CAP	Common Agricultural Policy
CARICOM	Caribbean Community and Common Market
CEC	Commission for Environmental Co-operation
CEEC	Central and East European Countries
CER	Closer Economic Relations
CFCs	Chlorofluorocarbons
CFSP	Common Foreign and Security Policy
CITES	Convention on International Trade in Endangered Species
COCOM	Co-ordinating Committee for Multilateral Export Controls
COMESA	Common Market of Eastern and Southern Africa
COPA	Comité des Organisations Professionnelles Agricoles
COREPER	Committee of Permanent Representatives
CP	Contracting Party
CTE	Committee on Trade and Environment
DES	Data Encryption Standard
DSB	Dispute Settlement Body (WTO)
DSU	Dispute Settlement Understanding (WTO)

EAI	Enterprise for the Americas Initiative
EC	European Community
ECA	Economic Commission for Africa
ECLAC	Economic Commission for Latin America and the Caribbean
ECOWAS	Economic Community of West African States
ECSC	European Coal and Steel Community
ECU	European Currency Unit
EEC	European Economic Community
EEP	Export Enhancement Program
EES	Escrowed Encryption Standard
EFTA	European Free Trade Area
EJC	European Court of Justice
EMU	European Monetary Union
EP	European Parliament
EPZ	Export Processing Zone
ERRA	European Recovery and Recycling Association
EU	European Union
Euratom	European Atomic Energy Community
FDI	Foreign Direct Investment
FOGs	Functioning of the GATT system
FTA	Free Trade Association
FTAA	Free Trade Area of the Americas
G-10 countries	Group of Ten (Belgium, Canada, France, Germany, Italy, Japan, Netherlands, Russia, Sweden, UK, USA, Switzerland)
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
GMOs	Genetically Modified Organisms
GSP	Generalized System of Preferences
IBASE	Brazilian Institute for Social and Economic Analysis (Rio de Janeiro)
ICFTU	International Confederation of Free Trade Unions
ICTSD	International Centre for Trade and Sustainable Development
IDB	Inter-American Development Bank
ILO	International Labour Organization

IMF	International Monetary Fund
IP	Intellectual Property
IPE	International Political Economy
IPRs	Intellectual Property Rights
ISA	International Strategic Alliance
IT	Information Technology
ITC	International Trade Commission
ITO	International Trade Organization
ITU	International Telecommunications Union
IUCN	International Union for Conservation of Nature and Natural Resources
LDC	Less Developed Countries
MAI	Multilateral Agreement on Investment
MCA	Monetary Compensatory Account
MEAs	Multilateral Environmental Agreements
MEP	Member of the European Parliament
Mercosur	The Southern Cone Common Market (South America)
MFA	Multi-Fibre Arrangement
MFN	Most Favoured Nation
MITI	Ministry of International Trade and Industry
MNC	Multinational Corporation
MNE	Multinational EnterpriseMRA Mutual Recognition Agreement
MTN	Multilateral Trade Negotiations
MTS	Multilateral Trading System
MWENGO	*Mwelekeo we* Non-Governmental Organization
NAFTA	North American Free Trade Agreement
NGO	Non-Governmental Organization
NIC	Newly Industrialized Country
NIDL	New International Division of Labour
NIDP	New International Division of Power
NIEO	New International Economic Order
NIST	National Institute of Standards and Technology (USA)
NSA	National Security Agency
NTB	Non-Tariff Barrier

OAS	Organization of American States
OAU	Organization for African Unity
OECD	Organization for Economic Co-operation and Development
OEEC	Organization for European Economic Co-operation
OMA	Orderly Marketing Agreement
PAFTAD	Pacific Trade and Development Conference
PECC	Pacific Economic Co-operation Council
PGA	Peoples' Global Action against 'Free' Trade and the World Trade Organization
PGP	Pretty Good Privacy
PPMs	Production and Processing Methods
PRI	Institutional Revolutionary Party (Mexico)
QMV	Qualified Majority Voting
R&D	Research and Development
RMALC	Mexican Action Network on Free Trade
RSA	A public key encryption algorithm named after the inventors Rivest, Shamir and Adleman
SAA	South African Airways
SACU	South African Customs Union
SADC	South African Development Community
SANGO	South African National NGO Coalition
SAP	Structural Adjustment Policy
SEA	Single European Act
SEM	Single European Market
SIGINT	Signals Intelligence
SME	Small- and Medium-Sized Enterprise
SMP	Single Market Programme
SPS	Sanitary and Phytosanitary
SSA	Sub-Saharan Africa
TABD	Trans-Atlantic Business Dialogue
TBT	Technical Barriers to Trade
TEU	Treaty on European Union
TNCs	Transnational corporations
TPRM	Trade Policy Review Mechanism (of the WTO)

TRIMs	Trade-Related Investment Measures
TRIPs	Trade-Related Aspects of Intellectual Property Rights
UCC	Universal Copyright Convention
UK	United Kingdom
UN	United Nations
UNCED	United Nations Conference on Environment and Development
UNCITRAL	United Nations Commission on International Trade and Law
UNCTAD	United Nations Committee on Trade and Development
UNESCO	United Nations Educational, Scientific and Cultural Organization
UNICEF	United Nations International Children's Emergency Fund
US	United States
USA	United States of America
USTR	Office of the United States Trade Representative
VER	Voluntary Export Restraint
VRA	Voluntary Restraint Agreement
WEDO	Women's Environment and Development Organization (New York)
WEF	World Economic Forum
WIDE	Women in Development Europe (Brussels)
WIPO	World Intellectual Property Organization
WTO	World Trade Organization
WWF	World Wide Fund for Nature

Introduction

Trade politics: environments, agendas and processes

Brian Hocking

As has frequently been noted, trade, together with war, constitutes one of the oldest modes of international communication and affects the well-being of an ever larger segment of the world's population. Moreover, there is a strong presumption that these effects are positive; that international trade, by means of the principle of comparative advantage, can provide benefits way beyond those which individuals or communities in isolation could provide for themselves. But, in practice, we know from hard experience that the shaping of trade policies is one of the most politically contentious of exercises. The reasons are obvious. Favouring free trade over protectionist policies, or vice versa, is likely to have a differential effect on groups within and across national boundaries. Decisions made by policy makers to reduce or increase tariffs on particular goods have thus been amongst the most sensitive of political acts and ones that have been the subject of bitter dispute. Generalized statements about the advantages of free trade are unlikely to be compelling if cheap imports lead to the dole queue. Given this, it is not surprising that, in many political systems over time, political parties have been identified in terms of their orientation towards free trade or protectionist principles.

But trade policy makers now have to operate in a far more complex environment, partly because an already highly politicized area is becoming more so. When one of the seminal studies of trade politics—Schattschneider's study of the passing of the 1930 Smoot-Hawley Tariff by the US Congress—was published in the mid-1930s, its focus was clearly on the ways in which protectionist interests succeeded in capturing Congress.[1] However, the sites of political contestation built around the trade agenda have increased vastly. Certainly, the free trade-protectionist arguments have lost none of their thrust. Rather, enhanced interdependence and globalization have reinforced them as across the world, groups of workers find themselves lashed by the storms of economic and social change. The language and context may have changed: 'fair trade' arguments now confront the free trade case but the essential debate about the benefits and disbenefits of opening up versus restricting access to markets remains.[2]

Nevertheless, as elsewhere, the US trade agenda has moved on during the half-century since Schattschneider's book was published. Now, the waters of trade politics swirl around new rocks. It is not simply, as various chapters in this book demonstrate, that the nature of what is being traded has changed. Certainly, against the continuing arguments about agriculture, with its own constellation of forces as

illustrated in Balaam's chapter, the rise of services—telecommunications and financial services (Kostecki, Chapter 4), for example—generates new concerns. But understanding the politics surrounding the creation and development of the North American Free Trade Agreement (Cooper, Chapter 14), to take but one instance, leads us beyond the arguments deployed by various business interests and into the politics of human rights, the environment and the respective powers of the federal and state governments in a globalizing economy. We only have to look at the current list of trade disputes to see how the traditional debates are interwoven with these new concerns as discussed by van Liemt (labour standards, Chapter 7) and Brack (environmental issues, Chapter 8):

- disputes between the United States and the European Union (EU) over a series of food-related issues, including genetically modified foodstuffs;
- the long-running argument between Washington, American business interests and governments and firms around the world on federal and state-level sanctions policies directed towards, amongst others, Cuba, Iran, Libya and Burma;
- conflict between India, Malaysia, Pakistan and Thailand on one side and the United States on the other over the latter's ban on the sale in the United States of shrimps caught in nets that do not allow sea turtles to escape;
- pressures brought to bear on governments and firms on human rights grounds, as with Occidental Petroleum in Colombia and Shell in Nigeria.

What is noticeable in these and many other cases is how the traditional arguments about free trade and protectionism are overlain with new issues sponsored by actors, particularly the ever expanding list of non-governmental organizations (NGOs), whose concerns now firmly impinge on the trade politics agenda (see Cloutier, Chapter 11, and Scholte, Chapter 10).

Thus enhanced issue complexity generated, as Woolcock's chapter demonstrates, by the evolution of the trade agenda beyond its preoccupation with tariff reduction in the early GATT (General Agreement on Tariffs and Trade) negotiating rounds, to embrace the much more complex problems associated with non-tariff barriers (NTBs) and trade in services, meets another form of complexity produced by processes of issue-linkage. Policy makers, thereby, find the conduct of intergovernmental trade policy to be much more testing—not least because the texture of contemporary trade politics is enriched by the emergence of new networks of non-governmental influence on processes which have been regarded as relatively insulated from the attentions of all but a select band of players. However, these developments present problems for the analyst as well as the policy practitioner. How do we describe and explain what is happening in this part of the policy agenda?

As many of the following chapters clearly indicate, the landscape of contemporary trade politics sits uncomfortably with realist, state-centred approaches to international relations, for at least two reasons. First, there is a presumption in such approaches that politics and economics inhabit separate worlds and that, in terms of international relations, it is political relationships, informed by the pursuit of power, that are

dominant. This has never appeared to constitute a compelling argument but, in the light of the growing integration of the global economy and the enhanced significance of economics in world politics, looks increasingly tenuous. As proponents of 'complex interdependence' pointed out in the 1970s, the notion that there is an automatic hierarchy of issues on the international agenda—'high' and 'low' politics—with economic issues relegated to the second category, below that represented by the military—security agenda, fails to take account of their significance in determining outcomes in world politics or the inherent fluidity of the categories themselves.[3]

Second, the very nature of trade policy, with its focus on balancing the economic interests of a range of domestic constituencies, undermines the notion of the state as a unitary actor, pursuing a clear and identifiable 'national interest'. Indeed, in many senses, trade politics, concerned as it is with the distribution of resources within and between political communities, is the most intensive manifestation of the processes determining who gets what, why and how. And as the trade agenda becomes more complex, explaining how trade policy is formulated and articulated demands that the role and interactions of a range of governmental and non-governmental actors be taken into account.

This is not to suggest that the nature of contemporary trade politics provides further evidence for the argument that the state is in a condition of terminal decline, in the face of multifaceted challenges subsumed under the term 'globalization'. As is recognized in much of the literature exploring this contested concept, an increasingly integrated global economy and enhanced communication flows are having more subtle effects on national governments than is often suggested.[4] The state may be challenged, its functions may be changing, but it is not powerless.[5] In this phase of the evolution of the Westphalian system, we are witnessing a dialogue between the forces of interdependence and globalization on the one hand and territoriality on the other. Far from resulting in the demise of the appeal of the locality in its various, territorially expressed, forms, the pressures generated by global economic forces are reinforcing the function and the appeal of national and subnational political communities.

The central problem in explaining the complexities of trade politics lies in disentangling the impact of influences at the systemic, state and substate levels. This, of course, is a problem common to all aspects of world politics. The literature of international political economy and foreign economic policy is replete with explanations as to the behaviour of governments in fashioning their international policies.[6] Whilst some may veer towards systemic factors, others emphasize the significance of decision-making processes and yet others focus on the nature of national societies, there is a significant consensus that no one level of analysis can, alone, provide a satisfactory account.[7] On the one hand, systemic theories do little more than explain broad policy characteristics. Statist approaches fail to penetrate the complexities of decision-making processes. Societal explanations, whilst providing a far richer tapestry of policy influences and exposing the limitations of an assumed national interest, can easily lead to the belief that policy is simply the expression of conflicting domestic constituencies, with policy makers exercising little or no influence over the shaping of public policy. The problem is highlighted in the trade

policy sphere in terms of arguments concerning the relationships between government and multinational business enterprises (MNEs). Here, it has become conventional wisdom, certainly within a certain sector of the globalization literature, that MNEs, having outgrown the confines of national economies, have relatively little concern with territorial 'place' and the governments that preside over it.[8] Others, however, sketch more subtle pictures, arguing that business works with state bureaucracies in promoting the interests of both sets of actors, an argument reflected in this depiction of the relationship between US government and big business:

> The extent to which MNCs [multinational corporations] are successful depends on the depth of their institutional ties to political elites in the United States and elsewhere, and on the resistance to their policies by domestic social actors, including domestic business firms and labor interests.[9]

Recognition of less clear-cut relationships such as this has prompted many analysts to develop 'integrative' approaches giving due weight to domestic influences whilst assigning a clear role to the policy maker at the point of interface between international and domestic negotiating environments.[10]

Certainly, as the contributions to this book make clear, understanding trade politics demands that we adopt broad, 'multiperspectival' approaches to understanding trade politics. Rather than engaging in debates as to whether one actor or another is of primary significance, what is needed is a recognition of the linkages and interactions between actors and the arenas in which they operate. A key theme of this book is the importance of linkages, such as those between the domestic and international dimensions of public policy, and continuities between issues, actors and political arenas.

Environments

One of the central features of the changing environment of trade politics is the erosion of the boundary demarcating the pursuit of the political in international policy (foreign policy) and the economic (foreign economic policy). As noted above, this distinction has frequently been expressed in terms of the relationship between high and low policy, a distinction which has become far less easy to sustain as economic issues on the international agenda have risen in prominence and economic and political issues have become evermore intertwined.

The setting after World War II favoured the intermeshing of security and economic policy. Whilst it was a key objective of governments to avoid what were seen as critical errors in the interwar period, with the growth of protectionism the context within which the newly established GATT operated was that configured by the Cold War. Not only did this delimit the range of participants engaged in multilateral trade diplomacy, but also it helped to ensure that the broader patterns of trade politics would be overlain by the geopolitical imperatives of the developing global conflict.

A manifestation of the emergence of the East-West divide and the use of trade as a foreign policy tool was the US-led strategic embargo symbolized in the US Export Control Act of 1949 and the Co-ordinating Committee (COCOM) whose aim was to co-ordinate the embargo amongst the United States' often unwilling allies. And where trade relationships developed between East and West, as they did during the 1960s when declining agricultural productivity led the USSR to become a net food importer from the West, then their use as a foreign policy tool in situations such as that which arose following the Soviet intervention in Afghanistan in late 1979 proved irresistible.

But by the 1980s, the relationship between foreign policy and trade policy had become far more complex. In part this reflected the lessening of East-West tensions accompanied by the growing significance of the economic dimension of foreign policy underscored by growing Third World economic demands and the emergence of resource diplomacy stimulated by the energy crises of the 1970s.[11] Whatever the realities of military bipolarity, the international economy had become multipolar, with a United States whose hegemony was challenged, whose confidence appeared to be sapped and which was confronted by rival centres of power in the shape of Japan and Western Europe. On the trade front, these developments manifested themselves in a proliferation of trade conflicts which seemed to strain the resources of diplomacy. These extended to the very heartland of the Western alliance as when, in 1982, European governments, particularly France and Britain, found themselves confronting the Reagan administration over their agreement with the USSR to import gas from Siberia.

In the vastly changed environment of the world following the Cold War, such conflicts came to be regarded as characteristic of an era which, in the view of a number of observers, was marked by the dominance of geoeconomics over geopolitics. Here, the traditional image of the relationship between foreign and trade diplomacy was reversed as the major systemic context of world politics was portrayed as one of conflict between rival forms of capitalism based on North America, Western Europe and the Asia-Pacific.[12] Consequently, it was easy to argue, as some came to do, that foreign policy had been subsumed by commercial policy or, to put it slightly differently, that all foreign policy was now foreign economic policy.[13] But things look rather different nearly a decade after the end of the Cold War. Geopolitical movement in the Asia-Pacific, uncertainty as to the future role and intentions of China, apprehensions regarding Russian foreign policy and the reassertion of nuclear politics have combined with the onset of the Asian financial crisis to erode assumptions that the politics in world politics had melted away. This is clearly reflected in the United States where President Clinton's famed emphasis on economics as the central preoccupation of his administration manifested itself in the attention given to trade negotiations and the creation of jobs through export-oriented programmes such as the Big Emerging Markets strategy. A less hospitable global political and economic environment together with domestic pressures—at both Congressional and state/local levels—to wield the economic sanctions stick at a range of countries, have reaffirmed the linkages between foreign and commercial policies.[14]

Alongside this dimension of systemic change exists another of at least equal significance in determining the character of trade diplomacy, namely the changing character of the global economy. As Woolcock suggests in the following chapter, many of the major changes in the environment of trade politics are related to the broadening and deepening of the global economy. From what was an *international* economy in, say, the late nineteenth century, when geographically discrete national markets were linked by flows of trade and investment across national boundaries, we have witnessed the evolution of what Kobrin terms a 'networked world economy' based on electronically integrated networks operating across rather than within those boundaries.[15] During the twentieth century, the progressive internationalization of production has been underpinned by the growth of the MNE, the increasing mobility of capital, the significance of knowledge and information within the global economy, and the revolution in information and communications technology—which has both facilitated economic integration and deepened it.[16] As noted earlier, these changes are most often depicted in terms of 'globalization' whose precise nature and implications for the state as a political and economic actor are the subject of considerable debate.

Thus it appears indisputable that the nature of the trading environment is very different from that of a century ago. The globalization of production now means that it is virtually impossible to identify in a meaningful sense the origins of a given product. Cars, computers, household electrical goods, each are sourced from components across the world and may be produced in a variety of locations. Central to these processes has been the growing significance of the MNE, now estimated to account for between one-fifth and one-quarter of world production. As a consequence, foreign direct investment has assumed added importance and an increasing volume of trade is intra-firm trade rather than trade in goods between national economies. In the early 1990s, it was estimated that some 50% of both US and Japanese trade assumed the form of MNE intra-firm trade.[17]

At the same time, the location of production has changed. The traditional image of a geographical division of labour between a core of developed, industrialized countries producing manufactured goods and a periphery providing them with natural resources has been fundamentally transformed by the reloca-tion and globalization of production and the emergence of the newly industrialized countries (NICs). As the chapters in Part III make clear, this reflects in part the regionalizing dynamics of the economic order after the Cold War.

Overall, these varying developments have had the effect of changing the demands placed on governments in terms of fashioning their trade policies as well as the nature of trade politics and, consequently, the character of trade diplomacy.

Agendas

Against this background, as the chapters in the first part of this book demonstrate, the nature of the trade agenda has changed in fundamental respects. When the GATT began to function in 1948, its small membership was relatively homogeneous in terms of political and economic characteristics. Furthermore, the central agenda, tariff reduction,

if by no means politically uncontentious, was susceptible to negotiation through comparatively simple mechanisms.[18] Thus the early GATT negotiating rounds recorded notable successes in reducing tariffs, albeit from very high levels.[19] The shift towards non-tariff barriers (NTBs) was a notable feature of the Tokyo Round of GATT negotiations in the 1970s and reflected success in reducing tariff barriers at national borders as well as the nature of what was being traded. Between 1970 and 1987, trade in the major commercial services such as telecommunications and financial services grew rapidly and by the beginning of the Uruguay Round negotiations in 1986, services were firmly on the agenda of the advanced industrialized states.[20] In 1980, manufactured goods accounted for 23% of world production and services 53%. By 1994, the figures were 21% and 63% respectively. This development was closely related to the growth of foreign direct investment (FDI) since most services, by their nature, can only be delivered directly rather than traded across national borders as in the case of goods. Hence presence in markets has become as significant as access to those markets.

At the same time, the homogeneity of the trading system was greatly reduced. By the time that the old GATT was replaced by the WTO in 1995, the former's membership had grown to 128, with the latter's prospective membership standing at some 150 countries and territories.[21] As a result, agendas differ far more markedly than in the early years of the GATT, as illustrated by the priorities of developed and developing countries during the Uruguay Round negotiations. Given the fact that international trade in commercial services constitutes a much smaller proportion of their gross domestic product, Third World countries were far more concerned with gaining enhanced access for their goods to the markets of the developed world. Thus, Africa (see Shaw and van der Westhuizen, Chapter 15), always marginalized in international trade negotiations, became even more so during the Uruguay Round with its inclusion of issues—Trade-Related Aspects of Intellectual Property Rights (TRIPs) and Trade-Related Investment Measures (TRIMs)—far from the core concerns of the countries of the region.

Apart from the growing significance of services, as Part II of this book demonstrates, other issues were crowding onto what has come to be regarded as the 'new' trade agenda.[22] In the cases of intellectual property (Capling, Chapter 5) and information technology (Bosch, Chapter 6) these new issues present differing kinds of challenge. On the one hand, they are often inherently more technical than the 'older' issues on the trade agenda. Second, as we shall see below, in adding to the range of issues on the agenda, they increase complexity measured in terms of the potential interaction between issues. Third, since many of these issues reach far more deeply into national communities than the older 'boundary' trade issues as represented by tariffs, they challenge core social values and can easily be presented in terms of challenges to national autonomy and, as Pigman demonstrates (Chapter 12), provide a focus for sovereignty-related debates. We shall return to these points shortly, but before doing so, it is important to an understanding of the nature of trade politics that we recognize the limits of 'newness'.

On the one hand, as Bosch's chapter on computer encryption demonstrates, there is a continuing interface between security and trade. Certainly, the script is being

rewritten in the era following the Cold War as the security challenges become more diverse and complex. The growth of transnational crime and illicit forms of trade, particularly in drugs, is facilitated by globalization and confronts governments and their societies with profound dilemmas. At the same time, the differences of interest between firms who wish to export encryption technology and the intelligence and security community who fear the consequences of doing so, underscore one of the continuing problems that have confronted the state in fashioning trade policies and in responding to the competing political interests on which these rest.

Furthermore, as Balaam's chapter clearly shows, traditional issues, such as agriculture, are alive and well and central to an understanding of the politics of the Uruguay Round negotiations. Additionally, in the context of a growing public concern with health, 'food politics' is taking on a new lease of life in the form of disputes such as that between the United States and the EU over hormone-treated beef and genetically modified foodstuffs. Moreover, returning to issue-linkage, it is important to remember that issues do not exist in isolation from one another. Indeed, the very nature of trade negotiations is rooted in the development of issue interrelationships, as in the case of agriculture and audiovisual issues in the final phases of the Uruguay Round. Even the growing significance of commercial services needs to take account of the fact that this accompanies and feeds off the growth in world trade in goods.

Much of the current debate about the new trade agenda relates to the evolving multilateral trading system. At one level, issues such as labour standards and the environment, as van Liemt and Brack respectively demonstrate, present problems with which trade policy makers, both at the national level and within international organizations, principally the WTO, are seeking to grapple. At the same time, they are also issues around which a cluster of actors are gathering in pursuit of political interests and goals which are broader in their focus and raise fundamental questions about the place of societies in a globalizing economy and the goals they should pursue. From one perspective, this is seen as part of a general shift towards a more ethical and humane brand of international politics underpinned by far greater sensitivity towards resource scarcities and the future of the planet. Hence it fits within Pirages' identification of a set of economic, ecological and ethical issues which, he argues, is changing basic perspectives in international politics and which he terms 'ecopolitics'.[23] However one regards such a claim, it is certainly the case that alongside the old business of conducting trade policy, there is an increasingly densely textured pattern of trade-related politics.

As Cable has noted, a growing ethical agenda impacts on trade politics in two senses.[24] On the one hand, trade is identified as promoting violations of what are portrayed as fundamental and universal values, whether these relate to human rights or respect for the environment. Opponents of the export of live animals, the importing of tuna caught in nets which also trap dolphins, and trading with countries accused of employing children or imposing inhuman conditions on workers, regard trade conducted in such circumstances as unacceptable. On the other hand, trade offers a tool by which deviations from accepted norms can be punished. In one sense

there is nothing new in this. Governments have used trade as a tool of statecraft for centuries and it became part of the fabric of international politics in the Cold War era. But the objectives of sanctions are now acquiring a much more overt ethical dimension removed from the interplay of traditional power politics.

Not only this but, as we shall see in the following section, the range of actors and patterns of interactions generated by ethically driven trade sanctions are far more complex. As Scholte's discussion of the WTO and civil society demonstrates, NGOs are increasingly drawn in to trade politics and cut across the interests and objectives of both governments and firms. Campaigns such as those directed towards Shell regarding its Nigerian operations and Greenpeace's European operations focusing on the forest management practices of forest industries companies in British Columbia have presented real challenges to both policy makers and corporate managers.[25] At the official level, the United States offers the most obvious manifestation of this trend. Not only have sanctions of the more traditional, politicized kind proliferated as Congress has passed extraterritorial legislation directed towards trade with Cuba (the Helms-Burton Act) and with Iran and Libya (the D'Amato Act), but state and city authorities have engaged in trade-related sanctions, as in the case of the Massachusetts 1996 law relating to trade with Burma and the state- and city-led campaign directed towards the Swiss banks and their treatment of Holocaust victims' funds.[26] Moreover, sanctions have hit the high street as NGOs and consumer groups bring pressure to bear on companies to source their goods from ethically and environmentally sound sources by organizing—or threatening to organize—consumer 'buycotts' of their products. It is in such situations that the loop between the shaping of trade policy and the broader patterns of trade-related politics closes. Consumer-led pressures on high street stores to stock 'fair trade' tea and coffee and source furniture from countries with sustainable forest management policies clearly impacts on the issue of 'eco-labelling', or giving official recognition to such goods.

This leads us into another dimension of the ethics-trade interface, namely the resounding differences between societies over these issues. The firm resistance of growers of tropical timber to controls over trade in this product reflects the fact that it is a significant earner of foreign exchange for a country such as Indonesia. And human rights/labour standards issues pose, at one and the same time, problems of differing cultural values and economic interests. The goal of free trade often sits uneasily with national communities' desire to preserve their cultural identity. But the entertainment industry is big business and accounts for a significant and growing proportion of world trade. As Capling's chapter illustrates, this fact underscores the significance of intellectual property as a trade politics issue, but the import of foreign films, literature and music poses broader political issues where societies resent the imposition of foreign cultures.

Of course, this manifests itself most clearly in clashes between Western and non-Western societies, but there is considerable resistance in Europe and Canada to the 'Americanization' of the media which has led to, amongst other measures, the imposition of local content rules for television programmes. And the economic choices are by no means clear cut. It may appear unacceptable to consumers in the

advanced industrialized societies that their vegetables and sportswear are produced by child labour or workers whose level of remuneration is vastly lower than that enjoyed by equivalent workers in the West. But the alternatives, in the absence of carefully constructed programmes of support, may be unemployment or far worse. One of the key problems is that concern with the environment and human rights may simply serve as a cloak for protectionist interests and certainly be seen as such by those who come to believe that the developed world's preoccupation with the ethical trade agenda is little more than a plot to deny the Third World legitimate opportunities to enhance its wealth.

The roots of much of the stuff of trade politics, then, are located in the growing integration of the global economy. The pressures that flow from this are balanced by fragmentary responses at both regional and domestic levels—the latter frequently dubbed 'globalization backlash'. Changes in the world trading patterns as well as in the substance of that trade have created pools of displaced and disaffected workers alienated from processes which they believe favour the interests of others over their own. These beliefs readily embrace a range of issues, notably attitudes to immigration, which lead to the politics of protest as represented by political parties which are able to capitalize on the resentments produced by global economic integration. Hence the recent—if evanescent—success of the One Nation Party in Australia whose appeal is primarily to groups who perceive their way of life threatened by a mix of foreign investment, government embrace of policies directed towards the opening up of the Australian economy and immigration policies which challenge the country's identity.

Processes

The developments outlined above have created a far more complex environment for trade negotiators. As we have seen, not only are the issues themselves technically more complex, but they embrace matters which have traditionally been regarded as falling within the domestic arena and therefore as the preserve of national governments. As McGuire notes in his discussion of business-govern-ment relations in Chapter 9, this reflects the growing importance of regulatory issues in world trade. From financial services—as demonstrated only too well in the context of the Asian financial crisis—to the often bitter conflicts generated by the politics of food, the role of state institutions as regulators has become a central concern of trade diplomacy.[27] The dispute between the EU and the United States over the former's reluctance to allow the sale of genetically modified foodstuffs is viewed in Washington as a failure of European regulatory procedures for vetting foodstuffs. How can Brussels take three years to undertake the necessary processes when the United States, Canada and Japan complete them in eight months?[28]

Underpinning such disputes lie deeper pressures for convergence in regulatory procedures and standards which pose critical issues for national political leaders who are confronted by external demands to adopt standards which might well be resisted by domestic constituencies for a variety of social, cultural or political reasons. As

Vogel has suggested in the context of transatlantic trade relations, domestic politics and international trade diplomacy collide with and feed off one another, stimulated by differences of approach to issues of consumer and environmental protection. Rather than disarming regulatory disputes, the similarities between the United States and the EU in terms of their levels of development and the salience of environmental issues within their respective societies simply serve to enhance pressures for greater regulation on an ever widening range of issues and to emphasize variations in consumer attitudes on such matters as animal rights and food safety standards.[29] Moving beyond the transatlantic arena, it is these pressures that have produced what is referred to as 'system friction' as the very nature of different cultures, and the structure of political and social systems becomes a key issue for trade diplomacy. Continuing US attempts to pressure Japan to adopt US policies and practices to facilitate access for American exporters to Japanese markets have received most attention in this context.[30]

At one level, this growing interaction between domestic and international environments is not particularly new and can be traced back to the Tokyo Round of GATT negotiations which gave far greater salience to NTBs. But the process has gone much further and deeper as trade negotiators concern them-selves with areas and issues traditionally regarded as the province of national jurisdictions. Indeed, a central characteristic of modern trade diplomacy, with its growing regulatory agenda, is a concern with the nature, role and capacity of jurisdictions. What might be termed 'jurisdictional diplomacy' has grown in importance and assumes a number of forms. The linkage between trade and competition policy has made national regulations concerning such issues as business mergers and acceptable or unacceptable business practices of central importance. The fact that about half of WTO member states have no competition laws and the huge variations in practice amongst those that do (European practice is bureaucratic in nature whereas US infringement of competition regulations can be tried in court) creates an environment of uncertainty and potential conflict. The Boeing-McDonnell Douglas merger and the proposed alliance between British Airways and American Airlines thus excite the interests of regulators in varying jurisdictions, namely the United States, the EU Commission and those individual EU member states with a close interest in the outcomes. Alongside this lies the thorny issue of the role of the WTO in such regulatory areas as competition policy. Here, Washington has in the past resisted the extension of WTO jurisdiction but reacted angrily when the latter rejected its argument that the Japanese operate rules which discriminate against firms such as Kodak trying to compete in their photographic film market

A further twist to the jurisdictional dimension of trade diplomacy is provided by what seem at first sight to be contrary trends: the extension of national jurisdictional claims outside national territories and the growing significance of subnational jurisdictions (states, provinces and cities) to trade diplomacy. In the first category, US claims to extraterritorial jurisdiction, as represented by the Helms-Burton Act, intended to punish foreign firms investing in American property expropriated by the Castro regime in Cuba, have been the source of considerable friction between the EU

and Washington.[31] Somewhat less visibly, so have attempts by Brussels to establish common rules for the export of various forms of personal data which could restrict data flows within companies' global communications networks. Such a threat has led the US administration to refer the matter to the WTO and Congress to pass legislation prohibiting American firms from observing the Commission directive.[32]

The growth of subnational authorities' involvement in trade diplomacy reflects the pattern of changes discussed in this and other chapters. Their significance as purchasers of goods and services has ensured that preferences given to local suppliers have become an issue on the trade agenda. Furthermore, many of the policy areas which determine national competitiveness—education, for example—fall under subnational jurisdiction and are thus of central concern to both government and business. Finally, local and regional authorities are increasingly pressured to adopt stances on the range of issues that form the stuff of trade politics. This is clearly demonstrated in the notable tendency for US state and city governments to adopt economic sanctions against a growing range of targets, from companies trading with Burma to Swiss banks and other institutions for failing to produce satisfactory settlements on the Nazi gold issue.

In the broader context of trade politics, jurisdictional diplomacy is also reflected in the growing tendency for individuals and groups to use the courts of other countries in pursuing claims against MNEs where their activities are seen to be in conflict with human rights principles. The upholding of the right of a group of Burmese farmers to sue the American energy firm Unocal of California in US courts on the grounds that the company was aware that the Burmese government was using slave labour to construct a pipeline to transport its natural gas is a case in point and poses new challenges to firms and governments in managing the interface between trade and human rights.[33]

We shall return to this issue, but it is important to recognize that the changing trade agenda fundamentally alters the parameters within which trade negotiators are required to operate—not least because of the tensions generated by a much more intrusive global economy. Sustaining a national social consensus for further trade liberalization rubs up against resistance from those who find their jobs threatened and groups who believe that other values—in such areas as social welfare and the environment—are being sacrificed to the demands of global capital. The refusal of Congress to grant the Clinton administration renewal of fast-track authority in trade negotiations in late 1997, followed by Vice-President Gore's tough public stance towards the United States' Asian trading partners as the US trade deficit seemed poised to increase dramatically in late 1998 and beyond, are indicative of the potency of renewed protectionist sentiment within Congress.[34]

A critical feature of this changing policy milieu is the relationships between key actors and the interests which help to determine them, not least the patterns of expectations that condition the relationships between business and government. Despite the decline of national economies and the territorially bound business enterprises on which they were based—epitomized in Reich's now famous question 'who is us?'—it is clear that firms, both MNEs and small and medium enterprises

(SMEs), have expectations of government, albeit redefined to take account of the changing conditions of the global economy.[35]

Not the least of the reasons why this is so is the fact that only government can determine the policies which, in the form of health, education and welfare provision, are a major conditioning factor in business competitiveness. At the same time, the rise of what Rosecrance has termed the 'trading state', whose capacity to perform its essential functions no longer rests on the control of territory and the exercise of force, demands that government opens a dialogue with firms to enhance national wealth through attracting inward investment to jurisdictions and ensuring that this investment remains in place. What Strange has characterised as the new triangular diplomacy based on the interactions between firms and government reflects the nature of mutual needs that bring together the worlds of governments and business.[36]

But this image of triangularity fails to explore the full complexities underpinning the nature of the changing diplomatic environment. In addition to government-firm interactions, both are increasingly required to engage with representatives of civil society in achieving their policy goals. In the words of one study, 'something is happening in the relationships between governments, NGOs and companies which draws them to engage more closely together to deal with certain issues'.[37] Accounting for this 'something' requires an appreciation of the forces outlined above and in other chapters of this book. As one senior Canadian trade official has noted, trade diplomacy was, until relatively recently, marked by low levels of consultation and public interest:

> In the early years of the General Agreement on Tariffs and Trade, federal ministers and officials rarely consulted with major industries that were directly affected and this seemed to cause little concern across the country. Successive rounds of GATT negotiations were routinely approved by the government with scant public or political debate. Trade disputes were fewer and less contentious than they are today.[38]

Not only have the pressures associated with globalization impelled a more diverse range of actors concerned with issues on the 'new' trade agenda to become involved with both bilateral and multilateral negotiations where these relate to issues of the environment and human rights, for example, but they have provided the opportunity for such engagement. The information and communications revolutions, in particular, have enabled Greenpeace to challenge Shell over the dumping of oil rigs in the North Sea and native groups in Colombia to pressure Occidental Petroleum to re-evaluate its oil exploration activities. However overdrawn is the attribution of the problems surrounding the negotiations on the Multilateral Agreement on Investment conducted within the Organization for Economic Co-operation and Development to the activities of various NGOs exploiting the resources of the Internet, it is undoubtedly true that such negotiations have to take account of these new pressures.

This reflects, once again, the growing significance of regulatory issues in the global economy. Answering his own question—why have regulations governing areas such

as food hygiene become such a contentious issue in US—EU relations?—Vogel argues that it is due to the activities of NGOs rather than pressures from relevant producer groups.[39] The expansion of those involved in trade politics to embrace the agents of civil society, however, serves to reinforce conflict, he suggests. On the one hand, as noted above, this reflects cultural and political differences and different priorities on the part of consumers and the groups that represent them. At the same time, it follows from a strong inclination on the part of NGOs to view each regulatory battle as crucial lest defeat on one issue leads to challenges to other regulations regarded as important on environmental or other grounds.

Because a core characteristic of this changing environment appears to be the enhanced dependency of the key actors, governments, firms and NGOs on, at a minimum, communicating with each other, diplomatic strategies need to adapt accordingly. Elsewhere, I have termed the emergence of this style of diplomacy 'catalytic diplomacy', reflecting the frequent need experienced by differing categories of actor to build and manage short-term coalitions of interests to achieve specific policy goals.[40] Rather than focusing on the pre-eminence of one type of diplomatic actor, it recognizes that, in the specific context with which we are concerned here, governments, firms and NGOs are each confronted by complex autonomy dilemmas rooted in their desire to achieve their policy goals whilst aware that they are deficient in certain crucial resources that enable them to do so. These may be tangible (governments lacking financial resources) or intangible—represented by knowledge and/or legitimacy deficits which require the development of communications with other actors.[41] This is not to suggest that all such communications will be conflict free but there is an impetus to develop co-operative strategies on a short- or longer-term basis depending on the nature of the issue.

The trade agenda is by no means unique in this respect for growing complexity is a characteristic of a number of issue areas with which diplomacy has to deal. However, the kind of catalytic strategies referred to here reflect two types of complexity: that relating to the inherent characteristics of a set of issues and that resulting from the growing issue-linkage that is a feature of contemporary world politics. The interaction of both varieties of complexity, as noted earlier, is one feature of trade politics and the diplomacy which it generates and can be portrayed in terms of diplomatic 'sites' characterized by a growing diversity of actors, embracing a broader agenda of issues and located on varying terrains. Conventionally, these terrains might be differentiated in terms of 'multilateral' or 'bilateral' diplomacy (always a problematic distinction in practice) and one of their defining qualities deemed to flow from their 'international' as distinct from their 'domestic' qualities. But as several contributors to this book make clear, the erosion of boundaries between these sites and the ways in which they touch upon one another is one of the stark realities which trade diplomats have to confront.

In particular, the growing linkage between the domestic and international components of diplomatic sites has affected the processes of trade diplomacy as internal bargaining goes hand in hand with international bargaining. A former US Special Trade Representative, Robert S.Strauss, recalled that during the Tokyo Round, 'I

spent as much time negotiating with domestic constituents (both industry and labour) and members of the US Congress as I did negotiating with our foreign trading partners'.[42] The need to sustain internal as well as external coalitions means that negotiators need to engage simultaneously in 'two-level games', with both domestic constituencies and international negotiating partners, treating domestic ratification of international agreements as a continuing process and one that cannot safely be left until the ink is dry on the paper. The domestic-international linkage may encourage trade negotiators to use it as part of their negotiating strategy: during the Uruguay Round negotiations, for example, US diplomats cited the existence of protectionist forces at home as a constraint on their freedom to negotiate.[43]

The processes of trade diplomacy also reflect their substance. The focus of GATT diplomacy on the reduction of tariffs during the early negotiating rounds (from Geneva in 1947 to the Dillon Round in 1960–1) meant that it was marked by a relatively low level of complexity, a high degree of transparency and the quantifiable nature of the core issues. Changes in the trade agenda, including the growing importance of NTBs and trade in services, have made the character of negotiation far more complex. Whereas it is fairly easy to quantify gains and losses in tariff negotiations, exchanges of concessions on which the principle of reciprocity is based are far harder to achieve when NTBs come to dominate the agenda.[44]

Moreover, the character of the negotiations (as in other areas of the global agenda) demands the generation of new knowledge as such issues as intellectual property assume greater prominence. Contemporary negotiations involve processes of mutual learning and are as much concerned with developing principles and systematizing new knowledge as persuasion. This is part of the move to what Winham has termed negotiation as a 'management process', marked by its technical qualities, complexity, uncertainty and bureaucratization rather than the traditional concept of the trading of concessions in pursuit of a negotiated settlement.[45] Thus Ryan's account of the negotiation of the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs)—what he refers to as 'knowledge diplomacy'—involved processes of organizational learning at several levels.[46] For the Office of the US Trade Representative (USTR), the emergence of intellectual property on the trade-negotiating agenda demanded that an organization whose prime focus prior to the 1980s had been on manufactured goods and agriculture needed to develop new competencies. Similarly, the challenge of the new agenda required that the main functional international agency in the area, the World Intellectual Property Organization (WIPO), enhance its resources and develop a role as a body capable of helping developing countries meet the obligations that TRIPs imposed upon them. In turn, these developments have affected the structure of trade negotiations. Agenda setting during often extensive pre-negotiations (establishing the negotiating agenda of the Uruguay Round took five years) has become a common phenomenon.[47] In the case of TRIPs, the content of the negotiations demanded that a 'layered' approach to the negotiations be adopted whereby the trading of concessions through linkage-bargain diplomacy was conducted within the GATT whilst function-specific diplomacy was

conducted within WIPO. It was the interaction of actors within these two arenas that was crucial to the success of the final negotiations.[48]

Conclusion

It was suggested at the start of this introduction that the growing complexities inherent in the trade agenda demand that we adopt more nuanced approaches to its analysis than are associated with the more traditional conceptions of foreign economic policy. In part, this reflects the fact that trade policy has evolved beyond a concern with border issues and now reaches deep into the recesses of national societies, their cultures and social preferences. As such, it is one dimension of broader processes of boundary erosion which are producing a multilayered policy environment marked by a growing diversity of actors, enhanced complexity in the strategies which they deploy in seeking policy objectives and the arenas in which these goals are pursued. The resultant image is one in which trade and trade-related issues are emerging at the centre of political debate in an international political economy marked by complex processes of integration and fragmentation. Within this complexity, actor roles and relationships are being redefined in such a way as to cast doubt on conventional distinctions between state-centric and pluralistic approaches to policy making. Thus much of the texture of emerging trade politics described by the contributors to this book rests on images of enhanced interaction and mutual dependency as reflected in the often intricate patterns of linkage between government, business and NGOs. The scenarios provided in this volume may, therefore, be viewed as portraying apparently paradoxical processes wherein trade policy, as traditionally conceived, has become subsumed under broader trends reflecting processes of globalization and the erosion of the international-domestic divide whilst, at the same time, these very processes are helping to elevate the significance of more densely configured patterns of trade politics. The outcomes are proving as intriguing for analysts to explore as they are testing for practitioners to manage.

Notes

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Part I

Environments and issues

Introduction

A central premise of this volume is that the trade agenda and, more generally, the international economic environment have become much more complex in several interrelated ways over recent years. Stephen Woolcock, in his opening chapter, traces these developments by examining the evolution of the multilateral trading system. First, there is the increasing erosion of the boundary between the domestic economy and the international. Early analyses of trade took the domestic economy as something of a 'black box' which simply produced goods for export; how an economy produced what it did was either ignored or, more typically, regarded as the unproblematic result of comparative advantage. Recent years have seen a steady erosion in the faith of comparative advantage to explain international trade. As Moon argues in his chapter, the export success of the Japanese economy served to remind observers that how a state organized its economy had trade implications. The interest among American economists during the 1980s in strategic trade policies flowed partly from this recognition.

Second, the number of issues areas embraced by trade politics has increased. To be sure, some stalwarts of trade negotiations remain, as Balaam reminds us in his chapter on agriculture. But arguments about corn, wheat and wine have been joined by debates about trade in goods that cannot be seen or touched, the so-called invisibles of world trade. This new area encompasses a variety of services trade, as well as intellectual property. In their respective chapters, Kostecki and Capling take the reader through the key developments in services trade and intellectual property. The chapter by Olivia Bosch is underpinned by a blend of trade, security issues and new technology. The encryption debate signals how trade issues cannot be separated from national security considerations.

In the final two chapters in this part, van Liemt and Brack highlight two new and important trade issues: labour rights and the environment. That these two appear is testimony to the increasing reluctance of civil society to regard trade issues as the sole preserve of economists, trade lawyers and politicians. Labour standards is an area where human rights meets international trade. Arguably, the same holds true with the environment. In both cases, controversy arises out of the perception that some issues ought to be above money. But does agitation for more rigorous international standards signal a genuine concern for human and planetary welfare, or an attempt to raise

protectionist barriers? Moreover, as Brack argues, it is by no means clear that market-based approaches to pollution problems are inimical to environmentalism.

Chapter 1
The multilateral trading system into the new millennium

Stephen Woolcock[1]

Introduction

As the multilateral trading system (MTS) enters the new millennium and the debate on the scope and nature of a millennium round begins in earnest, it is useful to reflect on central issues facing the MTS. This chapter summarizes the broad strategic choices facing the General Agreement on Tariffs and Trade/World Trade Organization (GATT/WTO) system under the heading of widening versus deepening. The pressure to widen comes from the increased number of countries accepting the liberal international trade paradigm for the world economy. This provides an opportunity of establishing a genuinely global system covering trade and investment. Widening would imply building a unified system of rules applying to all countries, including countries at different levels of development, as well as the major transition economies of China and Russia. At the same time there is pressure to deepen the coverage of the GATT/WTO rules to include more issues and in particular 'behind the border' issues concerning regulatory policies. This pressure comes from the increased international interdependence of economies as a result of increased trade and investment flows (globalization). Deepening implies more intrusion into domestic policy preferences with the result that agreement on a unified global system of rules for countries at all levels of development becomes more difficult.

An alternative view of the multilateral trading system sees the main options as harmonization versus competition between national policies. This characterization of the debate on the future scope of the GATT/WTO system also refers to regulatory policies. Harmonization would entail efforts to reach agreement on common standards for regulatory policies, such as financial market regulation, environmental or labour standards and intellectual property rights. As such it is broadly equivalent to deepening, in that it implies greater international economic integration. Competition would entail a system in which the GATT/WTO rules were limited to defence of some basic principles, such as non-discrimination. There would be no attempt to create a 'level playing field' through harmonization or approximation of national regulatory policies. Com-petition between national regulatory policies would then ensue in which each country or jurisdiction (including regional groupings or subnational regulatory bodies) would compete both as a location for foreign investment and in terms of the international competitiveness of locally based

companies or production facilities. With competition between national policies, local preferences would determine the balance between responding to globalization and defence of local policy objectives.[2] Central to both the widening versus deepening and harmonization versus competition debates is the issue of the scope of the WTO system of rules, thus raising the question of which criteria should be used to determine the scope of the WTO. If, as is argued in this chapter, there are no unambiguous criteria available, the outcome of discussions on the WTO agenda will be shaped by such factors as the kind of leadership provided and the relative balance of interests between key lobbies. Finally, there is the issue of whether the WTO system faces a challenge to its legitimacy. Existing levels of interdependence mean that 'trade' policy decisions taken within the GATT/WTO, such as in the shape of dispute settlement decisions, impinge upon national policy preferences, such as on environmental protection. The GATT/WTO rules can therefore be seen as limiting or even undermining national policy preferences, which could in turn provoke challenges to the legitimacy of the WTO.

This chapter argues that rather than facing stark choices between widening and deepening (or harmonization and policy competition), the GATT/WTO has for some time been engaged in both. At issue, therefore, is the balance between widening and deepening (or policy competition and policy approximation). This is analogous to the often cited 'conflict' between regional and multilateral approaches to trade and investment rules, where there is likewise more of a division of labour between the different levels of governance or rule making, than a stark choice between one or the other. In reality there are also other 'levels' to the international regime for trade and investment, including plurilateral rules (investment rules in the OECD, public purchasing and potentially also competition policies) and private systems of rules.[3]

The nature of the GATT/WTO system

The GATT was not and is not a charter for free trade. Its core principle is non-discrimination, in the shape of most favoured nation treatment (the benefits of a trade agreement with any country's most favoured trading partner are to be extended to all signatories of the agreement) and national treatment (once a good or service has been imported it is to be treated as national goods or services with regard to, for example, taxes, subsidies and all forms of regulatory policy). Compliance with these principles does not necessitate liberalization. The scope and speed of liberalization is negotiated among the signatories to the GATT (now WTO). The GATT/WTO is also based on reciprocity, or the balancing of benefits and concessions. Liberal economists would argue that reciprocity, even if based on global as opposed to the more restrictive sectoral reciprocity, is a mercantilist approach. A liberal approach would be unilateral liberalization, regardless of what other countries decide. In this way the GATT and now GATT/WTO system has the form of both a contractual agreement to comply with a set of principles and a negotiating forum for liberalization.[4]

The GATT rules also provided—and continue to provide—for a range of exceptions and loopholes that weaken its liberal character. Exceptions exist for

preferential trade agreements in the shape of Article XXIV of the GATT (and Art V of the General Agreement on Trade in Services (GATS)). These are important exceptions as evidenced by the considerable growth of regional and other preferential trade agreements in recent years. There are exceptions for balance of payments difficulties (GATT Art XVIII) which have been used extensively, especially by a number of developing countries. There is a broad national security exemption (in Art XX) which the United States has used in defence of trade sanctions taken against other WTO members for breaking US sanctions against Cuba (The Libertad Act) and Iran and Libya (the Iran Libya Sanctions Act).[5] Article XX also provides for exemptions from GATT disciplines when these are justified on the grounds of protecting human, animal and plant health. There is a general safeguard clause (GATT Art XIX) and anti-dumping (Art VI) and countervailing duty provisions which have been used as instruments of administrative protection. The GATT/WTO should therefore be characterized as a system of managed liberalization rather than one of free trade.

The origins of the GATT

The origins of the GATT can be found in the draft treaty establishing the International Trade Organization (ITO). The ITO was to have been the third Bretton Woods institution. The original proposals for the ITO originated in interagency committees in the US administration meeting between the spring of 1943 and 1945. The US proposals were more liberal than those which emerged as the result of negotiations with Britain, France and a small group of other countries. The ITO was not adopted by the US Congress. At that time the US administration believed that Congress could not be persuaded to accept the proposals and concentrated instead on other, more pressing, issues such as the Marshall Plan and international security issues.[6] The Havana Charter of the ITO was an ambitious text. In addition to establishing a formal organization for regulating international trade, it included provisions on restrictive business practices and investment. When the ITO treaty failed, only the non-discriminatory trade measures in the shape of the General Agreement of Tariffs and Trade (GATT), which had been adopted in 1947, remained. As a result it was not until the establishment of the World Trade Organization (WTO) in 1995 that an institution equivalent to the IMF and World Bank was established for trade. As will be shown below, the debate is still continuing on whether there should be multilateral rules for investment and competition/anti-trust policy.

The early rounds

The initial rounds of the GATT concentrated on tariff reductions. During the period between 1947 and 1961 there were five rounds of negotiations which progressively reduced the level of industrial tariffs. These relatively straightforward negotiations benefited from the application of the most favoured nation (MFN) principle. (MFN means that tariff reductions negotiated between two parties, usually between a contracting party (CP) and its principal supplier of a given product, are then extended automatically to other contracting parties (CPs) to the GATT.) At this time there was not much of a

deepening agenda. The failure of the ITO meant that trade negotiations in these early rounds were concerned exclusively with border measures. 'Embedded liberalism' could be said to have existed since national regulatory, tax and other policies were not subject to negotiation or threatened by increased interdependence.[7] Indeed, rather than deepen the coverage of GATT rules, important exceptions were made from the MFN principle during this period. In 1952 the CPs waived the provisions requiring that regional agreements should cover substantially all trade (Art XXIV) to allow the establishment of the European Coal and Steel Community (ECSC).[8] Political and strategic considerations lay behind the United States' willingness to support the ECSC and the subsequent construction of Europe which built upon it. European economic integration, however, represented a major exception to the multilateral disciplines of the GATT and provided a model for subsequent preferential trade agreements.[9]

From 1953 (until the completion of the Uruguay Round in 1994) most of agriculture was excluded following a US-inspired 'waiver'. National agricultural policies were developed which discriminated in favour of domestic producers in order to help manage farm income or prices in order to compensate for climatic effects on agricultural output. Some countries also pursued food security policies aimed at ensuring that national agricultural output was sufficient to provide for the population at times of crisis. From 1962 onwards, textiles and clothing products were progressively excluded from GATT rules prohibiting selective import controls. This started with quotas on the importation of cotton products under the so-called Long Term Cotton Agreement and was extended to include other textile and clothing products in the Multi-Fibre Arrangement (MFA). The motivation behind this move was to protect the textile and clothing industries in the developed economies from excessive import competition when developing economies threatened major inroads in this sector. The MFA was sanctioned by the GATT CPs and remained in place until the Uruguay Round when a phased reduction of the quotas was agreed.

There was also a widening of the GATT. The original 1947 agreement had been signed by twenty-three countries. During the 1950s Germany (1951) and Japan (1955) became CPs and by the end of the Dillon Round of negotiations in 1961, in which the European Economic Community (EEC) participated as a unit for the first time, there were thirty-nine CPs. A number of important devel-oping countries, such as India, Brazil and, indeed, China until 1949, had been signatories to the GATT from the start, but the GATT was very much a product of the OECD (then the OEEC) countries, with the United States providing clear hegemonic leadership.

The Kennedy Round of negotiations (1963–7) was perhaps the first of the major multilateral trade rounds. It came at a time when many former colonies were achieving independence and many of these emerging states became CPs to the GATT. By the end of the Kennedy Round the number of CPs had nearly doubled to seventy-four. During the Kennedy Round, Poland also became the first centrally planned economy to seek observer status to the GATT.[10] It was during this round that the first real test of how to deal with countries at different levels of economic development had to be faced. Some of the more hardline developing countries were critical of the GATT for being a 'rich man's club', and were not willing to sign up to

obligations which they saw as inappropriate for developing economies. The solution to this problem used in the Kennedy Round was the adoption of Part IV of the GATT. Part IV provided for special and differential treatment for developing countries, so that, in effect, developing countries could become CPs without accepting the same disciplines as the developed economies. The intention was that these countries would graduate to full membership of the GATT as their economies developed. Inevitably, few countries were willing to graduate voluntarily and resentment built up in developed countries as the growth of manufacturing exports from a number of newly industrializing countries grew during the 1970s and early 1980s. Part IV did, however, enable the GATT to be widened to include a growing number of developing economies.

There was little deepening of GATT rules during the Kennedy Round. This was not through lack of ambition. The United States tried, in vain, to bring agriculture back under GATT discipline. This effort was largely in response to the establishment of the Common Agricultural Policy in the EEC, which the United States recognized would support European farmers and have a negative impact upon American export markets. But the United States failed in the face of strong opposition from the EEC. Agreements were also reached on the rules concerning how the anti-dumping provisions of GATT Article VI should be applied, and efforts to address the issue of national subsidies. These early efforts to negotiate on the more obvious non-tariff barriers illustrated how attention shifted from tariffs to the less obvious, and less easy to negotiate, non-tariff measures.

The Tokyo Round of negotiations (1973–9) was primarily concerned with deepening or extending the GATT disciplines to include a range of non-tariff barriers. The number of CPs continued to grow during the 1970s, so that there were ninety-nine signatories to the Tokyo Round, but these new CPs tended to be smaller developing countries with little impact on the outcome of negotiations and almost all sought Part IV exemption from GATT disciplines. Developing countries had limited impact on the GATT process during the Tokyo Round, despite their efforts to establish a New International Economic Order (NIEO) and efforts to co-ordinate policy in the so-called 'Group of 77' (G77) to strengthen their leverage in negotiations. Leadership of the international trade regime was still in US hands at the beginning of the Tokyo Round. In 1973, however, the United States had a visible trade deficit for the first time since World War II. A growing number of American industries faced the challenge of import competition, from Japanese and European producers, which were in some cases seen as benefiting from 'unfair' government support. This led to both a qualification of US support for multilateralism (see below) and US efforts to extend GATT disciplines to what the United States saw to be the 'unfair' trade practices of its trading partners. The United States, although slipping from the position of a hegemon, at least in trade/commercial policy, still possessed structural power to shape the agenda.[11]

The deepening efforts during the Tokyo Round focused on a wide range of non-tariff barriers, including, in particular, subsidies and countervailing duties, government procurement, technical barriers to trade and anti-dumping and safeguard

measures. With regard to subsidies, the United States sought to ban or at least control subsidies provided by European and other governments. In return the European Community (EC) sought more effective GATT discipline over the enhanced countervailing duty provisions the United States had given itself in the 1973 Trade Act.[12] The US administration was also largely instrumental in adding government procurement to the GATT agenda, because a number of major American sectors (power equipment and telecommunications) argued that they were being systematically excluded from European and Japanese markets by the preferential allocation of public contracts to national champions in the countries concerned. The EC argued in return for a removal of Buy America provisions in US state and federal law that granted explicit preferences to American suppliers.

The inclusion of technical barriers to trade in the GATT agenda was the first major step towards including national regulatory policies. In this case the aim was to avoid the discriminatory application of health and safety regulations. The inclusion of anti-dumping and safeguard issues was due to pressure from Japan and the newly industrializing countries (NICs) to have more effective discipline over dumping duties, which both the United States and EC were using to harass or contain imports from low-cost countries. In the case of safeguards the aim of the Tokyo Round was to negotiate an effective safeguard provision for the GATT. Article XIX of the GATT 1947 prohibited the selective use of safeguard actions and required countries resorting to safeguard measures to provide compensation in the form of tariff reduction or other concession to all GATT CPs. As many countries were unwilling to 'pay' the compensation, the practice developed of pressurizing exporters to accept 'voluntary' export restraints (VERs) or orderly marketing agreements (OMAs). Pressure was often applied by threatening to take anti-dumping actions. Rather than face such uncertainty, exporters often preferred to accommodate the wishes of the importing industry or country and accept VERs. In addition to avoiding compensation, the use of VERs had the advantage that they could be used selectively. The Tokyo Round reviewed Article XIX with a view to making it more effective. The EC wished to see some degree of selectivity as a condition for accepting full GATT discipline of VERs, but developing countries were opposed to any watering down of the MFN principle. In the end no agreement was reached, Article XIX remained unchanged and the practice of using VERs continued. In 1994 agreement was reached to bring all VERs and OMAs back into consistency with the GATT/ WTO rules.

Efforts to deepen coverage of the GATT again raised the issue of how to accommodate countries at different levels of development. In so far as developing countries could afford to provide subsidies for national industries, they were not willing to see their efforts at industrialization impeded by disciplines from the GATT. Multilateral regimes for government procurement were also seen as inappropriate by developing countries. Developing countries would have their own procurement subject to multilateral discipline and thus limit the scope for national preferences as an instrument of industrial policy. Developing countries would also face the costs of compliance with such a regime, but had few indigenous industries that could be expected to benefit from more open markets in the developed economies. In the case

of technical barriers to trade, many developing countries simply did not have such national regulations. The GATT therefore faced the dilemma of wishing to deepen the rules to cover some key non-tariff barriers whilst, at the same time, widening to include a large number of developing countries with little interest in such deepening. The approach adopted was the use of qualified MFN codes. In other words, developed countries that wished to do so, signed a series of codes on non-tariff barriers. GATT CPs were not obliged to sign the code, but only signatories would benefit from and be subject to the disciplines.

The codes had at best modest success in their stated objectives. Generally speaking, there was some improvement in transparency. Foreign suppliers benefited, for example, from better information on national technical regulations or national procurement procedures. But the codes did little to enhance market access. National technical regulations could still be oriented towards national producer interests and thus represent a barrier to market access. National procurement markets remained closed to foreign suppliers, and differences concerning the definitions of subsidies limited progress on enhanced GATT discipline over national industrial policies.

The Uruguay Round

The Uruguay Round (1986–94) represented the most ambitious effort at deepening and widening to date. In the early 1980s efforts to extend further the GATT agenda had again originated primarily from the United States. A coalition of American private sector interests in financial and telecommunications services wished to see GATT rules extended to include services and thus provide a predictable framework for the provision of services. A coalition of US-based multinational companies in information technology and pharmaceuticals was also interested in strengthening international rules protecting intellectual property rights (IPRs) and believed that this could only be done effectively by integrating IPR into the GATT disciplines. Linking IPRs with the GATT would strengthen enforcement of IPRs by providing for trade retaliation against any country which failed to comply with multilaterally agreed standards of IPRs. Parts of American agriculture were also determined to see agriculture under GATT disciplines.

The United States was initially unable to get sufficient support for a new round of multilateral negotiations, including these and other topics at the GATT Ministerial Meeting called in 1982. But the 'new issues' of services, IPRs and investment had been placed on the international trade agenda. Each of these issues concerned regulatory policies or 'behind the border' measures. Work continued on these new issues in the OECD and they were introduced into the Uruguay Round when it was finally started in September 1986, following the EC's decision to back negotiations in March 1985. Along with these new issues, tariffs and all the outstanding non-tariff barrier questions again found their way onto the agenda. In the case of the latter it was because the qualified MFN codes had not had any significant impact. There was also an agenda item on the Functioning of the GATT system (or FOGs), which led to the introduction of the Trade Policy Review Mechanism, at the Mid-Term Review of the Uruguay Round in November 1988. The Uruguay Round also included discussion

of the dispute settlement procedures of the GATT and led to a significant strengthening of the rules.[13]

Other issues were added as the negotiations progressed, such as the discriminatory use of rules of origin and the impact of regional agreements. Rules of origin designate the origin of products and serve two main purposes. First, origin rules are essential for implementing controls on trade, such as anti-dumping measures. Rules of origin were included in the negotiations because of a concern among exporting countries, such as Japan and the newly industrializing countries, that the discretion open to national authorities in defining rules was being used in a discriminatory fashion.[14] Second, rules of origin are needed to implement preferential trade agreements, such as regional trade or integration agreements. Such preferential rules of origin were not included in the discussions because WTO members involved in regional agreements rejected discussions which would challenge the fundamentals of regional preferences.[15]

Developing countries resisted the addition of new issues such as services and multilateral standards for the protection of IPRs, but in the end accepted their inclusion provided the liberalization of textiles and clothing (ending the MFA) and safeguards were included. Agricultural exporters, such as the Cairns Group (including Australia, Canada, Argentina,. etc.) and the United States, pressed for serious efforts to include agriculture in GATT disciplines. The assembly of a large multilateral package of issues therefore facilitated a balance between the interests of all countries and helped remove logjams that would otherwise have existed with a narrower set of issues. This is the classic argument in favour of multilateral rounds of negotiation over sector by sector or small negotiations which do not permit such a trade-off between issues. As a result the Uruguay Round constituted a significant deepening of the GATT agenda. Table 1.1 shows how the GATT/WTO agenda has grown over the last three major multilateral rounds and the current commercial policy agenda. It also shows how issues seldom drop off the agenda, mainly because of limited success in negotiations.

The widening of the GATT/WTO during the period of the Uruguay Round took several forms. First, there was an increase in the number of signatories, which rose to 128 countries by 1994. Second, more countries were participating actively in the negotiations. In the case of many developing countries this consisted of negotiating on a few issues of immediate importance, but the net effect was the enhanced involvement of more countries in the process. Third, qualified MFN agreements and Part IV were dropped. The results of the Uruguay Round, including the creation of the WTO and its enhanced dispute settlement procedures, were embodied in a Single Undertaking, signed by all members of the WTO. All members of the WTO are therefore ultimately committed to conforming with all GATT/WTO rules. This went some way to satisfying the developed country demands for the graduation of newly industrialized countries and for a clampdown on 'free-riding'. At the same time it was not possible to expect all developing countries to implement all the Uruguay Round agreements at the same pace as the developed countries, especially in the new areas. The Uruguay Round therefore used the concept of 'progressive

Table 1.1 Coverage of negotiations in successive rounds of the GATT

Issue	*Kennedy Round*	*Tokyo Round*	*Uruguay Round*	*Current agenda*
Tariffs	•	•	•	•
Customs duties	•	•	•	•
Anti-dumping	•	•	•	•
Agriculture	•	•	•	•
Subsidies and countervailing duties		•	•	•
Technical barriers to trade		•	•	•
Import licensing		•	•	•
Public procurement		•	•	•
Safeguards		•	•	•
GATT Articles		•	•	•
Dispute settlement		•	•	•
Code on civil aircraft (subsidies)		•	•	•
Rules of origin			•	•
Pre-shipment inspection			•	•
Textiles and clothing			•	•
Functioning of the GATT			•	•
WTO			•	•
Investment			•	•
Trade-related IPR			•	•
Services			•	•
Competition				•
Trade and the environment				•
Labour standards				?

liberalization'. Progressive liberalization means, in effect, that developing countries will only be obliged to implement the Single Undertaking after a period of transition.[16]

The current agenda

Although the conclusion of the Uruguay Round in 1994 represented a significant advance for the GATT/WTO, the issues agreed were issues of the 1980s. As noted above, the American financial services sector had started its efforts to have GATT rules established for services in the earlier 1980s. By the time the Round was finally completed the commercial policy agenda had moved on. The driving force of 'globalization' had pushed a further set of commercial policy issues onto the agenda including trade and the

environment, trade and investment, labour standards and competition. These were sometimes referred to as the 'trade ands'.[17] The inclusion of any of these issues would represent significant further deepening of the coverage of GATT rules. In each of these policy areas regulatory policy is carried out at a national level with a view to pursuing legitimate national policy aims, such as a clean environment, competitive markets or satisfactory conditions of employment. National regulation reflects national policy preferences on the trade-offs between competing or complementary policy objectives, such as between a clean environment and economic growth. In each policy area there are well-entrenched patterns of behaviour and regulatory policies. In some cases, such as in labour markets, these are fundamental to national politics and the character of the national model of the market economy. The inclusion of such issues in the GATT/WTO would therefore result in a significant deepening. Agreed rules on the environment, investment or competition would constitute an important degree of national policy harmonization and would therefore intrude into domestic policy preferences far more than is the case with the more traditional trade issues which affect measures at the border.

The current agenda on widening is also qualitatively different from the widening of earlier periods, in that it would include major powers (China and Russia) which will wish to have an influence on the rules. Previous widening has generally taken the shape of smaller economies which were essentially price takers, that is small countries that had little choice but to accept the rules devised by the leading developed countries.

The case for deepening the GATT/WTO system is that multilateral rules must keep pace with the globalization of the world economy if they are to remain relevant. If the GATT/WTO lags too far behind the evolution of markets, the demand for a predictable framework of rules will mean that bilateral or regional systems of rules will emerge. Investment provides an example of how this can happen. Limited progress with multilateral investment rules in the Uruguay Round, which only covered a number of Trade-Related Investment Measures (TRIMs),[18] contributed to the growth of bilateral investment treaties (BITs). There are now in the order of 1000 BITs, many of which were negotiated in recent years. The growth of regional agreements during the 1980s could also be seen, in part, as due to the lack of progress in the multilateral negotiations. Deepening can also be seen as necessary in order to establish or maintain the legitimacy and value of the GATT/WTO system in the eyes of key interest groups. Failure to address investment has led investors to turn increasingly to bilateral agreements as a means of ensuring a predictable legal framework for large-scale investment. Likewise, a failure to include intellectual property in the GATT/WTO would have doubtless resulted in continued pressure for the use of unilateral measures, such as the US Special 301 provisions, as a means of protecting IPR.[19] From the point of view of environmental lobbies and organized labour, WTO discipline enforcing IPRs whilst excluding environmental or labour standards from the same discipline is seen as unjust and will undermine the legitimacy of the system in their eyes.

On the other hand, deepening creates significant problems. How can one reach agreement on some harmonization of international standards among countries at very different levels of economic development, different climate conditions, different traditions of labour market organization and different policy preferences? For example, inclusion of core labour standards, including the right of association, in WTO disciplines seems problematic to say the least since many developing countries, not to mention China, see freedom of association as a threat to the established political order. Rather than intervene in national regulatory sovereignty, the alternative widening scenario would have considerable attractions. National policy preferences could remain unchallenged. There would be no need to seek harmonization of international regulatory standards. Furthermore the GATT/WTO could develop into a genuinely global organization. There would be 'free trade' without the problems and loss of sovereignty involved in policy approximation. But under the widening scenario the GATT/WTO would retain a narrow trade focus with a limited agenda. Free trade in the twenty-first century also means much more than removing border controls and tariffs. Failure to address the regulatory barriers to market access involved in the 'new issues' would mean that the WTO would risk falling further and further behind the evolution of markets and become increasingly irrelevant.

As the above summary of the historical evolution of the GATT/WTO has shown, there has always been a widening versus deepening issue, and GATT/WTO members have always sought to achieve both aims. The political economy of the current WTO agenda is such that there is, in practice, little choice but to continue to seek to widen and deepen. What characterizes the current debate is the qualitative changes in both deepening, to include far more regulatory policies, and widening, to include major transition economies, that make it more intense.

The scope of GATT/WTO rules

Since the creation of the GATT in 1947 national treatment and MFN status have provided the reference point for GATT rules and the basis for the compromise of embedded liberalism. If one accepts the case that the GATT/WTO must continue to deepen, it is highly doubtful that these principles will continue to be sufficient. This section provides a few examples of why this is the case.

National treatment requires all like products (or services) to be treated equally once the good or service has been imported. This interpretation of the GATT rules, which has been upheld in numerous dispute settlement panels, means that it is not possible to distinguish between products according to the way they are produced. As most pollution is caused in the production or processing of goods (or services), the current GATT/WTO interpretation means that 'dirty' products must be treated the same as 'clean' products. In other words, when a 'dirty' product produced in country 'A' where environmental regulations are not especially stringent (and costs are correspondingly low) is exported to country 'B' where environmental regulations are stringent (and costs higher), it must be treated similarly. If pollution occurs during production and the end products are the same, or 'like products', national treatment

requires that regulators in country 'B' cannot discriminate against the products from country 'A' even if this means that the more expensive but cleaner products produced in country 'A' are being undercut by cheaper, dirty products. This limitation of the existing national treatment rule is one of the main reasons environmental groups see the GATT/WTO system as undermining national environmental policies. Discussions in the WTO's Committee on Trade and the Environment have therefore been obliged to address this issue of production and processing methods (PPMs).[20]

National treatment also has limitations when it comes to dealing with certain service sectors. For example, national regulation or competition policies may allow the monopoly supply of a service, such as basic telecommunications. A monopoly excludes new national as well as foreign suppliers and is therefore consistent with national treatment. This means that it is possible to close a market to foreign competition in, for example, telecommunications or air transportation, whilst still providing national treatment. The GATS negotiations were therefore obliged to go beyond national treatment and seek some harmonization of regulatory practice and competition policies in order to ensure market opening.[21] Offering national treatment for the protection of intellectual property was also considered insufficient during the Uruguay Round, because many countries did not have effective laws to protect intellectual property.

In the field of technical regulations and standards, national policies can ban products, such as food containing genetically modified organisms (GMOs), but still be consistent with national treatment provided the ban applies to both nationally produced and imported like products. But countries whose agricultural producers have a lead in biotechnology and make extensive use of GMOs would see a ban by countries lagging in such technology as protection, especially if there is no scientific basis for the ban.[22] Similar arguments could be made with regard to many of the thousands of potential technical barriers to trade. In this, as in the other cases noted above, some form of policy approximation or 'harmonization' is required to remove barriers to trade and investment. The question is how much. In the WTO context the debate focuses on how much harmonization is occurring in the committees dealing with the Technical Barriers to Trade (TBT) and Sanitary and Phytosanitary (SPS) Agreements along with the associated standards bodies.[23]

The other GATT principle is MFN status. As shown above, it has been necessary to qualify the MFN principle on various occasions in order to accommodate countries at different levels of development. This is likely to continue to be the case, despite the adoption of the Uruguay Round results as a Single Undertaking. For example, agreement in the GATS negotiations was possible only because the principle of MFN was qualified in the coverage of the agreement. The framework of the GATS upholds MFN, but there is scope to exempt sectors and thus avoid MFN. The same could be said for the plurilateral agreement on public purchasing, which not only fails to offer MFN to non-signatories, but also uses schedules to define coverage in such a manner as to undermine effectively the MFN principle even for signatories. Finally, a number of multilateral environment agreements, such as the Montreal Protocol of ozone-

depleting substances and the Kyoto Convention on global warming, contain provisions which are inconsistent with MFN.

It is, of course, possible to argue that the GATT/WTO should not compromise these principles, but as these few examples show, the genie is already out of the bottle. The implication of sticking rigidly to MFN and national treatment would almost certainly be a reversal of existing GATT/WTO rules and a significant check on any further deepening. For all practical purposes MFN and national treatment have to be treated as necessary but not sufficient principles, and the scope of GATT/WTO rules will depend on the relative strength of arguments for and against a deepening. It will also depend on the discipline of those making the argument. For example, economists using largely tariff-based models of international trade will tend to seek salvation in comparative advantage. Lawyers will seek the solution in the legal certainty of clear concepts. Negotiators will, however, seek solutions to political problems confronted in negotiations and these may not fit any given model.

Notes

1 This essay draws on research work carried out on 'Subsidiarity in the Governance of the Global Economy', as part of the Economic and Social Research Council's initiative on global economic institutions.

2 See Jagdish Bhagwati and R.Hudec, *Fair Trade and Harmonization: Prerequisites for Free Trade?,* Vol. 1 Economic Analysis and Vol. 2 Legal Analysis (Cambridge, MA: MIT Press, 1996).

3 The regional versus multilateral issue is not discussed in this chapter. There is a growing literature on this topic. See World Trade Organization, *Regionalism and the World Trading System* (Geneva: WTO, 1996).

4 Gilbert Winham, 'The World Trade Organisation: institution-building in the multilateral trade system', *Journal of World Trade* 32, 1998.

5 The United States has not yet had to use this case in defence of its sanctions policies, because of an accommodation reached between the United States and the EU as part of the discussions on a Transatlantic Economic Partnership in May 1998.

6 John Odell and Barry Eichengreen, 'The United States, the ITO, and the WTO: exit options, Agent Slick, and presidential leadership', in Anne Krueger (ed.), *The WTO as an International Organization* (Chicago: University of Chicago Press, 1998), pp. 181–212.

7 Embedded liberalism is the term used to describe the postwar compromise between liberal foreign economic policies and national intervention in the pursuit of full employment and stable growth. See Wolfe in this volume.

8 The GATT (1947) provided for waivers from obligations. These required the support of three-quarters of the CPs. The waiver for agriculture was also supported by many European CPs because they wished to support agriculture for employment, food security and competitive reasons.

9 Richard Pomfret, *The Economics of Regional Trading Agreements* (Oxford: Clarendon Press, 1997).

10 Within the GATT, centrally planned economies made commitments based on a fixed percentage of their national markets in return for tariff concessions from full GATT CPs.

11 Susan Strange, *States and Markets* (London: Pinter, 1994).

12 Countervailing duties are those imposed by national governments when imported products are found to have been subsidized and when the domestic industry concerned has suffered injury or the threat of injury.
13 See Wolfe in this volume and John Jackson, 'Designing and implementing effective dispute settlement procedures: WTO dispute settlement, appraisal and prospects', in Krueger, *The WTO,* pp. 161–80.
14 The negotiations on services did not attempt to define rules of origin for services. This is an issue which is down for the next cycle of services negotiations starting in 1999 or 2000.
15 See Michael Trebilcock and Robert Howse, *The Regulation of International Trade* (London: Routledge, 1995), for a summary of the key issues.
16 For further reading on the Uruguay Round see John Croome, *Reshaping the World Trading System: A History of the Uruguay Round* (Geneva: WTO, 1995).
17 There is already a large and growing literature on the 'new issues'. For a general introduction to the debate see Bhagwati and Hudec, *Fair Trade and Harmonization.*
18 See Trebilcock and Howse, *The Regulation of International Trade.*
19 See Patrick Low, *Trading Free: The GATT and US Trade Policy* (New York: Twentieth Century Fund Press, 1993).
20 See Daniel C.Esty, *The Greening of the GATT: Trade, Environment and the Future* (Washington, DC: Institute for International Economics, 1994).
21 On trade and services see, for example, Richard Snape, 'Reaching effective agreements covering services', in Krueger, *The WTO,* pp. 279–96.
22 This issue arose when the EU considered banning GMOs on health grounds. As the leading producer of genetically modified crops the United States protested that this was contrary to the WTO Sanitary and Phytosanitary (SPS) Agreement.
23 Mutual recognition offers a theoretical alternative to 'harmonization' in some cases of technical barriers to trade and possibly other policy areas. But as the EU experience with mutual recognition shows, a considerable degree of policy approximation is needed before mutual recognition becomes politically acceptable. A similar problem arises in EU-US bilateral efforts to remove technical barriers to trade.

Further reading

The following are recent books providing a general overview of the issues in international trade and investment and the WTO in particular. The most important journals which almost exclusively cover the multilateral trading system are the *Journal of World Trade* and *World Economy.*

Jagdish Bhagwati and R.Hudec, *Fair Trade and Harmonization: Prerequisites for Free Trade?,* Vol. 1 Economic Analysis and Vol. 2 Legal Analysis (Cambridge, MA: MIT Press, 1996).

Bernard Hoekman and M.Kostecki, *The Political Economy of the World Trading System: From GATT to WTO* (Oxford: Oxford University Press, 1995).

Anne Krueger (ed.), *The WTO as an International Organization* (Chicago: University of Chicago Press, 1998).

Michael Trebilcock and Robert Howse, *The Regulation of International Trade* (London: Rout-ledge, 1998).

Chapter 2
Ideas and policies

Bruce E. Moon

Any explanation for the trade policies of nations must begin from the premise that each seeks to fashion a policy that will achieve its interests. It is the thesis of this chapter, however, that such interests are extraordinarily difficult to identify, even for the parties themselves. Trade produces such a welter of consequences through so many dynamic and complex causal processes that preferences for trade policy are dominated by the relatively simple theoretical ideas used to interpret, calculate, and weigh the various interests of participants. Further, because these theoretical ideas are highly structured, the actual menu of choices available to policy advocates is relatively small and surprisingly universal. Consequently, the center of the trade policy debate has seldom strayed far from the basic division between the orthodox liberal trade theory which underlies strategies of (more or less) free trade and assorted ideas associated with mercantilist thought that inform strategies of managed trade. The choice can be illustrated with a comparison of the trade policy decisions of two of the leading actors in the contemporary global political economy, Japan and the United States.

Since the middle of the twentieth century, the United States has been the leading advocate of free trade. That position is rooted in an abiding faith in orthodox liberal theory, the basic parameters of which remain little changed from the principles of free market economics portrayed by Adam Smith in his classic eighteenth-century work *The Wealth of Nations*.[1] Japan, on the other hand, has been more strongly influenced by a broader, but less systematic, collection of ideas, ranging from Frederick List's nineteenth-century critique of Smith, which helped codify mercantilism, to eclectic offshoots of liberal theory itself, such as strategic trade. Japanese practices of managed trade have attracted imitators, especially in Asia, and also strong opposition, especially in the United States. Partially in angry response to the Japanese challenge and partially in grudging admiration for the apparent Japanese success, many have advocated replacing the *free* trade ideal with the more ambiguous goal of *fair* trade.

To trace these ideas, we begin with a summary of the free trade doctrine and the liberal theory which gives it structure, citing US trade initiatives that embody both the general approach and the specific policies to which it gives rise. We follow with a sampling of the theoretical critiques offered of liberal trade theory, ranging from List's infant industry arguments to strategic trade theory, illustrated with significant aspects of Japanese trade policy. We conclude the chapter by discussing US policies designed to achieve 'fair trade'.

The theory underlying the doctrine of free trade

The most powerful idea in shaping trade policy throughout the modern age is the liberal argument for free trade. It contends that global welfare is maximized if nations abandon self-sufficiency to specialize in those goods that they produce most efficiently. They may then export those goods in exchange for items produced more efficiently abroad, resulting in 'gains from trade' manifested as increased global production and consumption. David Ricardo's remarkable theory of comparative advantage, a brilliant elaboration and extension of Smithian ideas, remains at the core of the liberal case for free trade. In his 1817 classic work, *The Principles of Political Economy and Taxation* (1817), Ricardo demonstrates the theoretical possibility that mutually beneficial trade may be conducted between a pair of nations, even when one is more efficient than the other in the production of all goods.[2]

Table 2.1 (p. 42) is patterned after Ricardo's famous example of the gains to be achieved by trading English cloth for Portuguese wine.[3] The analysis begins with **production possibilities**—the output that could be produced by a worker in each country in each industry, together with the total labor force available. Here, an English worker in either industry can produce more than a Portuguese worker, signifying that England has an *absolute* advantage in both industries. To illustrate that trade between them would still be profitable to both, consider first the levels of production **without specialization,** assuming that both countries chose to produce equal quantities of cloth and wine. In England, 100 labor-hours devoted to the production of cloth and 200 hours to the production of wine would yield 600 yards of cloth and 600 gallons of wine. In Portugal, producing 400 units of each good would require that 400 labor-hours be devoted to cloth and only 200 to wine.

Portugal is said to have a *comparative* advantage in wine, because its workers can produce two-thirds as much wine but only one-sixth as much cloth as a worker in England. Suppose, then, that Portugal specializes completely in the production of wine while England shifts entirely to cloth. **After specialization,** Portugal could now produce 1200 units of wine while England could produce 1800 units of cloth, a substantial increase in global output over the 1000 units of each produced under conditions of self-sufficiency. If they were to trade 700 units of wine for 700 units of cloth, each nation could then consume more of each good than in the absence of specialization. The gains from trade consist of the increased consumption made possible by each producer allocating resources in the most efficient way.

Central to the free trade policy implications of this argument is the contention that comparative advantage results from the intrinsic characteristics of the economies—and requires no government action except to refrain from introducing trade barriers. Within the liberal tradition, the sources of comparative advantage have been best articulated by two Swedish economists of the 1920s, Eli Heckscher and Bertil Ohlin.[4] They argue that a nation's comparative advantage lies in its factor endowments. For example, a capital-abundant country (such as the United States) would have a natural cost advantage in the production of heavy manufactures like autos, which are dubbed 'capital-intensive' because they require large quantities of expensive plant and

Table 2.1 Comparative advantage illustrated

Production possibilities

Country	*Labor-hours*	*Production per hour*	
		Wine	*Cloth*
England	300	3	6
Portugal	600	2	1

Without specialization

	Labor-hours		*Production*		*Consumption*	
Country	*Wine*	*Cloth*	*Wine*	*Cloth*	*Wine*	*Cloth*
England	200×3	100×6	600	600	600	600
Portugal	200×2	400×1	400	400	400	400

After specialization and trade

	Labor-hours		*Production*		*Consumption*	
Country	*Wine*	*Cloth*	*Wine*	*Cloth*	*Wine*	*Cloth*
England		300×6		1800	700	1100
Portugal	600×2		1200		500	700

equipment and advanced technology. Countries like Mexico, where unskilled labor is abundant (and therefore cheap), will naturally specialize in labor-inten-sive light manufactures that involve simple assembly.

This pattern is assumed to arise naturally through market processes if governments eliminate barriers to imports (such as tariffs and quotas) and inducements for exports (such as subsidies). Governments need play no role because entrepreneurs will naturally gravitate toward the production of goods in which they have a comparative advantage, since it is there that profit margins will be greatest. Thus, they follow Smith's famous dictum that the pursuit of maximum profit by each individual inevitably steers them—as if guided by the so-called 'invisible hand of self-interest'—toward behavior which maximizes the benefit of the community as a whole:

> As every individual…endeavors as much as he can both to employ his capital in the support of domestic industry, and so to direct that industry that its produce may be of greatest value; every individual necessarily labours to render the annual revenue of the society as great as he can. He generally, indeed, neither intends to promote the public interest, nor knows how much he is promoting it.… [H]e intends only his own gain, and he is in this, as in many other cases, led by an invisible hand to promote an end which was no part of his intention. Nor is it always the worse for

society that it was not part of it. By pursuing his own interest he frequently promotes that of society more effectually than when he intends to promote it.[5]

The free trade doctrine in US trade policy

For a variety of reasons, the free trade doctrine has had special appeal in the United States and has come to dominate its foreign economic policy.[6] The United States has sought to expand global trade in accord with liberal principles along two parallel tracks. First, it has liberalized its own trade policies, not only by eliminating most trade barriers, but also by minimizing government intervention in the economic processes that lead producers and consumers to initiate trade. For example, US tariff rates have been reduced by more than 80% from their high-water mark after the Smoot-Hawley tariff of 1930 and subsidies, with the important exception of agriculture, have nearly disappeared.

Second, it has worked to move other nations toward free trade by creating a global economic system that facilitates that choice. While liberal theory argues forcefully that each nation stands to gain from lowering its own trade barriers regardless of what others may do, it remains that a policy of free trade produces the greatest benefits when open markets abroad enable each nation to take full advantage of its export specialization. The United States was a leading force in shaping the Bretton Woods institutions after World War II and has continued to play the greatest role in extending the liberalization process through the Uruguay Round of the General Agreement on Tariffs and Trade (GATT) that created the long-awaited World Trade Organization.

Liberal theory has played a central role in the evolution of US trade policy, not only because its center-piece, the Ricardian theory of comparative advantage, directly implies the free trade doctrine embodied in its unilateral and multilateral trade initiatives, but also because it has structured the debate over policy options. This school of thought contains more than a policy prescription, but rather a whole set of conceptual ideas that define the language used in the debate and the acceptable range of argumentation, together with a conventional interpretation of historical evidence that defines the 'lessons' learned from various policy experiments.[7] Some of these elements are highly controversial outside of the epistemic community of liberals who regard them as an article of faith, which explains how competing perspectives thrive despite liberalism's dominance of trade policy discourse in the United States.[8]

Mercantilist ideas underlying managed trade

Outside of the United States, a second vision, that of mercantilism, has competed on more equal terms, both in the academic arena of ideas and as an influence on policy.[9] While liberalism contains an integrated body of precise premises, refined logical arguments, and universalistic policy conclusions, mercantilism has always consisted of fragmented practical wisdom derived from an eclectic mix of past policy successes, tactical judgments, and a smattering of theoretical ideas. In fact, it is awkward to identify the boundaries of mercantilism as a doctrine, because 'mercantilism' is a name applied after

the fact to a compilation of diverse arguments in defense of the various commercial (i.e. mercantile) policies widely practiced in Europe prior to the nineteenth century. That is why the best-known text in the mercantilist tradition is Friedrich List's *The National System of Political Economy,* written in 1841, half a century after Smith's death, even though the practice of mercantilism it defends pre-dated liberalism by several centuries. Indeed, it was mercantilist practice in the form of the famous English Corn Laws that was the target of the critique by Smith and Ricardo, and thus the animating force in the formation of modern liberal thought. Mercantilist policies share little but the conviction that governments must manage trade in order for it to further the national interest. Because perceptions of that national interest have varied from time to time, from place to place, and from author to author—after all, the 'national interest' encompasses a multitude of imprecise and partially competing goals—no universal policy advice is offered by mercantilism.

The asymmetry in form of these two perspectives elicits much confusion, distortion, and frustration. Liberals, proceeding ahistorically in seeking the theoretical core of mercantilism, have mistakenly reduced it to naive protectionism and the pursuit of trade surpluses, a straw man easily defeated within liberalism's frame of reference, which does not even contain the language to express, let alone evaluate, the premises and goals which have historically motivated most mercantilist policy.[10]

Because of the breadth and diversity of the mercantilist ideas that inform the trade policy of most modern states (to one degree or another), this discussion is kept within space constraints by focusing on those most clearly manifested in the post-World War II Japanese policy of heavily managed trade. While most of these ideas are quite old—often pre-dating liberalism—they appear most coherent if developed as critiques of liberal theory.

The single most discordant element between liberalism and mercantilism concerns the goals meant to be satisfied by trade policy. While liberalism focuses almost exclusively on allocative efficiency in order to maximize aggregate consumption, mercantilism seeks a number of goals that compete with and sometimes outweigh that value.[11] Classical mercantilism accorded special priority to promoting the power and autonomy of the state, often expressed in terms of maintaining self-sufficiency in industries relating to war or indispensable consumption (like food). Ironically, it is the liberal Adam Smith who gives clearest expression to this idea with his famous defense of the mercantilist Navigation Acts: 'defense is of more importance than opulence'.[12]

States also seek to influence distributional patterns in income and wealth, often emphasizing the values of equality and stability over the liberal concern with aggregate living standards. Critics observe that the Ricardian argument fails to account for the short-term dislocations required to move from the autarchic case to full specialization. The human costs implied by such a shift in employment are considerable, and so long as nations remain open to trade, changing global market conditions are likely to make them a permanent part of the social and political landscape.[13] As Polanyi points out, security for workers is an important social value

that is undermined by the self-regulating market envisioned by liberals, even if liberalism delivers on its promise to maximize aggregate consumption.[14] Mercantilists also question whether the implicit assumption of full employment contained in Ricardian demonstrations of the gains from trade is realistic. Of course, these ideas may inspire either policies of managed trade or alternative strategies such as the growth of the welfare state.[15]

Finally, mercantilists often emphasize a favorable balance of trade. Under classical mercantilism, this was designed to produce an 'inflow of treasure' that would enrich the state itself while guaranteeing an adequate money supply for the domestic economy. In the modern era, the motive is to avoid a trade deficit that would require a capital outflow to balance it, since this usually leads to external indebtedness. While liberals do not disapprove of moderate debt if it finances investment for long-term growth, mercantilists, emphasizing freedom of action for the state, tend to place greater emphasis on the leverage acquired by a lender and the dependence suffered by a debtor.

Apart from differences over goals, mercantilists also question the wisdom of relying upon 'the invisible hand of self-interest' to determine such an important facet of a nation's long-term development as its industrial structure. They fear that entrepreneurs motivated by a short-term profit calculus will be satisfied with existing comparative advantages and thus will fail to develop product specializations that offer greater long-term prospects for the nation as a whole. Advocates of managed trade contend that 'it matters whether a nation specializes in potato chips or microchips', for example, because the latter offers spin-off effects in technology and human capital development that encourage growth in other industries, thereby strengthening everything from the nation's education to its national security.

In this connection, there is some doubt about the adequacy of the Heckscher Ohlin (H–O) explanation for the sources of comparative advantage and, consequently, its implications for government policy. The liberal counsel that the state should avoid intervention in trade flows from H–O's assumption that the sole basis for comparative advantage lies in national endowments of land, labor, and capital—which governments can do very little to affect. This account, mercantilists point out, ignores two additional considerations long appreciated by both governments and business: a firm frequently gains an enormous advantage over its competitors by entering the market first and by operating at a larger scale.

The advantage of being first is the basis of the 'infant industry' argument that dates back to at least the seventeenth century: because mature firms have substantial advantages over new ones, 'infants' must be protected by trade barriers or subsidies until they can compete successfully. Because this idea was central to the mercantilist policies that built England's economy prior to its nineteenth-century liberalization, List argued bitterly that free trade is appropriate only for a nation with established firms. For all others, the state must identify those sectors in which it would be desirable to specialize—today we call this 'industrial policy'—and then protect firms in those sectors through policies which manage trade:

> It is a vulgar rule of prudence for him who has reached the pinnacle of power to cast down the ladder by which he mounted that others may not follow. In this lies the secret of Adam Smith's theory,…as well as all of his successors in the government of Great Britain. A nation which by protective duties and maritime restrictions has built up a manufacturing industry and a merchant marine to such a point of strength and power as not to fear the competition of any other, can pursue no safer policy than to thrust aside the means of elevation, to preach to other nations the advantages of free trade, and to utter loud expressions of repentance for having walked hitherto in the way of error, and for having come so lately to the knowledge of the truth.[15]

Related to this is the advantage of being big. Micro-economic branches of liberal theory that study imperfect competition refer to this as 'economies of scale', but until recently its implication for trade policy—that it validates the strategy of managed trade associated with mercantilism—was not recognized. In recent years this insight has given birth to a body of thought called 'strategic trade theory' which explains the success of the Japanese mercantilist approach, especially its export promotion and industrial policies. Strategic trade theory breaks with liberal theory in providing a defense for two propositions which are antithetical to the free trade canon. First, comparative advantage is not *discovered* by the savvy investor but actually *created* by a powerful state. Second, export promotion may be as essential to some infant industries as import protection, because in some sectors a firm cannot be sustained by the market of a single country. For both reasons, government intervention may be necessary to trade successfully, especially in the form of subsidies to firms with export potential.

Of course, government subsidies have always been capable of affording competitive advantage to firms in one nation over others, but such a policy was regarded as self-defeating for the economy as a whole because they require tax revenue to fund them. However, government intervention *would* be appropriate if comparative advantage rested on some factor that could be provided at no net cost only by the state. Strategic trade theory suggests at least three such candidates: very large-scale capital, co-ordination among competing firms, and a credible commitment to aggressive export promotion policies. To be successful, though, all require the existence of economies of scale; that is, the unit cost of production must decline as the volume of production increases. Economies of scale arise in all products to some extent but in only a few do they persist at a volume that saturates the market, usually when the variable costs of production are low in relation to the fixed costs. For example, the major cost for firms that produce computer software—paying programmers for the creative process of writing it—is fixed regardless of how many copies are sold. Its variable costs—buying blank disks to distribute the software—are very small. Consequently, once a firm has sold enough copies to recoup its fixed costs, it can sell additional copies profitably at a price which cannot possibly be met by a new firm that produces a competing product at much smaller volumes.

Because comparative advantage in such industries resides wherever large-scale production is initiated, an industrial policy that subsidizes start-up may be beneficial

to initial firms and absolutely essential to later ones. Subsidies need not cause a *loss* of consumer welfare but only a *postponement* of it, because the mature firm should eventually generate employment, profits, and tax revenue which repay the state for its initial support. If so, a mercantilist industrial policy may itself be a source of comparative advantage. That is especially true when economies of scale accrue *outside* the firm itself, but *inside* the nation in which it is located. For example, the concentration of chip makers and computer industries in the Silicon Valley of California makes it profitable for similar firms to locate in the same area, taking advantage of the skilled technicians and the research expertise of those already employed there. Because the original companies produce advantages enjoyed by later ones, it may not pay *private investors* to initiate a dynamic industry, even though it would benefit the economy of the *nation*. In cases of 'market failure' like this—that is, when the private market fails to provide adequate capital because of 'externalities'—the state can play a pivotal role.

Furthermore, a state with an activist industrial policy can bestow sources of comparative advantage that no private market can provide, such as subsidies for pure research or relief from onerous laws and regulations (like anti-trust). But the most formidable weapon of strategic trade policy is the reputation of the state itself for aggressively supporting an industry and ruthlessly competing with rivals. The promise to subsidize firms (or benefit them in other ways) well beyond the capacity of an unsubsidized firm to respond can intimidate potential competitors in other countries. Indeed, if the intimidation is great enough, neither the initial advantage nor the economies of scale need be especially large.

Mercantilism in Japanese trade policy

All of these ideas find expression in Japan's policy of managed trade, which became the focal point of a far-reaching industrial policy through which the state reshaped Japan's postwar economy. Autarchic development was impossible because Japan was very poorly endowed in key natural resources. Since it had to maintain a significant level of imports, export revenues were needed to pay for them, yet Japanese industry lagged behind its North American and European counterparts. Thus, Japan used mercantilist-inspired managed trade to develop globally competitive firms in a few well-chosen sectors that promised long-term growth. The methods combined initial import protection motivated by infant industry arguments with vigorous export promotion programs consistent with strategic trade theory. A complex set of policies co-ordinated by the Ministry of International Trade and Industry (MITI) controlled credit and imports, permitted monopolies, and granted favored firms direct subsidies, tax relief, and other public support. The unusually close connection between the government and private industry and the unusually prominent position of MITI within the government gave rise to the term 'Japan, Inc.' to describe the total social mobilization undertaken in support of these fledgling export industries. This reputation discouraged some American firms from even competing in sectors such as consumer electronics because they were convinced that the commitment of the Japanese government to capturing the American market would make

their efforts futile and costly. Meanwhile, Japanese rice production was heavily protected by import barriers.

Under the influence of these mercantilist policies, the Japanese economy in general —and several specific export industries in particular—achieved great technical sophistication and market success. Specifically, Japanese firms achieved global dominance in textiles in the 1950s, electronics in the 1960s, and autos in the 1970s and 1980s. Japan's trade surplus became the largest in the world, bringing an inflow of capital that permitted aggressive foreign investment, not least in the form of purchasing more than 100 billion dollars of US Treasury bonds. This gave Japanese investors considerable leverage in affecting the American economy, which partially offset Japanese military weakness whenever the relative power of these two states became an issue in foreign policy.

The idea and practice of 'fair trade'

Japanese success in managing trade poses a dilemma for US policy: how to maintain a free trade doctrine when trading partners do not. If other nations practice extensive import restrictions, even a liberal nation may find it difficult to find export markets. While this 'reciprocity' objection is a common feature of all debates over free trade, liberal economists are unanimous in finding it to be totally without merit because protection always hurts consumers by increasing the prices of imports. Thus, while Smith acknowledges that 'revenge naturally dictates retaliation', he finds the policy unwise: 'it seems a bad method of compensating the injury done to certain classes of our people to do another injury ourselves, not only to those classes, but to almost all the other classes.'[17]

The sole exception to the principle that retaliation is self-defeating is the allowance that temporary measures designed to induce others to eliminate the objectionable barriers may be justified. On how far in this direction it may be safe to go, sage judgment cannot be found in the analytical ability of the economist, says Smith, but in 'the skill of that insidious and crafty animal, vulgarly called a statesman or politician'.

Statesmen in liberal nations frequently see great opportunities for such diplomacy to achieve 'a level playing field' for their nation's firms in competition with mercantilist ones. Because the methods such liberal states employ often borrow from the very managed trade policies to which they object, it is common for them to package these initiatives under the rubric of 'fair trade' rather than 'free trade'. This is especially true in the United States, where, ironically, the reaction came about the time the Japanese strategy was undergoing change anyway. Japan had become fully competitive in global markets by about 1975, and since then its trade policy has moved away from mercantilist extremes.[18] However, the balance of trade deficits remain, and so do the political pressures on the US government to defend American firms and workers from Japan's 'unfair' trade practices.

Though the United States remains committed to a liberal international system, US policy has employed a range of defensive tools of managed trade to achieve 'fair trade'. Section 201 of the Trade Reform Act of 1974 charged the US International Trade Commission (ITC) with investigating petitions for import relief and

recommending action to the President. Between 1974 and 1986, fifty-five cases were investigated under Section 201 and relief was provided in eighteen of them. GATT's Article VI, which permits countervailing duties to offset foreign subsidies, was implemented by Section 301, which authorizes retaliation against any foreign manufacturer found to be engaging in 'unjustifiable, unreasonable or discriminatory' trading practices. Countervailing duties are used by the United States primarily to protect American industry from injury caused by the 'dumping' of foreign manufacturers, which consists of either selling a product abroad for below its cost of production or below the price for which it is sold in the home market. The ITC has authorized countervailing duties against many countries, but the most frequent target has been Japan. The 'Super 301' provision of the 1988 Trade Act places pressure on the President to designate 'priority foreign countries' who maintain 'unfair' trading practices and to set a deadline for progress in correcting them. The major target again was clearly Japan, but both 301 and Super 301 have been broadly used in recent years. Such actions provide the teeth that encourage nations to seek bilateral negotiations with the United States over trade disputes.

As a result, it has become common for the United States to require competitors to 'voluntarily' reduce exports through bilateral voluntary restraint agreements (VRAs). Of course, when the United States asks another nation to restrict its exports and threatens retaliation if it does not agree, the agreement is voluntary in exactly the same sense that one hands over one's wallet to a gun-toting mugger voluntarily. The most notable of these arose from a conflict over automobiles which began in the 1970s and culminated in the early 1980s. In June of 1980, the US Senate adopted—by a vote of 90 to 4—a resolution calling on the Carter administration to send a signal to Japan by reviewing US import policies. In 1981, a VRA was negotiated that limited sales of Japanese cars in the United States to 1.68 million units per year. This illustrates that fair trade really means managed trade, even if one of the parties would have preferred free trade.

Conclusion

Thus, we see that the venerable ideas of international trade theory continue to exert a profound influence on contemporary trade policies. Given the range of alternative values being sought by nations and the different priorities attached to them by various actors, it is hard to argue unequivocally that any of these trade strategies best achieve the interests of any nation. We can say, however, that the acceptance of some ideas and the rejection of others powerfully shapes the strategies employed by nations—quite likely more than the interests themselves.

Notes

1 Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations* (London: Dutton, 1910).

2 David Ricardo, *Principles of Political Economy and Taxation* (London: John Murray, 1871)
3 For a graphical representation of both the Ricardian idea and its more modern extensions, see Paul Krugman and Maurice Obstfeld, *International Economics: Theory and Policy* (Glenview, IL: Scott, Foresman, 1988).
4 See, especially, Ohlin's classic work, *Interregional and International Trade* (Cambridge, MA: Harvard University Press, 1933).
5 Smith, *The Wealth of Nations,* p. 400.
6 See, for example, John Kingdon, *America the Unusual* (New York: St Martin's Press, 1999).
7 For example, liberal opponents seeking to discredit strategies of managed trade frequently cite the (disputed) effect of the Smoot-Hawley tariff in deepening the Great Depression.
8 A survey in which 95% of American economists support the proposition that 'tariffs and import quotas reduce general economic welfare' is reported in Douglas A.Irwin, *Against the Tide: An Intellectual History of Free Trade* (Princeton, NJ: Princeton University Press, 1996), p. 3. For a discussion of the quasi-religious character of the Anglo-American view of international trade, see James Fallows, 'How the world works', *Atlantic Monthly* December, 1993, pp. 61–87.
9 Of course, the trade policies of almost all nations, even the United States, encompass elements of both traditions.
10 Irwin's position (*Against the Tide,* p. 5) is illustrative:

> There are a multitude of non-economic arguments for protection.... These include political arguments (e.g. protection of an industry for national defense) or others broadly geared toward achieving some vaguely national or social objective (e.g. greater self-sufficiency in certain goods). Such considerations may or may not be important, but they will not be considered here. [because] Economic analysis can contribute little in determining whether or not such policy objectives are advisable.

11 To be sure, the liberal cosmology identifies several other values associated with the free trade prescription—including the belief that interdependence among nations will lead to international peace and that the economic freedoms in the marketplace will spill over into political freedoms—but these are not amenable to analysis within the deductive structure of formal economics and have played a limited role in advancing the case for free trade.
12 Smith, *The Wealth of Nations,* p. 408.
13 For example, 'under typical parameters, lowering of a trade restriction will result in $5 or more of income being shuffled among different groups for every $1 of net gain'. Dani Rodrik, *Has Globalization Gone Too Far?* (Washington, DC: Institute for International Economics, 1997), p. 30.
14 See Karl Polanyi, *The Great Transformation* (Boston: Beacon, 1944), for the argument that self-regulating markets are destructive of desirable social bonds.
15 The latter is usually linked to both socialist and Keynesian ideas, but Ruggie sees it as a pragmatic tactic in furthering liberalism. By pairing an expanded distributive role for the state domestically with free trade abroad—the so-called 'compromise of embedded liberalism'—the mercantilist *value* of maintaining social stability is met without resorting to the mercantilist *strategy* of managing trade and thereby incurring its efficiency costs. See John Ruggie, 'International regimes, transactions, and change: embedded liberalism in the postwar economic order', *International Organization* 36:2, 1982, pp. 379–415.

16 Friedrich List, *The National System of Political Economy* (Philadelphia: Lippincott, 1956), p. 440.
17 Smith, *The Wealth of Nations,* pp. 411–12.
18 In 1955, Japanese output per worker was one-tenth of the American level, but reached 65% by 1985. See Charlie G.Turner, *Japan's Dynamic Efficiency in the Global Market: Trade, Investment and Economic Growth* (New York: Quorum Books, 1991), p. xi.

Further Reading

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Chapter 3
Agricultural trade policy

David N.Balaam

One of the themes of this book is that many 'new' issues such as telecommunica-tion systems, financial services, and intellectual property rights crowd the international trade agenda. Yet more traditional areas such as agricultural trade policy are of significance in understanding the nature of trade politics at the end of the twentieth century. Old and new trade issues are often closely linked, as was the case in the recently concluded Uruguay Round of the General Agreement on Tariffs and Trade (GATT) multilateral trade negotiations (1986–94) that covered some fourteen items. Some of the major players in this part of the talks threatened to end the talks if an agreement to liberalize agricultural trade was not forthcoming.

Many hailed the Uruguay Round's Agricultural Agreement, reached in November of 1993, as one of the biggest breakthroughs in the annals of trade policy. In past rounds, except for a few minor agreements, agriculture was usually taken off the negotiating table. The new accord (discussed below) establishes for the first time new trade rules and modestly reduces the level of protection for agricultural trade. And yet technically, agriculture remains one of the world's most protected items.

The main issue that this chapter addresses is why officials kept agriculture on the negotiating table in the Uruguay Round and did not drop it as they had done in previous GATT rounds. In this case attention to states and their strategies[1] helps to explain the outcome of the struggle to arrive at an agreement on agriculture. A number of analysts have viewed agricultural negotiations mainly through the lenses of group politics.[2] However, state reaction to group interests alone does not sufficiently explain how and why officials reached an accord on agriculture, other than to suggest that some groups might have influenced the outcome based on their interest in it. If, as some have suggested, farm and other groups were the most important factors in the situation, agriculture would have been taken off the negotiating table once again, given the opposition of many farm groups to liberalizing agricultural trade policy and reducing support for farm programs, especially in the industrialized nations. In the Uruguay Round, however, a focus on states and their representatives captures more of the proactive negotiating, bargaining, and reconciling processes along with the deals they struck to reach an agreement. Indeed, parts of the agreement reflect deals states made in opposition to some farm interests and in consideration of a broad variety of other domestic and international political and economic interests.

The first two parts of this chapter explain why and how the United States, EU, and Japan (the major agricultural players in the talks) agreed to reduce the level of protection for agriculture and some of the consequences of that agreement. The first part is a general discussion of the connection between national farm and international agricultural trade policies as well as the political and economic background conditions that pressured officials of the industrialized and developing nations to seek an agreement on agriculture in the GATT multilateral trade forum. The second part of the chapter examines the Agricultural Agreement itself and some of the different strategies state officials employed along with the difficulties they encountered in their efforts to arrive at a compromise.

The thesis of this chapter is that seen from the vantage point of state authorities, an agricultural agreement yielded two primary benefits. First, progress on liberalizing agricultural trade and establishing new rules in the GATT was a precondition for agreement to open trade in the other thirteen areas, an objective nearly everyone else had an interest in. A second and more immediate benefit for many of the major commodity-exporting states was use of the accord to control the cost of domestic farm support programs while also reducing levels of agricultural trade protectionism and opening up markets for their farmers multilaterally. Finally, as regards to both of these benefits, another argument put forward is that it is clear that the GATT institution mattered a great deal in helping members reach an agricultural accord. The last part of the chapter discusses a number of views about the agreement itself as well as conditions and problems that could make agricultural trade policy an even more contentious issue in future trade negotiations.

Domestic farm programs and agricultural trade

Academics and trade experts characterize the relationship of domestic farm to agricultural trade policy as one that reflects a problem related to the economic transformation (i.e. modernization) of society where the agricultural base of the economy shrinks while its industrial base expands. Since the Industrial Revolution the application of more land, labour, capital, and new technologies to the food production process has resulted in commodity overproduction and declining food prices for consumers, but also in excess farm labour and lower farm prices as food supply outruns demand. Therefore, without some kind of protection complemented by a combination of import tariffs and export subsidies, farmers are likely to go into debt or bankrupt.

Those officials and experts who espouse free trade policies argue that trade protection tends to exacerbate the oversupply problem by insulating domestic from world prices. This stimulates production that requires more state support and eventually distorts international trade; that is, the market's ability to clear surpluses, control production, and conduct international (free) trade based on comparative advantage.[3] Economic liberals also argue that the state assists farmers in declining numbers because the farm vote can sway an election or powerful farm groups lobby legislators for state assistance.

For other officials and experts the connection between domestic and international agriculture cannot be separated from a variety of state interests. Trade protection is justified to the extent that it promotes food security and, as in the case of Japan, limits dependency on food suppliers or, as in the case of France, protects what remains of an inefficient but socially valuable farm sector. Major commodity exporters like the United States and the EU use surpluses to earn foreign exchange, adding to national wealth and power. Finally, food is often used as political leverage in a hostile international environment.

Since the turn of the century, but especially after World War II, the major commodity-exporting nations have had to deal with the problem of commodity overproduction. In so doing they have used various policy tools and instruments to support their national farmers bolstered by import-restricting and export-enhancing measures. The United States, the EU (formerly the EC or European Community), Canada, and Australia have routinely been the world's biggest agricultural exporters. The US and EU alone control one-half the world's grain trade. Together with Japan, one of the world's largest importers of commodities and food products (the United States being the world's largest), the three of them strongly influence developments in the agricultural trade system to the extent they control and manage international trade and monetary affairs. In all of these nations the budgetary cost of support for domestic farm programs has risen over the years, albeit at very different levels in different nations. The OECD reports that in 1995 (after the Uruguay Round ended, no less) the total producer subsidy equivalent rose 15% above the 1986–8 average. Meanwhile, the number of those employed in agriculture in each of these nations continues to decline, as does agriculture's share in total exports.[4]

Over the years American grains, oilseeds, and cotton have received the most direct state support, as a reflection, in part, of the influence of commodity producer groups and general farm organizations. These and other commodities have been supported by acreage control, storage, and price support programs combined with food distribution, food stamp, and other surplus disposal programs including PL 480, the Food for Peace program that used food to assist anticommunist regimes during the Cold War. Pursuant to its new hegemonic role after World War II, the United States officially espoused free trade, but separated agriculture from other trade items. In 1955 the United States also received exemptions for its agriculture from the GATT's trade liberalizing rules,[5] accepting the EC's discrimination against its agricultural exports and food products as the price for sustaining its anti-communist alliance with the West Europeans under US political and economic leadership.[6]

As commodity surpluses continued to accumulate US officials paid increasing attention to foreign markets and employed export subsidies in conjunction with a flexible price support scheme for commodities that set farm prices closer to world market levels. When market conditions turned around in the mid-1970s the Nixon administration aggressively marketed grain to the USSR and encouraged production to meet less developed country (LDC) growing needs along with increasing West European and Japanese demand for American food products generated by dietary changes and a devalued US dollar. By the early 1980s global

demand had slackened and many developing nations including India and China and East European states stressed self-sufficiency policies, cutting back on imports of American commodities and food items. To support its farmers, the United States has also employed import quotas and tariffs on cheese, butter, sugar, and some beef items as well as voluntary export restraints on a number of items.

Protectionist EU agriculture policies reflect an even tighter connection between farm policies and agricultural trade than in the United States as EU officials have since 1968 tried to harmonize national farm and agricultural trade policies of a growing number of community members. Basically, the goals of the Common Agricultural Policy (CAP) of the EU have been threefold: to achieve food self-sufficiency; to maintain and increase farm income; and to preserve the small-farm character of rural Europe. Reflecting pressures from community farm groups such as Comité des Organisations Professionnelles Agricoles (COPA), to achieve these goals the CAP has used various infrastructural support measures along with price support and disposal programs to assist dairy, beef and veal, sugar, cereal grain, pork, and table wine producers. CAP programs have covered as much as three-fourths of the EU's commodities. Trade protectionist measures have included a variable levy instead of tariffs, to limit food imports into the community, accompanied by subsidies to encourage exports.

The CAP also separated agricultural commodities from other trade items and received exemptions from the GATT for its farm produce. Largely because of its self-sufficiency programs, in the 1970s the EC became a major agricultural exporter, hurting US disposal programs and drying up export markets in Europe. In the early 1980s the CAP was eating up as much as 60% of the EC budget and a number of Community members (notably the UK) campaigned for its reform. US complaints in the GATT over EC agriculture protection increased in the 1970s and early 1980s, but the United States did not press the issue as much as it might have because of concerns over sustaining the Atlantic Alliance.

The connection between farm and agricultural policies in Japan has also been quite tight. Japan is notorious for its farm support programs, especially for rice, citrus fruits, and beef aimed at protecting Japanese agriculture from international competition, minimizing Japan's dependency on overseas food suppliers, and managing the structural transformation process in such a way as to help sustain Japan's economic recovery and promote investment in its industrial development strategy.[7] State officials have supported Japanese agriculture with domestic commodity programs and especially import protection measures that included tariffs, import quotas, and a variable levy, along with import restrictions tied to strict health and safety standards. Japan began to restructure its farm sector in the 1980s in opposition to the highly organized national farm organization, *Zenchu,* but also in response to a number of domestic and international pressures including consumer demand for less expensive food and more imports, along with US and EC pressure on Japan to import more to correct its growing balance of trade surplus.

In LDCs the relationship of domestic farm to agricultural trade policies has varied a great deal. Officials in some of the Latin American countries up until the late 1970s

pursued import substitution policies and limited imports to assist local peasants and farmers. In other countries officials taxed agriculture to help fund development projects and resisted supporting agriculture to the extent that costly farm programs would undermine their urban base of support. In pursuit of liberal economic development strategies, some states have relied on imports to make up food deficits or to meet urban population demand for food products of the industrialized nations.

Some critics of the GATT's trade policies have charged that northern border protection measures discriminate against LDC commodity exports and serve the interests of northern industrialized over southern developing nations.[8] More economic nationalist in outlook, other southern trade officials have argued that despite the protectionist barriers southern nations face in the north, the terms of trade for LDC products can be improved by negotiations with the north. Given their advantages in agricultural production (LDCs account for roughly 33% of agricultural trade in the 1980s), such countries as Argentina, Brazil, Mexico, Thailand, India, and China have become increasingly more aware of the connections between farm and agricultural trade policies, all the while interested in GATT negotiations that would open the door for their exports to compete with those of the industrialized nations. Meanwhile, many of the major commodity exporters have sought to reverse the situation where many LDCs adopted self-sufficiency strategies in the early 1980s, in part to limit expensive imports and decrease their dependency on foreign aid.

Before the Uruguay Round began in 1986, the major players became involved in a number of serious trade disputes: the United States with the EU over restrictions on imports of American chicken, pasta, and oilseeds, and with Japan over its rice, citrus, and beef import barriers. In some cases the United States complained to GATT, but found it to be ineffective in solving these disputes. A generally tense and competitive atmosphere reflected weak market conditions for agricultural exports along with frustration over the rising cost of domestic farm programs coupled with the growing use of protectionist trade measures by other commodity exporters and importers. LDCs routinely complained about the discriminating trade practices of northern industrialized nations against their primary agricultural and other products. At the GATT ministerial meeting in Geneva in 1982 that led to agreement to pursue a new round of talks, many state officials felt strongly that domestic and international protectionist measures had greatly distorted and destabilized international trade and that further liberalization of the entire trade system was needed. However, progress in other areas could not be made without an agreement to reduce agricultural trade protection.[9] Thus, in an effort to further liberalize trade and establish new trade rules in fourteen areas, at the opening session of the Uruguay Round at Punta del Este, Paraguay, in September 1986, GATT members agreed once again to confront the issue of international agricultural trade.

State strategies for agriculture in the Uruguay Round

The Final Act of the Uruguay Round produced an agreement on agriculture that included five elements.[10] First, export subsidies were to be cut in value by 36% and in volume by

21 % for the next six years; LDC cuts were 24% and 14% respectively over a ten-year period. Second was a reduction of 20% in aggregate domestic farm support. Third, 'tariffication'[11] required that non-tariff barriers be made transparent, that is visible, such that they could be quantified and added to existing tariffs and then reduced by 36% over the next six years. Additionally, protection for the most sensitive products was to be reduced by at least 15%, and countries would have to allow for imports equivalent to 3% of domestic production. Two other measures of the agreement included Sanitary and Phytosanitary (SPS) trade controls to protect human, animal, or plant life or health, and finally, a 'peace clause' whereby, if countries abided by their obligation to cut subsidies and trade barriers, they would be immune from WTO complaints for nine years. The Final Act of the Uruguay Round also contained several provisions that affect agriculture by strengthening the dispute settlement process. Timetables for decisions are to be set and bilateral settlements encouraged.

Although some trade officials and academic experts view the Agricultural Agreement itself as imperfect, they nonetheless see it as a major achievement because it begins the process of gradually reducing export subsidies and increases competition among exporters. Tariffication renders non-tariff and other barriers more transparent and easier to cut, and also generates more pressure that undermines support for them. Under the agreement American and EU farmers will continue to receive direct payments, but these payments are now decoupled (separated from production) thereby helping to decrease the distortion of international trade. Finally, because the agreement creates new rules to resolve trade disputes, it is also expected to help de-escalate US and EU export subsidy wars, especially over grains and oilseeds.

Others, usually strong supporters of free trade, were disappointed if not upset that the agreement did not substantially cut or eliminate altogether export subsidies for agricultural commodities and products. Not only does it not bite hard enough into protectionist measures, but it has the effect of sanctioning remaining subsidies and tariffs in the new WTO. The new export subsidy cuts are not commodity specific; countries can group them in any combination to arrive at the required average needed to show a decrease in support. Nations can also shift support for farm programs as long as they stay underneath the required ceiling of reduction, while some support programs, such as those for milk, remain exempt from the new rule. Also, ambiguous rules could result in 'dirty tariffs' where officials can inflate tariff rate equivalents used as base levels, negating the effort to cut tariffs. Finally, detractors worry that other countries may try to model their domestic farm programs on those of the United States and EU, thus slowing the process of trade liberalization.

Why did negotiators only marginally—if at all—reduce protection for agriculture? The argument put forward here is that after seven years of negotiations, officials compromised enough to make a dent in agricultural protection, while as yet preserving much of their domestic support and trade protection measures. At least four distinct factors combined to play a role in making the Agriculture Agreement part of the Final Act of the Uruguay Round possible: first, the central role an agriculture agreement played as a common objective in the talks; second, the critical condition that state officials had separated themselves enough from domestic farm

groups and other protectionist interests such that they could compromise at the ministerial level and conclude an agreement; third, the political and economic resources brought to bear on the outcome as well as their ideological outlook and willingness to comprise with one another; fourth and finally, the supportive role the GATT played in the negotiations.

The central role of agriculture

The important point here is that, despite technical difficulties and political setbacks, what drove national officials to reach an agreement more than anything else was the linkage between the anticipated gains to be made from liberalizing trade in other areas and an agreement on agriculture. But reaching an accord on agriculture was no easy feat. One trade expert put it aptly when he said that 'agriculture provided the glue, not the guts, of the Uruguay Round package of agreements'.[12] Several times during the negotiations, talks either deadlocked or broke down, usually over various technically complicated and politically charged issues related to agriculture. The first four years of the talks were spent assessing the situation and engaging in verbal jousting before the major parties got down to serious negotiations in 1990. After threatening to end the talks at two ministerial meetings in Montreal in 1988 and Brussels in 1990, officials began to compromise their positions, although no agreement was reached. A final agreement for the Uruguay Round that included liberalizing agriculture trade was hashed out in late 1992 at Blair House in Washington, DC. GATT members signed the Final Act of the Uruguay Round at Marrakesh in April 1994, creating the WTO to succeed the GATT.

The United States, backed by Australia—leader of the Cairns Group[13]—and Japan, was most interested in liberalizing agricultural trade policy. The Reagan administration opened the talks with a dramatic proposal to phase out all trade-distorting subsidies over a ten-year period (the so-called 'zero option', matching the President's arms control proposal in Europe at the same time). EC officials felt the United States was insincere and only trying to scuttle an agreement by starting from a position everyone knew was unacceptable. But Reagan officials viewed an agriculture agreement as an opportunity to accomplish two interrelated goals: first, by going after the protectionist measures of other exporters and opening up markets for American commodities all over the world, not just bilaterally, the administration could counter Congressional protectionist pressures on the administration and help cut farm program budget costs. Early on the administration had tried to reduce significantly the coverage and level of support of its farm programs, but Congress created the Export Enhancement Program (EEP) in 1985 and increased funding on other export-stimulating measures. Second, also at stake for the United States were broader national and international interests that included dealing with a growing balance of trade[14] and payments deficits and mounting debt. The United States also had an ulterior political objective, namely to reassert US political and economic hegemony by forcing the EC and Japan to tear down their trade barriers. Many Reagan officials also felt that the EC and Japan should help make a bigger contribution to the cost of US efforts to manage the international political economy.

Reluctantly, the EC came around to supporting new trade talks but was afraid reform would require more and bigger adjustments to the CAP, which tied farm support payments for different commodities to fluctuating (green) ECU currencies.[15] Owing to conflicting interests of its members, EC officials also found it problematic to develop a common negotiating strategy. The Council of Ministers eventually agreed to the talks, provided that discussion covered everyone's direct and indirect forms of support for agriculture, not just the EC's.

Japan went into the negotiations supportive of liberalizing trade in other areas but resistant to great change in its agriculture structure and reluctant to negotiate its farm and agricultural trade policies in a multilateral forum.

Some of the major technical sticking points in the talks were issues surrounding import restrictions, domestic support, and export subsidies. One of the major breakthroughs was on the issue of tariffication, which made import levies more transparent and convertible into tariff equivalents. EC domestic prices could then be 'recoupled' to world market prices and tariffs reduced over time. Negotiators also had trouble measuring different domestic protection levels and instruments. New trade rules would eventually mean cutting the budget costs of domestic farm programs. In Geneva, many US officials favored decou-pling US deficiency payments from production because that kind of support stimulated overproduction. Eventually, with pressure and assistance from GATT officials, negotiators supported the aggregate measurement of support (AMS)[16] as the best way to deal with the problem of comparing different (national) levels and instruments of support. Meanwhile, in 1990 EC agriculture ministers rejected Commissioner Ray MacSharry's proposal to reduce domestic support by 30%, and the French minister accused him of exceeding his mandate to reform the CAP. Much wrangling in the European Council and Commission brought about another impasse within the Community as some member governments faced new elections and were pressed not to reform significantly their agriculture sectors. Meanwhile, the United States and the Cairns Group made proposals to cut domestic trade-distorting subsidies by 75% and export subsidies by 90% as well over a ten-year period. Despite some progress, negotiations ended when the LDC members of the Cairns Group walked out of the talks for lack of an agricultural agreement.

Even so, GATT and other officials continued to search for solutions during the Persian Gulf War when allied co-operation took precedence over trade disputes. A second breakthrough came when EC Commisioner MacSharry led a successful two-year effort to reform the CAP 'as the EC sought to produce a GATT offer to meet its international obligations'.[17] Briefly, these reforms committed the EC to ensure that deficiency payments to its farmers would continue despite being decoupled from production (the new 1990 US Farm Bill already incorporated decoupling in determination of direct payments to farmers). The EC also increased set-asides for French farmers by 27%. A new EC proposal also became more acceptable to Community members because it cut domestic support by 30% based on 1986–9 levels, which meant that for some commodities, support would actually increase under the new agreement. Likewise, proposed export subsidy and tariff levels would

actually end up higher than they might have been without an agreement, given the flexibility in determining which products would be covered under the agreement.

When the United States and the EC became immersed in a new dispute over EC oilseed tariffs in 1992, Blair House in Washington, DC, served as a venue to resolve the dispute and to finally reach an accord on agriculture in the Uruguay Round. Despite French opposition, MacSharry assured the EC that the new agreement was in keeping with the latest CAP reform efforts. German Chancellor Kohl shifted to support the new agreement and pressed for a conclu-sion to the round, isolating the French, who did not carry through on their threat to veto the agreement.

The new Clinton administration supported the proposed accord, and its new US Special Trade Representative, Mickey Kantor, together with the EC's Trade Commissioner, Sir Leon Brittan, gained control over negotiations in their respective delegations and worked hard to put together an agricultural agreement. To reach an agreement on December 15, 1993 that would end the entire round, the United States made several concessions to the French, exempting 25 million tons of cereal stockpile from the agreement and shifting the base periods used to average export subsidies.

Throughout the talks the major players were unwilling to risk losing potential 'sweet deals' in areas such as financial services and intellectual property rights for lack of a serious effort to reduce the levels of protection for agriculture. The Final Act promised the industrialized nations more access to one another's and to LDC markets. In exchange LDCs were to gain access to industrialized markets for their primary commodities and for an increasing number of their semi-processed and finished products.

State separation from farm groups

A second factor that contributed to officials reaching an agreement on agriculture was the gradually increasing distance that they had put between themselves and their constituent farm groups and other protectionist interests since the 1970s. This was more the case in the United States and Japan than in the EC where groups in Ireland, Germany, Spain, Portugal, and France are still relatively strong. In the United States there are at least three strong interrelated pieces of evidence to support this contention. The first is President Reagan's proposal to gradually eliminate protection for agriculture. Even though it was a starting point, it sent a signal to American farmers that the state was no longer going to support them automatically in trade talks. The second is the practice of tariffication, which applies to all states and marks a distinct development in the history of agricultural trade policy. Because import barriers are quantified, reduced, or bargained away like any other trade item, farm and other groups have been put on notice that state officials may be willing to compromise their interests with other domestic and international interests. Finally, that agriculture was not taken off the table as it had been in the past also reflects the increasing autonomy of negotiators given that state officials were no longer willing to exempt agriculture from trade negotiations.

Several developments have contributed to this trend of increasing separation between state officials and farm groups. One is the increasing authority officials have

accumulated pursuant to their role in managing national economic functions like trade and monetary policy in the United States, EU, and Japan in particular. There has also been a gradual weakening (or diffusion) in the voice of farm groups in these countries related to increasingly contentious views about trade within their farm communities and the growing number of non-farm interests that compete with them.[18] Another development that makes state officials more autonomous is the transformation of the agriculture sector in these economies where farm and commodity production is no longer dominated by small family farmers. More often, state officials must reconcile the interests of bulk commodities with the broader interests of upstream food investment, processing, packaging, marketing, and transportation businesses of the 'agrofood' sector. Most of these businesses are pro free trade and stand to profit from greater volumes of food in commercial channels.[19]

This is not to say that farm interests still do not constrain state officials when it comes to agriculture. If they did not, clearly they may have been more easily traded away during the negotiations. Certainly pressure on US state officials by beef, dairy, and soybeans groups, for example, had something to do with the United States shifting away from its zero-option proposal. The argument here, however, is that during the talks it was the state that negotiated the terms and 'big deals' of the agreement, more often representing its own interests over those of its different constituents. In the case of the United States, farm group views on the Uruguay Round were diverse, with of many of them complaining about the US official position and taking their cues about trade policy from the Department of Agriculture or the Office of the US Trade Representative. Rufus Yerxa, the permanent US Representative at the GATT, told the author that during the talks, groups were in a 'feeding frenzy' until they could be shown the benefits of the deals that were struck in a final agreement. They were constantly barraged with figures like $ 1 trillion in economic gains in the next decade, and $35 million a year in earnings from trade.

Likewise, EC and some national officials also helped organize community groups. Moyer and Josling argue that EC proposals were 'shallow gestures' to put off the United States but that 'the EC proposal was a conscious attempt by the Commission to impose on the domestic political process some constraints from outside the narrow agricultural area'.[20]

State resources

During the negotiations officials employed a variety of resources to achieve their state-conducted diplomacy according to the internal and external pressures on them. At first the US style consisted primarily of blaming the EC and its CAP, along with Japan, for distorting international trade, but also cajoling and provoking them, especially the EC, into significantly reducing protectionist trade measures and ultimately continuing to reform their domestic agricultural structures. Some experts view Reagan's zero-option proposal as a masterful stroke because, even though the United States protected its agriculture, the President shifted the burden of proof on the EC and Japan to justify continued use of support for agriculture. Espousing economic liberal and free trade

principles, Reagan (and later Bush) officials[21] often blurred the line between free trade and managed fair trade when they went so far as to threaten Japan, India, and Brazil (among others) with Super 301 trade legislation,[22] which required the President to punish those nations using unfair trade practices to hurt American producers. Other intimidating measures included threatened loss of American markets, more bilateral agreements made with other nations, and the loss of markets that would likely result from US efforts to promote regional trade agreements with its American (via NAFTA) and later with its Asian (via APEC) neighbors. From time to time the administration also used the threat of Congress increasing export subsidies, which it did in the form of legislation to protect soybeans, in the event talks failed, to pressure competitors.

Once negotiations got serious, the Bush administration sought to isolate the EC by emphasizing common interests with some members of the Cairns Group and Japan. Interested in easing bilateral economic but also security relations with the United States, throughout the talks Japan generally 'kept its head low' while US and EC officials engaged one another. Quite often its negotiating style reflected an effort to appear co-operative and a team player, thereby playing a more positive role in the international system. The Cairns Group found itself in fundamental agreement with the United States and shifted its role in the talks to become an honest broker between the major parties.

Under the Bush and Clinton administrations officials like Trade Representatives Carla Hill and Mickey Kantor acted less aggressively and adopted a tougher but sometimes conciliatory negotiating posture, all the while focusing on making deals and reaching an agreement. President Reagan's earlier zero-option proposal notwithstanding, it was difficult for them to support an agreement that would completely liberalize agricultural trade. However, they did want an agreement that began the process of liberalizing agricultural trade.

EC officials acted more defensively throughout the talks, especially in the face of US efforts to push them and the anticipated adjustment costs that would come with an agreement. However, even as they enlarged the community, many EC ministers and commissioners felt they could no longer claim that trade protection was the price to be paid for European integration or extending the Community eastward. In his effort to reform the CAP, MacSharry and other national officials used the negotiations to claim that domestic programs would have to be cut back in order to come into line with GATT proposals.

The role of the GATT

Finally, GATT officials played a critical role in talks. They continually pressured national officials to negotiate, even when the talks were stalemated or when countries walked out of them. Their strategy was to stay one step ahead of national officials with recommendations that moved them closer together and to make negotiators aware of their stake in the outcome. GATT officials also performed a variety of functions that helped members solve and get by a number of technical and political sticking points such as accepting the AMS and the idea of tariffication. GATT Director-General Arthur

Dunkel's 'deft diplo-macy'[23] resuscitated the talks in 1990, and, for all intents and purposes, he wrote the final draft that served as the basis of the Final Act of the Uruguay Round.

GATT's critical role in the talks was based on the opportunity it provided national officials to see the whole agriculture picture. At the state level, institutions mitigate differences between groups and other actors, and in previous rounds there had been a tendency to capitulate to the demands of producer groups. At the GATT level in this round, however, state officials were able to make proposals and deals, while seeing where they could make concessions and which parts of the system would be advantageous to them.

Future agricultural trade talks

The next scheduled meeting to review progress on implementing the Agriculture Agreement is due to take place in 1999. Market conditions for commodity exporters continue to remain poor while the costs of domestic programs continue to grow, distorting international trade. Given the precedent set by the Agricultural Agreement in the Uruguay Round, at future ministerial reviews and negotiations progress in liberalizing trade in other items is once again likely to be linked to more progress in reducing agricultural trade barriers. Tariffication promises to make identification of import barriers easier and, therefore, the negotiation of reductions in their levels. Likewise, agreement about domestic AMS may also help states negotiate reductions in these programs. Whether state officials can maintain a distance between themselves and their protectionist bulk commodity constituents remains to be seen. Likewise, it remains to be seen whether the United States will continue to use what remains of its hegemonic power to promote openness in this part of the trade system. Given the Clinton administration's emphasis on enhancing American trade competitiveness, the chances are that it will. The globalization process also continues to pressure state officials to counter trade protectionism as it hastens the pace of liberalization and economic integration. Finally, some are hopeful that increasing authority and a bigger role for WTO officials in the negotiation process itself will help facilitate reductions in protection.

Future talks could be equally, if not more, frustrating, and even less productive than were these talks owing to a number of combined technical and political economic issues and trends. To make progress future negotiations will have to 'bite harder' into the flexibility and slippage of the current agreement when it comes to commodities covered under export subsidies, import measures, domestic farm support programs, and setting sanitary and phytosanitary health standards. The extent to which officials will be willing to do this depends on the extent to which they can reach an agreement that allows them to reconcile domestic with international interests. Yet, as commodity surpluses accumulate in the major grain-exporting countries, especially wheat and corn, state officials will more than likely face protectionist pressures, especially in their legislatures, to subsidize agricultural exports instead of funding costly commodity-specific domestic programs as a partial solution to budget constraints.

Officials are also likely to encounter more support for protecting agriculture as part of a growing anti-globalization, anti-trade liberalization effort that views the WTO as part of an effort to transfer control of food production and distribution to apolitical agribusinesses and other multinational business enterprises.[24] Others less critical of the WTO argue that officials are increasingly being pressed to reconcile their trade liberalization efforts with a broader and politically more complicated state agenda that combines food production (agrarian) issues with other issues on the agro-food agenda, including the impact of overproduction on the environment, food health and safety, food security, and Third World development.

In international negotiations, tariffication makes import barriers more transparent, but the bulk of agricultural commodities continues to be relatively 'location-based' tradable goods that tend 'not to enjoy the economies of scale and product differentiation found in many industrial products'.[25] This study has shown that agricultural trade now shares many of the characteristics of new traded items: that is, states are willing to make deep cuts in protection for their products and resolve trade issues multilaterally. However, the political sensitivities associated with agricultural commodities are still very different from those associated with semiconductors or banking services. Recent EU efforts to join with the Latin American Mercosur nations has once again generated strong French opposition to 'cheap imports' that are likely to come into the community.[26] In the meantime, agricultural trade negotiations are likely to still be more multinational than transnational in character, and thus more difficult to negotiate than new items in any sizeable forum.

Notes

1 John Zysman, *Governments, Markets, and Growth* (Ithaca, NY: Cornell University Press, 1983), comes close to developing a framework by which to compare different industrial state strategies, although not in the case of agricultural trade policy.

2 See, for example, D.Gale Johnson, *World Agriculture in Disarray* (New York: St Martin's Press, 1991), and also Robert Paarlberg, 'Agricultural policy reform and the Uruguay Round: synergistic linkage in a two-level game?', *International Organization* 51:3, Summer 1997, pp. 413–44.

3 Johnson, *World Agriculture in Disarray*.

4 OECD, *Agricultural Policies, Markets and Trade in OECD Countries: Monitoring and Evaluation 1996* (Paris: OECD, 1996), p. 12.

5 The two main areas in which agricultural trade receives special exemptions from GATT rules are Article XVI that applies to export subsidies and Articles XI and XIII that apply to quantitative restrictions.

6 See Benjamin J.Cohen, 'The revolution in Atlantic economic relations: a bargain comes unstuck', in Wolfram Hanrieder (ed.), *The United States and Western Europe* (Cambridge, MA: Winthrop, 1974), pp. 106–33.

7 For a more detailed discussion of the role of agriculture in Japan's recovery strategy see David N.Balaam, 'Self-sufficiency in Japanese agriculture: telescoping and reconciling the food security-efficiency dilemma', in William P.Browne and Don F.Hadwiger (eds), *World Food Policies: Toward Agricultural Interdependence* (Boulder, CO: Lynne Rienner, 1986), pp. 91–

105, and Masayoshi Honma, 'Japan's agricultural policy and protection growth', in Takatoshi Ito and Anne O.Krueger (eds), *Trade and Protection* (Chicago: University of Chicago Press, 1993), pp. 95–114.

8 Many Marxist structuralists and other critics of these strategies have documented cases where a good deal of state assistance goes to agribusinesses or firms that invest in that country, many of them producing crops for export to northern markets, while local producers become impoverished and state officials dependent on foreign aid and foreign direct investment. See, for example, Susan George, *Ill Fares the Land: Essays on Food, Hunger, and Power* (Washington, DC: Institute for Policy Studies, 1984).

9 Tim Josling, 'Multilateralism: a constraint on unilateralism and regionalism in agricultural trade', *American Journal of Agriculture Economics* 75, August 1993, p. 808.

10 For a more detailed discussion of the Final Act of the Uruguay Round see Jeffrey Schott, *The Uruguay Round (Washington,* DC: Institute of International Economics, 1994).

11 For more detailed discussion of issues surrounding tariffication, see Paarlberg, 'Agriculture policy reform and the Uruguay Round'.

12 Schott, *The Uruguay Round,* p. 43.

13 The Cairns Group was named after the Australian city where fourteen nations who supported the liberalization of trade met before the Uruguay Round got underway. These nations were Argentina, Australia, Brazil, Canada, Chile, Colombia, Fiji, Hungary, Indonesia, Malaysia, the Philippines, New Zealand, Thailand, and Uruguay.

14 The US trade deficit had grown from $31 billion in 1977 to $122 billion in 1985. See OECD, *United States: 1989/90* (Paris: OECD, 1990).

15 The European Commission uses a mechanism known as the Monetary Compensatory Account (MCA) to establish special exchange rates that convert common farm prices into national currencies. See David M.Wood and Birol A.Yesilada, *The Emerging European Union* (White Plains, NY: Longman, 1996), p. 153.

16 According to Alan Swinbank and Carolyn Tanner, the AMS is 'the difference between the domestic and world price, multiplied by the volume of production, plus any direct or indirect payments received by the farm sector'. See their *Farm Policy and Trade Conflict* (Ann Arbor, MI: University of Michigan Press, 1996), p. 71.

17 Swinbank and Tanner, *Farm Policy and Trade Conflict,* p. 88.

18 As per the United States, this is one of the subthemes of William P.Browne, *Private Interests, Public Policy, and American Agriculture* (Lawrence, KA: University of Kansas Press, 1988).

19 For a more detailed discussion of this trend in the United States, see J.C.Brooks and C.A.Carter, *The Political Economy of US Agriculture* (Canberra: ABARE Research Report 94. 8), especially Chapter 3.

20 H.Wayne Moyer and Timothy E.Josling, *Agricultural Policy Reform: Politics and Process in the EC and the USA* (Ames, IA: Iowa State University Press, 1990), p. 190.

21 While many attribute the administration's liberal outlook and tough negotiating style to Reagan himself, Alan Oxley, Australia's Representative to the Uruguay Round, claims that Clayton Yeutter, US Special Trade Representative at the time, was the inspiration behind the move. See Alan Oxley, *The Challenge of Free Trade* (New York: Harvester Wheatsheaf, 1990), Chapter 5.

22 Super 301 is a provision of the 1988 Omnibus Trade and Competitiveness Act.

23 Swinbank and Tanner, *Farm Policy and Trade Conflict,* p. 74.

24 Karen Lehman and Al Krebs, 'Control of the world's food supply', in Jerry Mander and Edward Goldsmith (eds), *The Case Against the Global Economy: And for a Turn Toward the Local (San* Francisco: Sierra Club Books, 1996), pp. 122–30.

25 Tim Josling, 'Multilateralism: a constraint on unilateralism and regionalism in agricultural trade', p. 807.
26 Neil Buckley, 'Farm fears hit EU plan for Mercosur deal', *Financial Times* 9 July 1998.

Further reading

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Chapter 4
International trade in services

Michel Kostecki

Services stand out as one of the most dynamic components of international trade and the nature of international service transactions is changing rapidly. What is international trade in services and why is it important? What are the driving forces behind the services trade and how is the General Agreement on Trade in Services (GATS) affecting trade politics in that area?

International trade in services

A service is variously defined as an activity, performance or an advantage. The most widely used definition of services in international trade is that based on the listing of twelve service sectors and 155 subsectors adopted by the GATS (Table 4.1).

Table 4.1 What are services?

Business services (including professional and computer services)
Communication services
Construction and engineering services
Distribution services
Educational services
Environmental services
Financial services (insurance and banking)
Health services
Tourism and travel services
Recreational, cultural and sporting services
Transport services
Other services (not included elsewhere)

Source: WTO Secretariat

This definition has the advantage of being clear cut, but numerous service activities, such as services performed within the manufacturing firms or certain services around products, escape its attention. Definitions are important in the GATS context because it is against their background that trade negotiations take place.

Export of services differs from export of manufactured goods. Services are most often intangible and cannot be stored. Proximity between demanders and service

Table 4.2 Modes of service exports

Cross-border supplies
Consumers abroad
Temporary entry of natural persons
Commercial presence (FDI)

providers is then usually required for services to be marketed.[1] Certain service transactions may occur across borders (e.g. 'on-line'), but others will require that clients and service providers are at the same place at the same time. This can be achieved through the temporary entry of service providers into the territory of a client or via physical movement of consumers to the location of the service provider (as in the case of tourism). All three modes of service supply are considered to be international trade and are reported as such in the balance of payments. But many services are not tradable and this means that cross-border exchanges or temporary physical movement of providers or clients do not suffice for an exchange to be feasible. Providers of such services can contest foreign markets only by establishing a long-term commercial presence abroad by engaging in foreign direct investment (FDI). The GATS negotiators agreed that sales by foreign firms maintaining a commercial presence abroad are international trade in services. Export of services therefore covers four modes of service supplies as listed in Table 4.2.

Commercial services worldwide were valued at above US$10,000 billion in the late 1990s, close to one-half of the world's total production of marketed goods and services. Services are traded less than tangible goods. In the high-income countries (OECD) the ratio of exports to output is on average over six times less than for manufactured products. The value of services traded across borders is about $1.3 trillion, that is about 25% of the value of merchandise trade. This is small given that services account for more than half of the world output.[2]

During the period 1987–97, services have been the fastest-growing component of international trade. Leading exporters and importers included the United States (about 17.5% of the world exports in 1997), Germany (5.7%) and Japan (5.2%).[3] These figures—referring to services traded across borders—will substantially increase if account is taken of services marketed abroad by subsidiaries or affiliates of foreign firms. Conventional wisdom holds that FDI is probably the dominant mode of export marketing for most categories of services and that it is increasing in a spectacular manner.[4] For example, US data suggest that the value of services marketed by American affiliates abroad is roughly of the same importance as the value of other forms of American exports of services.[5]

The anatomy of change

Services assume an increasingly strategic role in business and economic development. Factors such as new technologies (which lower costs and render many services tradable), technical complexity and product differentiation, client orientation and more services around products require a new state of mind in management of international trade transactions (see Table 4.3).

Table 4.3 Forces driving the change in international services markets

Strategic role of service in merchandise exports	Reduced economic distance
Extended product responsibility	Increased tradability of services
Products contain more intellectual property	Growing demand for services
Technical complexity of products	Global service concept
Trade facilitation services	Deregulation

In modern economies, customers want solutions to their problems rather than products and services *per se*. They demand products and services integrated into performing systems offering specific benefits.[6] The very concept of 'efficiency' is subject to change. Yesterday's efficiency was predominantly about lower costs, improved quality of labour and optimal organization. Today's efficiency is increasingly customer oriented. It is about optimal use, customers' value chain and environment. Service activities such as research and development (R&D) and design, distribution, promotion, customer services, product stewardship and guarantee, insurance, and remarketing are gaining importance in exports. New patterns of comparative advantage depend not only on the cost structure of export industry, but increasingly on the performance of the industry's service base abroad, for example marketing. The ability to manage such services internationally is an increasingly critical factor of export success.

The growth of trade in services is due to the increased tradability of many services, reduced economic distance, increased demand and more scope for service standardization. In the past, the only way to supply intangibles was through direct contact between producer and consumer. The current information technology allows the 'codification' of knowledge and numerous services may be 'stored' in the form of software, stockpiled for future use or shipped abroad.[7] Telecommunications also make possible exports of 'on-line' services (services that are information intensive and amenable to long-distance delivery). Deregulation and new options for export of standardized services through franchising and other forms of international partnership further encourage trade.

Demand for services is growing fast because it is 'revenue elastic': that is, it grows more rapidly than per capita income and because services are 'central' to a modern

economy.[8] Certain services such as telecommunications, banking or financial reporting assume a strategic role and without them countries would find it impossible to foster growth and expand exports.[9]

Barriers to trade in services

The main instruments used to protect service industries are domestic regulations. They lay down conditions of investment, establishment of service operations by foreign suppliers and the terms on which those suppliers can offer services. Most favoured nation (MFN) treatment demands similar treatment for service firms from different countries. National treatment signifies that domestic regulation does not put foreign firms at a disadvantage compared with domestic companies. The most important barriers limiting access to local service markets include discriminatory treatment of foreign investments, more rigorous regulation on foreign establishment, restricted terms in conducting business and prohibitions and sales quotas.

Deregulation has begun to expose previously sheltered service sectors—such as transportation, health care, telecommunications, banking, education or postal services—to more open competition. The biggest change has been in the fast-growing service sectors such as financial industries (see the section below) or telecommunications, which in the past have seen most of the barriers to entry. More and more service sectors are likely to open up to international competition. The underlying idea of the GATS is that open markets, non-discrimination and competition in international trade in services are conducive to the wellbeing of all nations. Trade is not a zero-sum game but a way of making every nation more prosperous.

The code of conduct in international trade of services

Two viewpoints are particularly helpful in understanding the role of the GATS. The first is to regard it as a code of conduct; the second is to view it as a market. The GATS is a code of conduct because it contains a set of rules and procedures which govern the regulatory framework for trade in services. The code relies on the five basic principles of non-discrimination, reciprocity, market access, fair competition and transparency, and consists of three main elements:

1 general concepts and rules (applying to all measures affecting international service transactions;
2 sectoral rules (i.e. concepts and rules dealing with sectoral issues); and
3 specific commitments (applying to particular sectors and subsectors and listed in the schedules).

The core general concept of the GATS is the principle of non-discrimination which has two dimensions: the MFN rule and the national treatment principle (see the section below). MFN is a general obligation but its coverage is determined by a so-called negative list: it applies to all services except those listed in the schedule, that is in the list of member

country commitments. MFN exceptions are in principle to last no longer than 2005 and will be reconsidered in any forthcoming multilateral trade negotiations (MTNs). Financial services, audiovisual services and transportation (air, road and maritime) are particularly affected by the MFN exceptions. The main reasons in financial services were the reciprocity concerns *vis-à-vis* countries which allow limited access to their finan-cial service markets. Exceptions for audio-visual services were mainly motivated by cultural considerations. The sectoral coverage of national treatment is determined by a positive list which only applies to sectors listed by a country, and then only so far as existing measures are not exempted. Market-access obligations include prohibition of market-access restrictions such as limitations on the number of suppliers, value of transactions or assets, quantity of output, number of employees, type of establishment (branch versus subsidiary, for example), as well as percentage of shares or value of foreign investment.

An emerging approach of the GATS is that of harmonization of national legislation (deep integration) which is opposed to the traditional reliance on the removal of border barriers to trade (shallow integration). Deep integration may take place either through mutual recognition (a standard that is acceptable in the exporter's country is also acceptable in the importing country) or through common standards in domestic regulations. The approach is illustrated by the GATS embryonic rules on recognition of professional qualifications.

Most GATS commitments are status quo commitments, but liberalization of trade in services is to continue. Important progress has already been accomplished in the area of telecommunication and financial services, and a new series of negotiations should be held before the year 2000. The GATS members are encouraged to negotiate bilateral or plurilateral agreements on (mutual) recognition of licences, education and professional experience. Transparency is to be favoured and GATS members maintain enquiry points providing information on qualification requirements, technical standards and licensing procedures affecting trade in services. The GATS rules on restrictive business practices are weak because monopolies and oligopolies are allowed.

Scheduled commitments define the extent to which the rules of GATS apply to specific countries and sectors and the limitations to which such commitments are subjected. Scheduling of specific commitments is essentially on a sector-by-sector and mode-of-supply basis. For each of the subsectors the commitments are further listed according to the four modes of service supply. Certain commitments are *horizontal* (applicable across sectors) as in the case of commitments referring to movement of natural persons and commercial presence. Other commitments are sector specific. Commitments may also apply across all modes of supply or to a particular mode only.

Where no limitations are included for a given mode of supply, the member undertakes a commitment not to introduce any new restrictions on market access or the application of national treatment. Where limitations have been indicated, the member is obliged not to impose any other new limitations restricting the entry of foreign service providers. The term 'unbound' signifies that the member country maintains its freedom to modify the conditions of entry for foreign service providers. In the Uruguay Round, the Organization for Economic Co-operation and

Development (OECD) countries made commitments for an average of about 53% of all service sectors and developing countries for some 15%. The weighted average coverage of market-access commitments—adjusted for whether exemptions are listed and policies are bound—is above 40% for the OECD countries and above 9% for developing countries.[10]

Numerous limitations imposed by developed countries under horizontal commitments apply to the movement of natural persons. The establishment of subsidiaries by foreign service providers is generally allowed in developed countries, but certain developing countries maintain the requirement of joint ventures with domestic partners or other restrictions on investments which are largely motivated by vested interests of the local economic elite.

International trade in specific service sectors

GATS contains rules referring to specific service sectors (GATS annexes) and several sectoral agreements. For the time being, the most significant sectoral arrangements refer to telecommunication and financial services.

Telecommunication services

The global telecommunications market, worth more than $600 billion in 1997, is one of the most rapidly growing service markets. Basic telecommunication services include voice telephony, telegraph, telex, facsimile, data transmission, leased circuit services, cellular telephony, mobile data services, paging and personal communication systems, and mobile and fixed satellite systems and services.

MFN and national treatment is to be accorded to foreign service suppliers (cable or broadcast distribution of radio and TV programmes being excluded) among the GATS countries. A significant number of market-opening offers and progress in the area of regulation of state monopolies were achieved owing to the telecommunications pact which came into force in February 1998. The seventy-two countries which accepted the agreement account for about 93% of the world's telecommunications market.[11]

Financial services

Starting from March 1999, a World Trade Organization (WTO) agreement subjects a trillion-dollar trade in financial services to legally binding fair trade disciplines, encourages more than 100 countries to open up their insurance, banking and securities sectors to foreign competition, and enables them to challenge transgressors in the WTO dispute settlement system (see the section below). The world's multi-trillion-dollar market for financial services comprises about $38 trillion in international bank lending, $2.5 trillion in worldwide insurance premiums and an estimated $18 trillion in global securities assets. The WTO deal imposes disciplines on more than 95% of that market and provides for more generous licensing for the establishment of foreign financial institutions. The sectoral arrangement covers not just cross-border trade but all the ways

foreign suppliers can deliver services to a country's market, including the establishment of local branches or subsidiaries.[12]

The political economy of re-regulation in services

We turn now to a political-economy-based discussion of re-regulation affecting trade in services, trying to provide some sense of how the system might evolve and what the future challenges might be.

The nature of negotiations on trade in services

GATS is a market through which governments and their lobbyists attempt to alter the code of conduct, and to exchange liberalization commitments. Achieving liberalization for trade in services is no trivial matter and the ongoing negotiations on various service sectors continue to prove it. In most countries numerous interest groups have different preferences with respect to regulation of services trade and a compromise has to be reached to make the agreement politically acceptable. Governments come together in the GATS negotiating forum to exchange market-access commitments on a reciprocal basis. The exchanges take place in a barter market since the actors concerned have no money. This renders the negotiations a tortuous process indeed.

How does the system work? The structure of protection is the result of the interaction between the demand expressed by various pressure groups and the supply (regulation) offered by governments. Attempts to alter this equilibrium will result in opposition by those interest groups that are likely to lose from the liberalization. The losses associated with trade liberalization are usually more concentrated than the gains. This means that those facing losses have a much greater individual incentive to invest in lobbying than those that gain from trade liberalization. A reciprocal exchange of concession in a multilateral forum such as the GATS may solve this problem by confronting the losers with the domestic firms which expect to gain from greater access to foreign service markets. The negotiations on both telecommunications and financial services were successful owing to the latter option and the increasing awareness that the two sectors were of capital importance to economic development.

The negotiating process is even further complicated by the complexity and diversity of restraints to trade in services. While seeking to reduce incrementally barriers to services trade, negotiators require a focal point, in the form of some tangible and measurable variable which enables them to set objectives and assess the results of the offers of their negotiating partners. Lacking such a focal point the negotiators focused their attention on rules as is frequently the case in services.[13]

The shortcomings of the sector-by-sector approach

The sector-based definition of services in GATS reflects the preference for a sector-by-sector approach in trade negotiations. Obviously, the sector-by-sector approach towards

negotiations does not encourage rapid and worthwhile results. While intersectoral linkages may be maintained, as a matter of principle deals for particular service sectors are negotiated in separation from each other. Consequently, the framework agreement on trade in services contains only limited obligations of a generally binding nature and specific commitments tend to be applied on a sector-specific level. This signifies that numerous commitments are offered a la carte: governments schedule commitments whilst maintaining considerable regulatory discretion in sensitive areas of services regulation.

Owing to the sector-by-sector approach the bargaining process, both at the domestic and international level, is largely driven by the sector-related concerns and interests of service firms and industry associations. The balance of concessions is mainly determined on a sector level as the negotiators aim at reciprocity for each sector (such as financial services, telecommunication services or audiovisual services) rather than on a global level of the service industry as a whole. This has clear implications for the decision making and the pattern of lobbying for market access in services. Sectoral balancing of commitments limits the scope for mutually beneficial arrangements discouraging countries which are willing to contribute in one sector in exchange for market openings in another area. The sectoral approach also signifies that cross-border alliances involve producers and distributors rather than users of service inputs who are outside the sector.[14] Sectors such as financial services, telecommunications or maritime transportation are highly sensitive in numerous countries and probably more could have been accomplished if intersectoral balance of concessions were established.

Liberalization lobbies are difficult to form

The process of negotiations on trade in services may be expected to be even more difficult than in the case of manufactured goods. Services are traded less than material products. Consequently, the number and political weight of import-competing sectors may greatly exceed that of export-oriented service sectors pushing for access to export markets. This implies that trade liberalization lobbies may be more difficult to form in the case of services than in the case of material products and that leadership of the interest groups favouring liberalization is particularly needed.[15]

Furthermore, numerous service activities are highly regulated. The regulatory agencies involved may then have a vested interest in defending their turf.[16] Being close to the decision-making bodies they may exercise influence and complicate the necessary interagency co-ordination. Pro-active participation of the business community in the negotiation process is desirable to limit that risk.

Liberalization of those service sectors which do not require establishment (commercial presence abroad) as a primary mode of delivery may be discouraged by the government's mistrust of firms that operate from a foreign base. Indeed, regulators are likely to find it more difficult to control service providers located in foreign jurisdictions and have greater objection to liberalization that is not linked to establishment. Trade liberalization will be easier to achieve for those services for

which establishment constitutes the most efficient mode of exporting also because sector-specific labour interests may accept the establishment of foreign-owned firms in so far as they expect that net employment in the sector will not be affected.[17]

As far as the non-establishment modes of supply are concerned, the number and political weight of import-competing service activities seems to exceed that of export-oriented activities. However, the situation is likely to change with an increased tradability of numerous services resulting from new technologies (e.g. 'on-line' services), lower costs of flows (e.g. lower transportation costs) and greater cost pressures in the high-income countries. It is important that service lobbyists of that type of industry remain particularly active in pushing for market access. There is evidence to suggest that those leading service firms and industry associations that engaged in lobbying gained better market access as the result of the Uruguay Round negotiations.[18] Service firms should become more pro-active in shaping policy making affecting trade in services.

The case of negotiations on financial services

The WTO deal on financial services is an interesting illustration of how the multilateral mechanics of trade liberalization and deregulation work in the area of services. There is a generalized feeling in the world business community that the national regulatory system for financial services became obsolete owing to technological change, mutation in the nature of trade and rapid innovation of financial instruments. The growing integration between banking, securities and insurance opened up new opportunities for coalition building in support of liberal policies and globalization created new scope for a geography-free community of interests. But, since the issues remained controversial and loaded with highly ideological and emotional contents, the multilateral negotiations were never easy.

In numerous developing and transition economies liberalization is hampered by the nationalistic sentiment that open markets for financial services signify selling out heritage to foreign banks. The fact that low-income countries tend to be demanders of financial services, with exports concentrated mainly in advanced economies, further reinforces the nationalistic bias. Neither is liberalization well served by the involvement of government departments (such as some ministries of finance) which do not share the free trade orientation of trade ministries. The departments concerned sometimes encourage protectionist stands by appealing to public fears of looser controls over banks or the loss of national sovereignty over exchange policies—issues particularly sensitive during the 1997–8 Asian financial crises.

The initiative for a WTO deal on financial services originated in the US financial sector which acted as a visionary at the catalyst stage of the multilateral negotiations. The US administration which maintained close working relationships with its financial industry was able to define in broad terms the issues to be negotiated upon and place constraints on the parameters of the formal negotiations that followed. Washington wanted either a good deal or no deal at all. It considered that the existing system of bilateral agreements worked reasonably well and that a multilateral deal should provide value added in order to be attractive. It also felt that since, in most countries,

financial sectors were not distorted by monopolies or subsidies (as distinguished from telecommunication services), an agreement in that area was less urgent if no significant progress could be made.

The US financial industry and administration have proven instrumental in building an international coalition in favour of a WTO arrangement with major support coming from constituencies in the European Union, Japan and even low-income countries. The motto 'don't just stay ahead of the game, make the rules' motivated financial institutions from the advanced economies, but also from Brazil, Malaysia and India, to play a more active role in WTO horse trading.

The support for a liberal arrangement came not only from the most competitive providers of financial services which hoped for new export markets, but also from the users of services. Indeed, there was a growing conviction that banking, insurance or financial reporting were strategic for economic development. In particular the users of financial services in developing and transition economies considered that a key part of the development effort required replacing antiquated financial institutions with a market-oriented financial system. They realized that banking was more 'strategic' than, say, car production or growing another 1000 tons of wheat. When things go wrong, cars and wheat—meaning manufactured products and commodities—can be imported. However, no modern economic system may operate with inefficient financial institutions. That stand was reinforced by the necessity to look for additional financial sources on international markets, which made a further integration of national financial sectors into international networks even more desirable.

The WTO negotiations were also supported by the dynamics of the regional arrangement in that area of financial services. For example, the European Union (EU) members or the potential EU members in Central and Eastern Europe realized that their policies with respect to financial services had to be liberalized anyway in the context of European integration which made the acceptance of multilateral commitments easier. Dealing with the protectionist lobbies within the labour movement was largely facilitated by the fact that the bulk of the industry exports relied on foreign direct investments rather than cross-border transactions and created little risk for employment. The WTO negotiators benefited from a favourable political momentum for rapid progress in the area since the political masters expected a deal to be concluded after years and months of bargaining and delays.

The hard-core negotiations on financial services were essentially bilateral, with the United States and the EU being the driving forces. In the bilateral negotiations numerous countries, including Japan and the emerging economies of Asia, submitted substantial offers to make the deal acceptable to Washington. The success of the WTO deal on financial services was also due to the creativity of those involved in the negotiating process. The WTO negotiations on financial services provide an example of 'problem-solving' negotiations which are signifi-cantly different from distributive bargaining. The financial services negotiators approached the negotiations as a process in which issues were to be solved. They commonly identified issues for which an agreement was feasible, proposed competing solutions, established preference orderings for the solutions considered and searched for the final deal. Whereas

distributive bargaining might call for bluffs, threats, manipulation of information and minimally honest behaviour, 'problem-solving' negotiations on financial services required a high level of trust, openness and intellectual input. The culture of such WTO negotiations and the attitudes and behaviour of their participants are thus substantially different from making a deal in the commercial sphere.

Modern economies are service economies and international trade in services is likely to expand rapidly owing to deregulation, trade liberalization and technological change. Numerous services, such as financial services or telecommunications, assume a strategic role in the global economy because they are the economy's 'nervous system' and a growing number of interest groups dependent on them favour liberalization. International service transactions are expected to receive a further boost in the coming decade as the WTO progressively implements a rule-based world trading system for services (GATS) and encourages further liberalization and deregulation. Owing to the multifaceted nature of trade in services, new issues such as investment, competition and labour standards are likely to gain importance in the WTO negotiations.

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Chapter 5
Intellectual property

Ann Capling

One of the most astonishing outcomes of the Uruguay Round was the inclusion of a new multilateral code governing trade-related aspects of intellectual property, the so-called TRIPs agreement. Certainly the US negotiators who spearheaded the drive to include intellectual property within the auspices of the General Agreement on Tariffs and Trade (GATT) had not anticipated the scope and nature of the final TRIPs agreement. Unlike the GATT itself which prescribes a set of rules and norms for trade in goods which each Contracting Party is free to implement in its domestic laws as it sees fit, the new TRIPs agreement actually requires members of the World Trade Organization (WTO) to harmonize their legal and regulatory systems in matters concerning intellectual property rights. This represents a far greater incursion on national sovereignty than has ever been the case in past multilateral trade negotiations. In that sense, it will be a real test of the future capacity of the WTO to maintain the 'compromise of embedded liberalism' which has been a strength of the multilateral trade system since 1947.[1] Moreover, the theoretical rationale for the new TRIPs regime is very shaky and its inclusion represents the triumph of powerful economic interests rather than the measured consideration of costs and benefits within the global trade system. Indeed, as this chapter will demonstrate, the debate over intellectual property rights is characterized by competing normative positions, few of which are grounded in either economic theory or empirically demonstrable outcomes. As a result, it is possible that the new TRIPs regime will simply enhance the economic benefits accruing to the holders of intellectual property rights while imposing new and greater economic and social costs for many others.

What are intellectual property rights?

Intellectual property is a somewhat abstract concept which encompasses ideas and images, sounds and symbols, words and music, text and designs, formulae and blueprints. The rationale for intellectual property rights is that most forms of intellectual property have the characteristics of a public good—that is, their use cannot be limited to those who incur the initial cost of its creation. Without a way to prevent 'free-riding' (the unauthorized or uncompensated use of intellectual property), there would be no economic incentive for individuals to create intellectual property. This is the 'market failure' argument for intellectual property rights which sees the creation of intellectual property as purely the outcome of material, instrumental and rational self-interest.

Without reward, there would be no incentive to create intellectual property. Moreover, society would suffer from the loss of benefits derived from the creation of intellectual property, whether that be films or computer software or drugs. This reward/incentive argument is typically used by pharmaceutical companies which claim that they would not develop new drugs if other companies could simply copy the formula and sell an identical product at a lower price, without having incurred the initial research and development costs. Hence the use of patent protection which gives drug companies exclusive control over their new drugs for a set period of time, during which they can recoup the millions of dollars invested in the initial costs of research, development, conducting trials and marketing.

There are many forms of intellectual property rights which can be divided into two main categories: industrial property rights and copyright.[2] Industrial property including novel ideas, inventions, ornamental designs on functional objects, packaging, emblems and logos are protected by *patents, trademarks* and *registered designs.* Literary, artistic and musical works are protected by *copyright.* Unlike industrial property rights which protect ideas, copyright protects only the concrete expression of an idea, as might be embodied in a film, a compact disc, a book or a photograph. All intellectual property rights (IPRs) give the holder of the right control over the use of the product. In effect this is a monopoly right which enables the person or firm which holds the IPRs to determine the distribution and price of the product.[3] All of these rights can be sold, traded or licensed in return for royalties being paid to the holder of the right.

IPRs have traditionally been the domain of national legislation. Because of the monopoly nature of IPRs, considerations of social welfare and the public interest must be balanced against the private monopoly which is bestowed by the IPRs of the property holder. For instance, pharmaceutical companies might be tempted to profiteer from their exclusive rights to manufacture and distribute a new life-saving drug. For that reason, governments limit the monopoly power of drug patents by setting expiration dates on a patent, or by creating a competitive market through compulsory licensing requirements, or by not recognizing patent rights at all.[4] The wide variations in national regimes for IPRs depend on many factors including, most obviously, a nation's economic and industrial structure, its national development objectives, and its comparative advantage in trade. Generally speaking this has meant that IPRs have been weaker in poorer nations which have been unwilling or unable to underwrite the high cost of patent-protected drugs, chemicals and technology, and in nations which are imitators rather than innovators of technology. As Trebilcock and Howse note:

> A country where innovation is not a major source of economic activity and growth is likely to choose, on balance, a less stringent intellectual property regime than would a country whose economy is highly dependent on innovation. From this perspective, there is nothing suspect or unreasonable with the preference of many developing countries for a relatively lax system of intellectual property rights.[5]

Cultural and legal traditions also influence a nation's regime for IPRs. For instance, nations which are not heir to a Western European or British legal tradition which asserted the primacy of private individual rights over public collective rights are less likely to have a strong system to protect intellectual property. Moreover, the registration and enforcement of IPRs is a resource-intensive administrative activity which requires high levels of technical and legal expertise. In that sense, the willingness of national governments to recognize and enforce IPRs depends to a great degree on the administrative capacity and sophistication of the state and the judicial system.

Finally, differences in national systems to protect intellectual property can also be attributed to the relative strength of domestic interest groups. Thus in many countries, copyright support for literary, artistic and musical works, film and software tends to be stronger than patent protection for industrial property and technology. This is likely due to domestic pressure from associations representing writers, artists, musicians and film makers. In India for instance, home to the world's biggest film industry and a highly competitive computer software industry, copyright protection is quite strong. On the other hand, as a net importer of technology, India's patent protection has traditionally been quite weak. A similar example relates to the United States. Now the international champion of strong IPRs, the United States had until recently a notoriously slack regime for the protection of copyright. American publishers freely reproduced and sold books by foreign authors without paying royalties to either the authors or their foreign publishers. In addition, US law prevented the import of English language literary material, written by an American citizen or resident, which was not manufactured in the United States or Canada. This weak copyright protection was motivated by the desire to protect the American publishing industry against competition from cheaper imported books.[6]

Although IPRs remained within the realm of national legal systems, since the late nineteenth century there have been concerted moves by national governments to create legal and institutional frameworks to foster international recognition of IPRs. Since then, several international agreements have been established which create international disciplines for the protection of intellectual property. These include the Paris Convention for the Protection of Industrial Property (1883) which protects patents and trademarks, the Berne Convention for the Protection of Literary and Artistic Works (1886), the Universal Copyright Convention of 1952 (UCC), and the Rome Convention for the Protection of Performers, Producers of Phonograms and Broadcasting Organisations (1961). With the exception of the UCC, which is administered by the United Nations Educational, Scientific and Cultural Organization (UNESCO), these agreements are administered by the World Intellectual Property Organization (WIPO). Established in 1967, WIPO has been a specialized agency of the United Nations since 1974. Signatories to any of these conventions are required to accord *national treatment,* that is the same legal protections and remedies to foreigners as to their own nationals in matters concerning IPRs. However, membership in these conventions is voluntary and as a result coverage has been quite uneven. Moreover, the conventions do not require signatories to harmonize their IPRs at a particular benchmark level, and each member country is allowed to determine its own level of

protection and its own enforcement mechanisms.[7] Of course it was this 'relatively loose international' system which made it possible for the rich industrialized nations like the United States and Japan to achieve parity with those on the cutting edge of a particular technology.[8] Indeed at least part of Japan's economic 'miracle' was due to its ability to imitate and then improve upon American innovations.

IPRs on the international trade agenda

The establishment of WIPO was an important step in the development of a framework for international co-operation on IPRs. However, in addition to the problem of uneven coverage, there was no scope within WIPO or its individual conventions to consider trade-related aspects of intellectual property, an issue of increasing importance to the world's leading exporters of intellectual property, especially in the United States and Western Europe. During the 1970s, the manufacturers of luxury items such as expensive watches and designer apparel were concerned about the manufacture of cheap counterfeits, largely in South-East Asian countries which had few domestic laws to prevent such activities. Pirated cassette tapes and videos were also a problem. This led to US attempts during the Tokyo Round of multilateral trade negotiations (1973–9) to have IPRs strengthened within the GATT, especially in the area of counterfeit goods. But these efforts failed, largely because of the opposition of many of the developing countries which argued that intellectual property issues did not properly belong within the purview of the GATT. From their perspective, WIPO was a UN agency and was perceived to be more open and sympathetic to the perspective of developing nations than the GATT, an institution which tended to privilege the trade interests of the rich industrialized countries, usually to the detriment of the poorer nations.[9] In addition, WIPO already had a considerable track record in providing financial and technical assistance to nations which wished to develop their own intellectual property regimes. But from the American perspective, WIPO was neither an adequate nor an appropriate vehicle to secure the IPRs of US interests.

By the early 1980s, intellectual property had become a trade issue of considerable importance to many rich industrialized countries. As these nations began to lose older, labour-intensive manufacturing to the newly industrializing countries, they sought to locate their future trade competitiveness in technological innovation and research-intensive activities. Areas targeted for growth included pharmaceuticals, chemicals, microelectronics, telecommunications and information technology, biotechnology, medical and scientific instruments, entertainment products such as videos and CDs, and high-value-added luxury items such as wine, fashion apparel and perfume.

Just as the impetus to include trade in services in the Uruguay Round agenda came almost entirely from the US government acting on behalf of American corporations, so too did the push for matters relating to trade in intellectual property. Indeed, this was an area where powerful domestic industry interests had been very active in the lead-up to the Round.[10] At the forefront of lobbying efforts were the pharmaceutical, information technology, entertainment and clothing industries which commissioned

dozens of reports to demonstrate how American firms lost billions of dollars a year owing to infringements and inadequate protection of intellectual property. One study by the US International Trade Commission claimed that in 1982 alone, 131,000 American jobs were lost due to foreign counterfeiting of American consumer and industrial goods. Other studies claimed that violations of IPR cost American industry from between $30 to $60 billion each year.[11] Figures of this magnitude spurred the US government to adopt aggressive action to secure improved protection for the IPR of American industry. As in other areas of its trade policy, the US government adopted a three-pronged approach of unilateral, bilateral and multilateral initiatives to pursue its agenda on IPRs.

Unilateral and bilateral initiatives

In the area of unilateral action, the US government already had recourse to Section 337 of the US Tariff Act of 1930 which allows the seizure of any imports which are alleged to contravene US intellectual property laws. Scope for unilateral measures was considerably enhanced with the passage of Section 301 of the Trade Act of 1974 which allowed the US administration to take action against other countries deemed to have inadequate IPRs, regardless of whether imports to the United States were involved. This was further strengthened with the passage of the Trade and Tariff Act of 1984 which gave the US President the right to withdraw preferential tariffs or impose punitive tariffs on any goods imported from countries which, in the view of the United States, had inadequate IPR regimes. Under this law, punitive action was taken against Brazil, Mexico, the Republic of Korea and Taiwan. In 1988 the unilateral thrust of US trade legislation was extended with the Omnibus Trade and Competitiveness Act. In particular, the notorious 'Special 301' section requires the US Trade Representative (USTR) to identify all nations which have intellectual property regimes which are objectionable to US trade interests. Unilateral trade sanctions may follow as a consequence and this threat has been used to extract policy concessions from target countries. These have included the usual targets such as Brazil, India and Japan, but other nations such as Australia, Canada, Norway and Spain have also been placed on the USTR's 'priority watch list'.

In addition to these acts of 'aggressive unilateralism', the United States also undertook a variety of bilateral initiatives to secure the IPRs of American exporters and foreign investors.[12] In the late 1980s, it completed bilateral agreements with Japan and the EU which provided copyright-style protection for semiconductor chips. It is worth noting that these unilateral and bilateral actions were not aimed at promoting a new international multilateral regime for the protection of intellectual property. Indeed, the general effect of these initiatives was to distort international trade further in a way that favoured the United States over its competitors. For instance, Korea responded to US pressure not by improving its system of IPRs, but by granting protection to American technology, while denying that same protection to others.[13]

Multilateral initiatives: the Uruguay Round

The inclusion of IPR in the Uruguay Round agenda came very late, practically on the eve of the meeting at Punta del Este which launched the Round in 1986. In fact, the US government was divided over the wisdom of trying to include IPR in the new round, which was already overloaded with serious and longstanding issues such as agriculture and textiles, as well as the contentious new issue of trade in services. Moreover, intellectual property experts were reluctant to support a 'change in policy venue' from the WIPO to the GATT. There was also debate over whether it would be better to pursue IPRs through the negotiations to liberalize trade-related investment (TRIMs). For instance, as part of the TRIMs negotiations, countries might agree to strengthen their protection of intellectual property, thus enabling American companies to undertake foreign investment knowing that their patent rights in these markets would be secure. Despite the differences of approach, the growing importance of intellectual property in international trade and investment could not be ignored. When the Chairman of IBM came out in favour of pursuing the IPR issue in the GATT, the the was cast in favour of pursuing a multilateral discipline to strengthen IPR.[14]

Prior to the Uruguay Round, there were few GATT rules concerning trade in intellectual property. Articles IX and XX recognized the right of contracting parties to prevent imports of counterfeit goods, but GATT rules did not establish a clear set of binding IPR. In effect, the TRIPs negotiations were beginning from a blank slate and, as such, the negotiating mandate established at the beginning of the Uruguay Round was both broad and general. Specifically, the TRIPs negotiators were required to consider 'the need to promote effective and adequate protection of intellectual property rights' in order to reduce distortions and obstacles to international trade.[15]

From the outset, there were deep divisions within the TRIPs negotiating group. In one corner was the United States, which was pushing for a new and comprehensive agreement on intellectual property. Such an agreement would establish minimum standards for the protection and enforcement of a wide variety of IPRs including patents, trademarks, trade secrets, semiconductor layouts and copyright. In effect, the United States wanted all other GATT members to raise their levels of intellectual property protection up to American levels. In addition the US proposal included provisions for a dispute settlement mechanism and strong penalties including 'cross-retaliation' (the withdrawal of other GATT trade benefits) for GATT members which violated or failed to live up to any aspect of a new agreement. The US position was supported with varying degrees of enthusiasm by other members of the OECD (Organization for Economic Co-operation and Development) club of rich nations. The strongest support came from the EU and Japan, where powerful domestic lobbies, working in collaboration with the intellectual property lobby in the United States, pressured their governments to take a strong stand on TRIPs.

In the other corner were the G-10 countries, a group of influential non-OECD nations led by Argentina, Brazil, Egypt and India. This group was willing to negotiate a stronger GATT discipline to prohibit trade in counterfeit goods, something which the United States had pushed for during the 1970s. However, these nations objected

to any broader discussion of intellectual property along the lines sought by the United States, the EU and Japan, and they believed that any discussion of IPRs was properly the domain of the WIPO, not the GATT. Indeed, Brazil and India argued that IPRs were by their very nature trade restricting and anti-competitive, the implication being that they violated the fundamental rules and norms of the GATT. If that claim sounds capricious, it is worth considering their objections in some detail.

The case against strengthening IPRs

The main objections to strengthening intellectual property protection are based on pragmatism and principle. There are social and economic dimensions to these arguments as well. For instance, many nations have traditionally given little or no patent protection to pharmaceuticals on the grounds that patent protection for drugs will inflate prices to a level beyond the reach of many of their citizens. Argentina, Brazil, India, Mexico, the Republic of Korea and Taiwan are all examples of countries which have used lax or non-existent patent protection to promote competition in their domestic markets for pharmaceuticals in order to keep prices low. In addition to the social welfare rationale for this practice, there are also ethical arguments. For instance, in 1982 Indian Prime Minister Indira Ghandi argued that: 'The idea of a better-ordered world is one in which medical discoveries will be free of patents and there will be no profiteering from life and death.'[16] While this sort of public good argument has been associated with the so-called developing countries, it is hardly their exclusive preserve. Until recently, Italy had no patent protection at all on drugs, while Canada had compulsory licensing laws which forced competition on the pharmaceutical companies before patent protection expired.

Another argument against IPRs pertains to issue of technology transfer. Patent owners may place onerous conditions on the use of new technology, or may simply refuse to license new technology at all in order to preserve their monopolistic position. In this way, instead of promoting innovation (the market failure argument for intellectual property protection), patents can actually slow the dissemination of new ideas, basic knowledge and technological advancement. This has been a long-standing area of concern for importers of technology, especially for industrializing countries which have found their development objectives thwarted by the restrictive practices of foreign investors.[17] As a result, many newly industrializing countries developed trade and investment policies which offer little or no patent protection to foreign-owned companies which seek to produce or sell pharmaceuticals, computer hardware and software, and other technologies. Brazil is frequently cited as being especially 'aggressive in using discriminatory intellectual property laws' to promote its own technological development.[18] This aroused the ire of the United States and, as a result, Brazil became the target of US sanctions during the 1980s.

A related argument asserts that contrary to claims that IPRs are necessary to promote research, in fact they can inhibit research and the diffusion of knowedge. For instance, patents and copyright can act as barriers to the sharing of information and research. In the late 1970s, inventors engaged in trying to develop personal computers openly shared and exchanged information on a regular basis. Once it

became possible to commercialize these ideas and designs, information sharing gave way to secrecy. This led to costly duplication of research and other suboptimal outcomes. For instance, intellectual property laws prevented software designers from infringing the copyright of other designers; hence the proliferation of different key strokes required to execute a simple 'exit' command, depending on the program or operating system. In this way, copyright laws prevented software designers from creating universal standards. As Branscomb notes, this 'often frustrates users, requires programmers unnecessarily to reinvent the wheel, places higher development costs on funding sources, and inhibits the compatibility which encourages a competitive market place'.[19]

Another area of considerable concern, especially to South American and African countries, was the debate about the patentability of biological life. Traditionally biological processes and products have not been included in the domain of IPRs. However, as the global leader in the development of biotechnology, the United States (along with Japan and Switzerland) was keen to secure patent protection for processes and products involving genetic manipulation. This raised the spectre of foreign corporations raiding the forests and jungles of the poor nations in order to 'discover' and patent the genetic material of indigenous flora and fauna. Apart from any ethical considerations, such activities would greatly undermine national sovereignty over territory and resources.[20] Farmers in poor agricultural countries also feared this would mean that they would be forced to pay royalties on the seeds of their plants and the offspring of their animals.[21]

The TRIPs negotiations

Much of the academic literature depicts the TRIPs negotiations as a battle between 'developed' and 'developing' countries, the 'industrial countries' versus the 'Third World', the 'North' versus the 'South'. However, apart from the semantic problems[22] with these descriptions, these dichotomies tend to gloss over some of the fundamental difficulties and issues at stake. To be sure, the most vociferous opponents of a strong and comprehensive TRIPs agreement were nations from Latin America, Africa and the Indian subcontinent.[23] In that sense, it would be much more accurate to characterize the divide in the TRIPs negotiations as one which pitted OECD countries against the rest. However, as the negotiations proceeded, cracks and fissures emerged within both groups. Some newly industrializing countries (Mexico, South Korea, Singapore, Malaysia and Thailand) began to distance themselves from the G-10 nations. This was partly due to unilateral pressure from the United States but also in recognition that future foreign investment in their own high-technology sectors depended on improved levels of patent and copyright protection. But even among the OECD nations, as the negotiations moved from broad statements of principle to more specific concerns, sharp differences began to emerge.

The issues which divided the OECD nations concerned patent protection and copyright. The length of patent protection, especially for pharmaceuticals, was a long-standing issue which had often united rich and poor nations against the powerful drug companies in the United States and Western Europe.[24] Now the United States and the

EU were seeking the extension of protection on all patentable products and processes to a minimum of twenty years in all countries. For some OECD countries, this would mean extending the length of their existing patent protection. For many developing countries this would mean granting patent protection where none had previously existed. Together these countries advocated a compromise proposal which would see patents expire after fifteen years (and twenty for drugs).

The other patent issue concerned US discrimination against foreign patent seekers. In the United States patents are awarded to the 'first to invent', whereas in the rest of the world, patent protection is granted on a 'first-to-file' basis. The effect of the 'first-to-invent' rule was to create a US patent system which discriminates against foreigners and in favour of American nationals. This is because US courts will not accept overseas evidence concerning the date of invention. In order to end this discrimination, all nations apart from the United States were seeking to negotiate an obligation that patents would be available without discrimination as to where the inventions were first made.

The other areas of dispute related to copyright issues: neighbouring rights, rental rights, moral rights and parallel importation. Again, these issues tended to pit the United States against most other countries. Long before the Uruguay Round began, there was considerable ill-feeling against the United States because of its long-standing refusal to accede to the Berne Convention and because of its *de facto* withdrawal from the UCC which occurred when the United States dropped out of UNESCO in the early 1980s.[25] Concerning many important copyright issues, there were points of fundamental disagreement between the United States and other countries. One issue was neighbouring rights, which refers to the rights of producers, performers and broadcasting organizations to initiate action against pirates. These rights were strongly supported by Japan, the EU, Switzerland, the Nordic countries and Australia but not the United States. Another area concerned rental rights, which refers to a right by copyright owners to collect extra royalties to cover the possibility that their computer program, film or CD might be copied. In essence, the United States wanted the recognition of rental rights which would effectively prohibit the commercial rental of copyright material such as cassette tapes and CDs. Again, this was opposed by Japan, Australia and other countries which allowed consumers to tape rented music recordings for their own personal use. The issue of moral rights also separated the United States from other countries. Unlike every other form of IPRs, moral rights do not involve issues of financial compensation. Instead, they refer to the creator's right to preserve the integrity of the original work. The United States opposed moral rights on the ground that they are not an 'economic right' and therefore had no place in the TRIPs agreement.

IPRs and the threat to national cultures

Another contentious area was the issue of parallel importation, particularly with respect to books and music recordings. This is worth exploring in some detail because it demonstrates how IPRs are not just an economic issue but a cultural one as well. A brief

case study of popular music in Australia provides an illustration. The popular music industry worldwide is dominated by five corporations the 'majors'—which control at least 70% of the global market for music.[26] Here 'control' means both production and international distribution. This is because copyright law in Australia prevents parallel importation—the import of copyright material by anyone other than copyright owners.[27] For instance, if Sony chooses not to release one of its CDs in Australia, the ban on parallel importation makes it illegal for any retailer in Australia to import that CD in commercial quantities. In effect, the majors have import monopoly rights which allow them to determine what CDs they will release in Australia. This import monopoly also ensures that the majors control the distribution system within Australia. As a consequence, both the availability and the price of most CDs sold in Australia are determined under monopolistic conditions.

It can be argued that the exclusive import rights of the majors undermine Australia's distinctive national culture. Because profits are generated by volume sales —30% of their revenue is typically generated by their top five sellers—the majors release only what they expect will be big sellers. In Australia, this amounts to only about 20% of the music that the majors produce and control worldwide. This accounts for the prevalence of music 'mega-stores' which have about as much cultural diversity as a chain of hamburger restaurants. Moreover, this is the music heard on commercial radio stations which play only what the majors make available to them. Less 'mainstream' music, such as classical, jazz, blues, ambient, indigenous, folk and children's music, is rarely broadcast, except on the government-funded and public radio networks. This alternative music is also difficult to find in record stores, especially for people living outside major urban centres. In effect, the import monopoly of the majors serves to undermine cultural diversity and facilitates homogenized international culture.

The import monopoly also makes it difficult for Australian performers and composers to get airplay in Australia. Pop and rock music account for close to 90% of the Australian CD market, but with the exception of a handful of Australian acts which have won an international following, this market is overwhelmingly dominated by North American and British artists. Since they are in business to make money, the majors have no desire to promote Australian acts which are unlikely to become internationally profitable. As a result, music by Australian performers is marginalized by the domination of the majors.[28] In this way, the ban on parallel importing also works against the development and promotion of Australian talent, and thus undermines Australian popular and local culture.

There is little doubt that this particular aspect of copyright facilitates the globalization of a mass culture of commercialized mediocrity. In the face of such pressures, governments have taken various measures in an attempt to promote local culture. Nevertheless, in recent years such measures have come under attack from US government agencies acting on behalf of the powerful entertainment corporations. For instance, Australia has local content rules to promote local music and programming on radio and television. However, the US government is opposed to these rules, and in the future Australia will be pressured to abolish them.[29] Moreover, in 1992 when

the Australian government considered the introduction of parallel importation for music recordings, the US government registered its strong objections. Australia remained on the USTR's 'priority watch list' until 1995 when the government decided not to allow parallel importation. In 1997 when the Australian government again proposed legislation to allow parallel importation, the USTR cited its concern about this develop-ment.[30] This suggests the desire of US trading interests to preserve not just market share, but cultural hegemony.

The TRIPs agreement

The previous section demonstrates that the issue of intellectual property was not simply one which pitted the 'developed' countries against the 'developing' countries. In fact, no country supported the radical US proposals on intellectual property protection, not even the EU or Japan. For that reason, it is all the more astonishing that such a comprehensive TRIPs agreement was concluded. The key aspects of the final agreement include the extension of basic GATT norms and principles. This meant that all WTO members had to afford the same level of protection to foreigners accorded to nationals (national treatment); members had to accord the same legal protections to all other WTO members on a non-discriminatory basis (most favoured nation); and members were required to notify the TRIPs Council of their domestic laws and regulations concerning intellectual property, and respond to requests for information from the Council and other members (transparency). The agreement also establishes minimum standards of protection which, in effect, will lead to the globalization of US laws governing intellectual property. The TRIPs agreement also requires all WTO members to establish mechanisms for the domestic enforcement of IPRs. Trebilcock and Howse contend that this 'constitute [s] a largely unprecedented degree of control by an international regime over domestic civil and administrative procedures'.[31] Finally, the WTO's new dispute settlement mechanisms apply to disputes over trade-related aspects of intellectual property.

The TRIPs agreement was weighted heavily in favour of American interests. Issues of concern to other OECD countries (moral rights, rental rights, neighbouring rights and parallel importation) were either resolved largely in favour of the United States, or held over for future negotiations. A few concessions were included for developing countries. For instance, developing countries were given five years to comply with the TRIPs agreement. And to the dismay of pharmaceutical companies, this phase-in period was extended to ten years in the case of drugs. Plants and animals were excluded from patentability, largely due to the EU's opposition. But the patentability of plant varieties was affirmed and the patentability of life is bound to be a future issue in IPR negotiations. Finally, least developed countries were exempted entirely from the TRIPs agreement.[32]

In the end, the TRIPs negotiations proved to be less contentious than some of the other areas of the Uruguay Round such as trade in services, trade-related investment measures, subsidies and agriculture. There are a few reasons why this 'new' issue was more easily concluded. First, there was the potential in multilateral trade negotiations for 'linkages' which had never been possible in the WIPO. During the Uruguay

Round, countries which otherwise had very little economic or political leverage could make their co-operation in one area of negotiations dependent on progress in another. For instance, the developing countries were able to secure some of their trade objectives in contentious areas such as textiles and agriculture in return for their acquiescence to the TRIPs agreement. The same was true for countries like Australia and Canada which were willing to support a TRIPs agreement as a trade-off for obtaining the reduction of agricultural protectionism and subsidies that were highly damaging to their own export interests.[33] In that sense, one positive outcome from the inclusion of intellectual property rights in the Uruguay Round was that it became more difficult for the United States and the EU to wiggle out of making commitments in regard to the liberalization of trade in textiles and agriculture.

More than just linkages though, many industrializing countries were moving towards a less hostile and decidedly more welcoming view of foreign investment. Whether this was due to an ideological shift among governing elites is open to debate. But there were certainly strong pressures on these governments to liberalize their investment and trade restrictions in the global competition to attract foreign investment.[34] In this context, domestic pressure for intellectual property law reform have tended to come from two different sources. First there are foreign-owned companies dealing in intellectual property whose profitability is undermined by inadequate IPRs. Their influence would have increased as governments began to place increasing value on foreign investment. The other source of pressure came from exporters who feared retaliation from the United States as punishment for their inadequate intellectual property laws. In particular, export interests in Brazil, Mexico, South Korea, Singapore and Taiwan lobbied their governments to strengthen their intellectual property laws.[35]

Finally, as in other areas of trade, most countries are of the view that it is preferable to have multilateral regimes in trade, however flawed they are, than to be on the receiving end of US unilateral actions. This is as true of the other OECD nations as it is of developing countries. No doubt the desire to restrain US unilateralism was an important factor in the achievement of the TRIPs agreement.

Problems

Like the GATT, which had been of great benefit to the exporters of manufactured goods, the TRIPs agreement will bestow great benefits on the exporters of intellectual property. But in the same way that the GATT has been less able to promote the interests of agricultural exporters and developing countries, it is likely the TRIPs agreement will be less accommodating of the needs of developing countries and other industrial countries which are net importers of intellectual property.[36] In the immediate future, countries which are attempting to comply with the TRIPs agreement are likely to encounter many adjustment problems. While there may well be future benefits in terms of enhanced investment and export opportunities, in the short term many nations will be worse off. It is not a case of these governments, firms and consumers now being forced to pay the 'market' price for drugs, food, books and technology. Rather, these groups will now be

forced to pay the monopoly price. In particular, developing countries will be much worse off as wealth is transferred from their consumers to 'capital-exporters, technology-leaders and service-providers'.[37] This is a striking asymmetry, or in the words of Jagdish Bhagwati, a zero-sum game 'with the majority of developing countries losing and many developed countries gaining, according to most impartial observers among the economists'.[38] In addition, many countries are bound to encounter high costs and great difficulties in developing their legal and administrative systems to the point that they meet their new obligations. As Sylvia Ostry notes: 'Compliance with these extremely detailed obligations will be very demanding for countries with legal systems or traditions that differ significantly from the American model'.[39]

As implied throughout this chapter, any theoretical justifications for IPRs are interest driven and certainly open to debate. Far from being a strictly individual and instrumental activity, the creation of intellectual property is almost always a highly social act. As Trebilcock and Howse pithily observe:

> Society provides the context in which creative activity takes place—few inventions or works of art or literature spring fully grown from the inventor's head. They usually depend on education within society, and build on the work of many others.[40]

This understanding of intellectual property is common among many indigenous cultures which view intellectual 'property' as belonging to the community, not to an individual. In this sense, the notion of intellectual property being a 'private right' is problematic. Moreover, the economic rationale for IPRs remains underdeveloped and their inclusion in the Uruguay Round represented a significant triumph for powerful corporations from rich countries.[41] And unlike GATT negotiations, the norms of reciprocity and mutual advantage were nowhere to be seen in the TRIPs negotiations. Indeed, concerning IPRs, it was much more a case of 'Just Do It'.

Notes

1 This refers to the capacity of the international economic institutions which shaped the postwar reconstruction to balance the domestic responsibilities of nation states against the need to promote a liberal international economic system. See, for instance, John G.Ruggie, 'International regimes, transactions, and change: embedded liberalism in the postwar economic order', in Stephen D.Krasner (ed.), *International Regimes* (Ithaca, NY: Cornell University Press, 1983).

2 Other forms of intellectual property rights include *integrated circuits* which protect semiconductor chips, *plant breeders' rights* which protect some biotechnological processes and products, *moral rights* which assert a creator's right to have some control over the use of his or her artistic, musical or literary work, and *trade secrets*.

3 It should be noted that intellectual property rights do not necessarily belong to the original creator of intellectual property, but rather to the entity which has produced the concrete expression of that property. For instance, a technological breakthrough achieved by a

university research team is patented by the university, not the team. It is the publisher of a book, not the author, which holds the copyright. The copyright for a compact disc (CD) recording rests with the record company which produced the disc, not with the musicians who performed the music, nor the composer and lyricist who wrote the songs, nor the company which manufactured the plastic CD itself.

4 The terms and conditions of patents are highly nuanced from state to state. For instance, Europe grants stronger patent protection when a significant 'step up' in technology is involved while the United States makes no such distinction.

5 Michael J.Trebilcock and Robert Howse, *The Regulation of International Trade* (London and New York: Routledge, 1995), p. 251. The same point has been forcefully made by Alan V Deardorff, 'Should patent protection be extended to all developing countries?', *World Economy* 13, 1990, pp. 497–508.

6 Robert P.Benko, *Protecting Intellectual Property Rights* (Washington, DC: The American Enterprise Institute for Public Policy Research, 1987), pp. 6–7.

7 On 1 January 1995 when the TRIPs agreement came into formal legal existence, the Paris Convention had 134 members, the Berne Convention had 114 members and the Rome Convention had only 48 member nations.

8 F.S.Ringo, 'The trade-related aspects of Intellectual Property Rights Agreement in the GATT and legal implications for Sub-Sahara Africa—prospective policy issues for the World Trade Organization', *Journal of World Trade* 28:6, 1994, pp. 122–3.

9 Trebilcock and Howse, *The Regulation of International Trade,* p. 259.

10 For a discussion of the US interests which shaped the US negotiating strategy see Peter Drahos, 'Global property rights in information: the story of TRIPS at the GATT', *Prometheus* 13:1, 1995, pp. 6–19.

11 R.Michael Gadbaw and Timothy J. Richards (eds), *Intellectual Property Rights: Global Consensus, Global Conflict?* (Boulder, CO, and London: Westview Press, 1988), and Benko, *Protecting Intellectual Property Rights,* p. 21. It should be noted that many experts are sceptical of the accuracy of these figures. See, for instance, Keith E.Maskus, 'Economic analysis of intellectual property rights: domestic and international dimensions', in Murray G.Smith (ed.), *Global Rivalry and Intellectual Property: Developing Canadian Strategies* (Toronto: Institute for Research on Public Policy, 1990), p. 120.

12 The term is Jagdish Bhagwati's. See Bhagwati and Hugh T.Patrick (eds), *Aggressive Unilateralism: America's 301 Trade Policy and the World Trading System* (Ann Arbor, MI: University of Michigan Press, 1990).

13 Ashoka Mody, 'New international environment for intellectual property rights', in Francis W.Rushing and Carole Ganz Brown (eds), *Intellectual Property Rights in Science, Technology and Economic Performance. International Comparisons* (Boulder, San Francisco and London: Westview Press, 1990), pp. 203–40, especially p. 205.

14 Ernest H.Preeg, *Traders in a Brave New World: The Uruguay Round and the Future of the Trading System* (Chicago and London: The University of Chicago Press, 1995), p. 65.

15 Quoted in John Croome, *Reshaping the World Trading System: A History of the Uruguay Round (Geneva:* World Trade Organization, 1995), p. 130.

16 Quoted in Carlos Alberto Primo Braga, 'The North-South debate on intellectual property rights,' in Smith (ed.), *Global Rivalry,* p. 175.

17 Chakravarthi Raghavan, *Recolonization. Gatt, the Uruguay Round & the Third World* (London: Zed Books, 1990), p. 133.

18 Maskus, 'Economic analysis', pp. 125–6.

19 Anne Wells Branscomb, 'Computer software. Protecting the crown jewels of the information economy', in Francis W.Rushing and Carole Ganz Brown (eds), *Intellectual Property Rights in Science, Technology and Economic Performance. International Comparisons* (Boulder, San Francisco and London: Westview Press, 1990), p. 52. Of course, exit commands have been standardized with the dominance of Microsoft operating systems since the early 1990s.

20 The Biodiversity Convention, concluded at the Rio Environmental Summit in 1992, affirmed the sovereign right of nations to determine the terms and conditions of access to their own biological resources. Not surprisingly, the United States refused to sign the convention. Trebilcock and Howse, *The Regulation of International Trade,* p. 264.

21 Raghavan, *Recolonization,* p. 124.

22 The semantic problem derives from the use of the terms 'developed' and 'developing', which are official GATT parlance. Critics of the developed/developing/least developed nomenclature quite rightly point out that such terms are based on a particular Western notion of modernization. Most of the other terminology used to divide the world into 'rich' and 'poor' countries is equally problematic. The expression North-South is misleading given that there are very rich nations in the southern hemisphere and very poor nations in the North, and given the socio-economic disparities *within* these nations as well. And the dichotomy of advanced industrialized/newly industrialized/industrializing does not quite capture it either, especially when one considers that there are very wealthy nations, traditionally classed as 'industrialized', which have relatively low levels of industrialization (Australia and New Zealand), while other wealthy nations and city states are almost pure service-based economies with barely any industrial base at all (Singapore and Hong Kong).

23 Croome, *Reshaping the World Trading System,* p. 255. Croome identifies these as Argentina, Brazil, Chile, Colombia, Cuba, Peru, Uruguay, Egypt, India, Nigeria, Pakistan, Tanzania, Zimbabwe and China. Although not a member of the GATT, China would have had observer status.

24 For instance, in 1981, the G-77 nations (of developing countries) were joined by Australia, Canada, New Zealand, Portugal, Spain and Turkey in proposing amendments to WIPO conventions that would curb the monopoly powers of pharmaceutical companies conferred through trademark and patent protection. Benko, *Protecting Intellectual Property Rights,* p. 9.

25 The United States finally joined in 1988.

26 These are Sony, Warner, NV Philips, Thorn EMI, and the Bertelmanns Music Group (BMG).

27 The United States, Canada and the EU also prevent parallel importation but these laws exist in quite a different context. *Within* the EU, parallel importation is legal, so there is a highly diverse range of music available in each member country. The proximity to the American market enjoyed by most Canadians ensures that the majors price CDs in Canada competitively with the American market. And in the United States an independent distribution system exists to compete with the distribution network owned by the majors; this provides price competition at the wholesale level.

28 Ann Capling, 'The conundrum of intellectual property rights: domestic interests, international commitments and the Australian music industry', *Australian Journal of Political Science* 31:3, 1996, pp. 301–20.

29 These sorts of provisions are likely to come under scrutiny in the WTO in coming years, in the context of the new General Agreement on Trade in Services (GATS).

30 See the entry on Australia in the 1997 National Trade Estimates Report on Foreign Trade Barriers. This can be found on the USTR's Website: www.ustr.gov.

31 Trebilcock and Howse, *The Regulation of International Trade,* p. 270.

32 For a brief but clear article-by-article explanation of the TRIPs agreement see Lenore Neal, 'Trade-related aspects of international property rights', in Kym Anderson (ed.), *Strengthening the Global Trading System: from GATT to WTO* (Adelaide: Centre for International Economic Studies, 1996), pp. 99–112, and also Terence B.Stewart (ed.), *The GATT Uruguay Round. A Negotiating History (1986–1992). Volume 1: Commentary* (Deventer and Boston: Kluwer Law and Taxation, 1993), pp. 107–16.

33 Bernard Hoekman and Michael Kostecki, *The Political Economy of the World Trading System: from GATT to WTO* (Oxford: Oxford University Press, 1995), p. 153.

34 These pressures are explored in John Stopford and Susan Strange with John S.Henley, *Rival States, Rival Firms: Competition for World Market Shares* (Cambridge: Cambridge University Press, 1992).

35 Gadbaw and Richards, *Intellectual Property Rights,* p. 16.

36 R.Dhanjee and L.de Chazournes, 'Trade-Related Aspects of Intellectual Property Rights (TRIPs): objectives, approaches and basic principles of the GATT and of intellectual property conventions', *Journal of World Trade* 24:5, 1990; C.Arup, 'The prospective GATT agreement for intellectual property protection', *Australian Intellectual Property Journal* 4:3, 1993, pp. 181–208.

37 Deepak Nayyar, 'Globalization: the game, the players and the rules', in Satya Dev Gupta (ed.), *The Political Economy of Globalization* (Boston, Dordrecht, London: Kluwer Academic, 1997), pp. 13–40.

38 Bhagwati comments (p. 112) on a chapter by Bernard Hoekman, 'Services and intellectual property rights', in Susan M.Collins and Barry P.Bosworth (eds), *The New GATT. Implications for the United States* (Washington, DC: Brookings Institution, 1994).

39 Sylvia Ostry, *The Post-Cold War Trading System: Who's on First?* (Chicago and London: University of Chicago Press, 1997), p. 190.

40 Trebilcock and Howse, *The Regulation of International Trade,* p. 249.

41 This is summed up neatly by Ernest Preeg, a member of the US negotiating team for the Uruguay Round, who observed that: 'Efforts to bring intellectual property rights into the GATT…focused predominantly on direct trading interests rather than analytic debate'. Preeg, *Traders in a Brave New World,* p. 63.

Further reading

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Chapter 6
International trade and security
The case of encryption

Olivia Bosch

The increased use of encryption in the 1990s by private business to protect trade and financial services has raised concerns about the ability of governments to fulfil their responsibilities for security and law enforcement. Cryptography is the practice of scrambling messages to make them unreadable except by authorized recipients. When applied to electronic communications and stored data, this practice is termed encryption. Until the 1970s encryption had been used solely in the military and diplomatic services. As international trade increasingly relies on telecommunications and computers and more than 90% of these information technologies lie in the civilian sector, a large commercial market for encryption products outside the military and government security services is beginning to emerge. In 1994, military messaging networks used only about 1 % of the world's encrypted communications.[1]

As US government and industry dominate both the supply and use of information technology products, the debate about the use of encryption to protect it takes place not only between US government agencies and industry but also between the United States and its trading partners. While international trade has benefited from the developments in information technology and products capable of supporting encryption software to protect trade transactions, American firms in the information technology sectors believe their market share outside the United States will be damaged if their products are prohibited by export controls from containing strong encryption which is already available abroad.

However, law enforcement and intelligence agencies want to limit the spread of encryption via government export controls to minimize its use by hostile governments, international criminal groups, terrorists and other security threats. Export controls were considered to be an effective tool by the United States and its allies during the Cold War, whereby advanced technology (including crypto-graphic products) was denied to the former Warsaw Pact. Such controls, however, are no longer sustainable in the 1990s when international trade has become so much more interdependent and reliant upon easily available and more affordable information technologies. It is not evident, therefore, that sustaining these restrictions on an increasingly profitable market sector will be successful against the challenges facing law enforcement and military security. This chapter seeks to explore how policy is developing to restore a balance between the competing demands of trade and state security.

The interaction between security and economic dimensions of international relations both during and after the end of the Cold War will be examined first. Developments in encryption and related telecommunications and computer technologies in trade, and how state and non-state actors try to influence policy regarding controls on encryption, will then be analysed. While a complete discussion, including full operational details, is not possible, there is sufficient information in the public domain to enable an understanding of the key issues relating to the use and control of encryption.

Political and economic context

The interplay between politico-military and economic issues both within and between states is not new, but the way in which they affect national foreign and domestic policies with respect to national security is constantly changing.[2] During the early stages of the Cold War, national security was perceived primarily in traditional military terms. Trade restrictions operated by most NATO members and other countries within the Co-ordinating Committee for Multilateral Export Controls (COCOM) had the military objective of denying former Warsaw Pact member countries both commercial and defence-related advanced technologies and products. In the 1970s, the shift from fixed to floating exchange rates in the international economy, the energy crisis, superpower *détente* and new advances in information technology meant that economic rather than the military dimensions of state activities had become more prominent. While the 1980s were dominated by renewed superpower nuclear and other military rivalries, the end of the Cold War has resulted in the economic dimensions of state activities regaining supremacy. Unlike the 1970s, however, non-state actors have increasingly become part of the international global economy, with the number of transnational companies having tripled since then, now accounting for about a third of the world's private sector productive assets.

Though the end of the Cold War resulted in diminished superpower rivalry and attention of governments and the press have turned to economic issues, approximately the same number of conflicts occur now as during the Cold War. Some conflicts have ended, unable to be sustained without superpower backing, and global sales of new conventional armaments have decreased by 60% from 1989 to 1995. In other areas, however, conflicts have emerged, in part, as the two former superpowers no longer influence regions as they did during the Cold War. The United Nations and regional security organizations have been involved in more peacekeeping and related military missions in the past decade than at any other time during the Cold War. Terrorism continues, while violence associated with drug trafficking and international criminal activity has increased. With 5% of the world's population not living in their country of birth, the communications network of diaspora populations is extensive and a growing concern to governments. Though conflict still prevails in the international system, its character has changed. It is now more diffuse and complex with non-state armed groups, including criminal groups, much more

involved. This poses new challenges for law enforcement and the military and security services.

Despite the number of military conflicts in the 1990s remaining approximately the same as in the previous four decades, more states and private commercial enterprises have tried to improve opportunities for trade. Trade is defined as the component within economics concerning the commercial (and bartered) transfer of goods and services within or between state boundaries. To open markets to international trade, states can provide the conditions and incentives for their commercial sectors to develop products, raw materials or services for exchange. In addition, emerging markets are also having to establish banking and financial institutions to manage the monetary and credit facilities to conduct international trade. Underpinning most commercial exchanges are telecommunications and computer technology and infrastructure, the revolutionary development of which in the 1970s and 1980s raised hopes of a new, international, economic order. Western foreign aid during the last decade was aimed in part at developing the technology for the infrastructure to support global trading. A general decline in barriers to trade and investment over the past decades has resulted in a more interdependent world economy and more trade including 'borderless' twenty-four-hour transactions.

Despite the currency and economic crises in Asia, Russia and Latin America at the end of 1997 and in 1998, information technologies have spread to more countries and are now used by more non-state actors than ever before. The majority of transactions (value and volume) are business to business rather than business to individual consumer. Trade is conducted primarily between private non-state actors such as multinational corporations (MNCs) and small- and medium-sized enterprises (SMEs), as well as by state-owned companies in most developing countries. The use of new information technologies means that banking and financial processes have become more automated and manufacturing processes have increasingly adopted the Japanese-pioneered 'just-in-time' production methods.[3] In addition to improving manufacturing processes, data search technologies are used to improve research and development for new products in the pharmaceutical and biotechnology sectors. The trade of stocks, shares and bills of lading have more rapid turnover than before, and new infor-mation-based and media products have been created and sold. The rise in global money laundering, estimated to be at least 8% of international trade and worth US$400 billion annually, illustrates that drug cartels and international criminal organizations also take advantage of the same developments in information technologies, and also participate in the global economy.[4]

In future, electronic commerce over the Internet is expected to contribute to trade at an estimated value of US$300 billion worldwide, approximately US$5 billion of which will be in Europe, by the year 2000–2. This is still a small amount, however, valued in 1996 at US$5 billion compared with US$670 billion gained from telecommunication services overall.[5] Trade in information and communications technology itself, in the form of both equipment and services, has been the fastest-growing commercial sector, valued worldwide at US$1370 billion in 1995. This

comprised 43% telecommunication services, 18% computer services, 17% computer hardware, 14% telecommunications equipment and 8% software.[6]

The strategic importance of economic security for states during the 1990s is illustrated by the attention which government intelligence agencies have given to trade- and economic-related issues. Technological developments in communications and computers led to the creation of special units or agencies to acquire, process and analyse the electronic and other communications—known as signals intelligence (SIGINT)—of foreign governments. These specialized communications agencies have capabilities which include cryptanalysis (the process of deciphering encrypted communications), an example of which is the construction and use of the Colossus machine by the British to break encrypted German communications in World War II. The United States has the largest SIGINT capability in its National Security Agency (NSA), which along with the Central Intelligence Agency (CIA) and the National Imagery and Mapping Agency, had an annual US intelligence expenditure of approximately US$26 billion in 1996.[7] The NSA, with its expertise and national security responsibility, has had a strong influence on the type and strength of encryption allowed to be exported by American companies in the information technology sectors.

This dimension of national security has not been analysed by political scientists in the same way as the more traditional issues of defence and security. In part this is attributable to the lack of publicly available information about the activities of the intelligence agencies. The requirement to understand the technical and mathematical complexity of encryption also contributes to the lack of analyses by political scientists. As encryption becomes more widespread in the civilian sector's information technology industries, the intelligence services role within a state's security system and the use of encryption in the marketplace will become new areas for academic research.

Encryption

By the early 1990s, large businesses and multinational companies began using cheaper leasing options on public communications networks to accommodate their growing volume and value of trade and business transactions. The US government also relies on these channels for more than 95% of its communications. These telecommunication carriers, whether comprising cable (coaxial copper), fibre optic, satellite, radio or microwave-based channels, do not have secure lines but are open and therefore vulnerable to interception. Media reports have led to the misperception that hackers breaking into Pentagon computer networks is the main problem of telecommunications and computer security, as more than half of computer and telecommunications-based crime, fraud and unauthorized use is conducted by current or former employees of private commercial and bureaucratic organizations. A much smaller proportion of computer crime and unauthorized access is by professional or organized criminal groups and hackers and, perhaps, terrorists. In terms of type of security breach, theft of equipment, user error and viruses were the most common breaches according to a study in the UK, with network

failures and hacking often remaining undetected and unreported.[8] The civilian industrial, financial and information technology sectors, worth trillions of dollars, not only have the bulk of the security problems, but also, compared with the significantly smaller expenditure for the NSA, have vastly more resources which could be applied to developing defences.

Encryption is only one means of protecting electronic communications and stored data, and it is not necessarily always the best way to protect networks from attack. Many of these attacks are a result of poor password and access controls and associated technical and administrative procedures, as well as of untrustworthy computer operating systems and personnel. An encryption system, however, can be used to safeguard confidentiality (secrecy), integrity (preventing modification of information during transmission) and authentication (the knowledge that persons in a transaction are who they say they are). For example, bank transactions may require not only that large sums not be disclosed during transfer (confidentiality) but also that the amounts are not modified *en route* (integrity).

Encryption is also used in the process of creating electronic, or digital, signatures for authenticating transactions or producing legally binding electronic documents or agreements. A public demonstration of this function of encryption was the use by US President Clinton and Irish Taoiseach (Prime Minister) Bertie Ahern of their digital signatures to sign a joint communiqué on electronic commerce on 8 September 1998 in Dublin. In policy terms, the use of encryption for confidentiality is being distinguished from that solely for authentication and electronic signatures. Though the distinction is still not clear-cut, it has the effect of making policy decisions which previously seemed daunting and unworkable now more manageable.

The most common types of encryption are private (symmetric) key encryption and public (asymmetric) key encryption. In the former, both parties to a transaction have the same keys to both encrypt and decrypt messages, the keys having been exchanged prior to use, for example by courier or by a public key encryption system (discussed below). A widely used private key encryption algorithm is DES (Data Encryption Standard) which the US government has used as a standard since 1977 for encrypting federal government non-classified sensitive computer data. Its use has since spread internationally underpinning the security of most banking transactions and many encryption products for maintaining confidentiality of non-classified sensitive data. The 'one-time' pad is also a symmetric key cryptosystem whereby each key pair is used only once, and thus it is unbreakable. This system requires strong physical protection of the transfer of keys and, therefore, is used mainly by the diplomatic and military services which already have elaborate security systems in place for other purposes. Encryption, however, does not need to be unbreakable to be successful; success primarily depends on cryptanalysis taking longer than that for which the information being protected is of value. Extending the key length is one way to make encryption stronger. While key lengths can be as long as, for example, 1024 bits, a key length of 56 bits has been set as one of the criteria for US export control purposes.

In public key cryptography, each party to a transaction has separate but mathematically related keys: a private key and a public key. These unique key pairs

are generated during the process of a transaction and therefore obviate the need to exchange keys physically beforehand. A message sender will use a recipient's public key, available on Internet directories, to encrypt data while the recipient, the sole owner of the related private key, is the only person capable of decrypting the message. A well-known public key encryption algorithm is RSA (named after inventors Rivest, Shamir and Adleman), which generates keys based on large prime numbers. Banks, for example, will send their private DES keys by a public key process instead of by courier which is more costly. This form of key distribution is called 'key management'.

The private key can also be used to make an electronic or digital signature. Only the public key would be able to read any message sent signed by the private key. The purpose of using encryption in this case is not for confidentiality, and therefore subject to stronger export controls, but authentication and non-repudiation which are essential components of trade transaction. Certification Authorities or Trusted Third Parties are being established globally to verify identities and sign keys to be registered as 'digital signatures'. Establishing international legal frameworks and procedures for the use of digital signatures in electronic commerce is the subject of major directives and proposals within many international organizations including the European Union (EU), the Organization for Economic Co-operation and Development (OECD), the International Chamber of Commerce, and the United Nations Commission on International Trade and Law (UNCITRAL).

Export controls: from COCOM to the Wassenaar Arrangement via US national export regulations

Trade and commercial interest in expanding the use of encryption have led to a relaxation of governmental controls on the export of cryptographic products and software. As the military and security agencies of the United States (and the former Soviet Union) used encryption to protect their communications, including that for the control of nuclear weapons, encryption was considered a munition which the United States prohibited for export. Exceptions in certain circumstances required individual licenses from the US State Department. While export controls were national they were co-ordinated within the multilateral COCOM forum comprising other NATO countries except Iceland, plus Australia and Japan. Created in 1949, COCOM was designed to deny the sales of conventional weapons and nuclear and dual-use (civil and military) high-technology goods and services and know-how considered to improve the military capability of the Soviet Union and other Warsaw Pact countries. Since the end of the Cold War, the collapse of the Warsaw Pact removed the *raison d'être* of COCOM. It formally ended in 1994; however, a successor, the Wassenaar Arrangement, formally began operating in July 1996.

The Wassenaar Arrangement is a consensus-based multilateral export control regime where members semi-annually exchange information about licences issued and items transferred concerning the exports of either conventional muni-tions or dual-use sensitive technologies, the latter including cryptographic products. As important,

information is also exchanged about licences denied to countries which do not have adequate controls on the proliferation of weapons of mass destruction or which would be accumulating militarily destabilizing equipment. Encryption might improve military communications and therefore offensive capabilities or hide communications regarding the development of prohibited weapons programmes. And, as not all governments and militaries use encryption, its use in particular areas of the world may make neighbouring countries feel less secure.

Unlike COCOM, Wassenaar Arrangement members do not have veto power on each other's national export control policies or decisions, nor do they name publicly which countries are proscribed, though they tend to be the countries which the United States lists as prohibited destinations in its national legislation. EU members of the Wassenaar Arrangement implement the criteria through the 1995 European Dual-Use Goods Regulation, on the basis of European Commission competence on trade issues.

The process of moving from COCOM to Wassenaar, however, meant that many cryptographic and encryption software products were shifted as a result of commercial pressure from COCOM's munitions category to commerce-controlled lists. This shift reflected two major trends: telecommunications liberalization and advances in computers and supercomputing. The liberalization of trade of goods and services in the telecommunications sector, in the mid-1990s, has led to the sell-off of many monopoly, state-owned telephone companies with more and smaller companies increasingly competing to provide information technology products and services. In addition, the rise of cellular phone networks in countries with embryonic or no traditional physical telecommunications infrastructure, for example in Africa, Central and Eastern Europe, has also provided a new source of telecommunications competition, as will new satellite mobile-based systems, such as Iridium, Globalstar and ICO Global Communications, expected to launch services between 1998 and 2002.[9]

In addition to telecommunications technology, developments have also taken place within the computer industry which affect not only encryption but also cryptanalysis. Computing developments have been dominated by the widespread use of the microprocessor so that in the early 1990s, higher levels of computing power previously only attainable by large commercial organizations and governments became available in smaller portable and cheaper units. The increased availability and lower costs of stronger computing capability enabled individuals, smaller businesses and other non-governmental groups to obtain easier access to information and participate more directly in electronic commercial transactions. Greater computer power has also facilitated some processes of cryptanalysis, such as 'brute force' attacks whereby an exhaustive key search would take days or hours instead of years. While a response has been to lengthen encryption keys, for example 56-bit DES has been lengthened to Triple-DES, stronger encryption becomes less user-friendly and more costly to install; businesses are unlikely to upgrade or install new systems until it becomes cost effective to do so.

The processes of the Wassenaar Arrangement have also coincided with US national export control policy. This is because the US federal government and industry dominate the world's supply and use of telecommunications and computers. In the late 1980s and early 1990s, American software and other information technology industries raised significant concern about continued government restrictions on the export of encryption technology, arguing that controls harm their trade prospects in the world market where other countries may have products incorporating their own strong encryption. As domestic use of strong encryption is not prohibited and software consumption is largest in the United States, proponents of encryption export controls were not fully convinced by industrial fears of loss of market, except perhaps at the more advanced technology level.

Despite continued military conflict and increasing international criminal activity, the United States had begun relaxing controls from 1983. However, not until October 1996 did it announce proposed legislation which appeared to mark a major relaxation of controls. Primarily in response to the concerns of American information technology industries, and after a major study on national cryptography policy recommended the progressive relaxation but not elimination of controls,[10] encryption allowed to be more easily exported was lengthened from 40- to 56-bit key lengths. On the other hand, the principle of 'key recovery' (shortcut or spare-key access to encrypted data) was introduced to meet the demands of law enforcement. Reflecting these two concerns, an Interim Rule to export regulations was passed which took effect from the end of December 1996 for a two-year trial period. It meant that all encryption items previously on the US Munitions List, except those specifically designed or modified for military applications, were transferred to the Department of Commerce Control List. Military encryption (including command, control, communications and intelligence (C3I) applications) would still be controlled by the Department of State. Items which were moved to the jurisdiction of the Department of Commerce were subject to licensing policy (a form of export control) for several categories of encryption. The first category was that certain 40-bit key length mass-market encryption software, after a one-time review, did not require licensing for export. Second, a licence exemption was possible for the export or re-export of key escrow (key copies held by government), key recovery (key access for encrypted, usually stored, data) and recoverable encryption software and commodities, subject to review, to all destinations except Cuba, Iran, Iraq, Libya, North Korea, Syria and Sudan. Third, a licence exemption renewable every six months was available for the export and re-export of 56-bit key length DES or equivalent-strength encryption if accompanied by plans to provide key recovery capabilities. Fourth, applications for export could be made on a case-by-case basis, to all destinations except Cuba, Iran, Iraq, Libya, North Korea, Syria and Sudan.

These categories were reviewed in less than the two-year trial period when on 16 September 1998, US Vice-President Al Gore announced further relaxation of export controls on encryption. The export of 56-bit DES and equivalent products no longer required key recovery plans. This relaxation acknowledged the fact that 56-bit DES keys could be computer searched more easily and that many larger commercial

enterprises already have their own key recovery capabilities for 'good business practice'. For example, senior management or security personnel key holders the and unexpected events might occur which require emergency recovery of encrypted data. Gore also stated that the exports of unlimited strength encryption products would be streamlined (under licence exception) to certain sectors including subsidiaries of American firms worldwide (except in the seven 'terrorist' states) and including with some exceptions insurance companies, health and medical organizations, and on-line merchants for client-server applications to the forty-five countries recently approved for exports to banks and financial institutions. In addition, key recovery products would be exportable under licence exception as before though the semi-annual review of key recovery agents is eliminated. Exports of 'recoverable' products would be approved to most commercial firms in countries which cover the major commercial markets including Western Europe, Japan and Australia. Case-by-case exemptions and one-time product technical reviews are maintained.[11]

In October 1998, and in the wake of Gore's announcement, the US Department of Commerce granted export licences to a coalition of major American technology firms called the Alliance for Network Security. These companies, which had sought to export strong encryption products with key recovery features, included Ascend Communications, Cisco Systems, 3Com, Hewlett-Packard Company, Network Associates, Nortel Networks, Novell, RedCreek Communications, Secure Computing Corporation, and Sun Microsystems. Other members of the Alliance not included in the October announcement are Bay Networks, Intel, Microsoft, and Netscape Communications Corporation. These firms were involved in litigation at the time.

Also in line with the US announcement, the Wassenaar Arrangement issued on 3 December 1998 a public statement arising from its fourth Plenary Meeting, which included among other items the need for 'modernisation of encryption controls to keep pace with developing technology and electronic commerce, while also being mindful of security interests'.[12] Members of the Wassenaar Arrangement are in the process of re-examining their export controls on encryption but some, like Canada, believe that the proposed controls may be stronger than existing national export controls.

Issues for law enforcement and intelligence agencies

Law enforcement agencies, which tend not to have their own cryptanalytic resources, believe that widespread use of encryption will inhibit reading information obtained from lawfully authorized monitoring. The number of individual users of encryption, however, has been relatively low (users tend to draw attention to themselves), and commercial firms are likely to share their key recovery capabilities with law enforcement upon lawful request. Yet at some point in the future, it is expected that the balance will shift to most traffic being encrypted. As controls on encryption continue to be relaxed, American software suppliers, controlling approximately 75% of the world market, will begin to export versions of their products embedded with strong encryption. Additionally, strong

encryption such as PGP (Pretty Good Privacy) continues to be accessible from the Internet. In response, law enforcement agencies are making arrangements with network service providers that decrypted information be made available upon lawful requests or in exceptional circumstances.[13]

For intelligence-gathering purposes, patterns of telecommunications flows, or traffic, can often provide more crucial information even if message contents are encrypted. It is argued that the NSA's cryptanalytic capabilities are not challenged as much as the ability to separate the information which is relevant from that which is not. According to one study:

> The NSA is alarmed that the widespread use of encryption will generate a rapid increase in the volume of coded messages sent over global networks and, as a result, severely tax its ability to acquire and exploit telecommunications. It is not that NSA will be less able to decipher specific coded messages; rather, the concern is that a flood of new encrypted traffic will make its job much more difficult.[14]

As encryption continues to be used and is less controllable, it is not certain that controls would actually deal with the security concerns newly confronting the military and intelligence communities. It would appear that even before the rapid expansion in the use of telecommunications and computing networks, let alone in the expected growth of the use of encryption, intelligence agencies were concerned less about decryption than targeting acquisition of data and then processing it. This therefore raises issues of how SIGINT is dealt with in the future. New telecommunications technology may also mean new opportunities for intelligence gathering and as more valuable communication is transmitted over telecommunications channels, even encrypted, the NSA may find more and better information over links it can exploit.

Standards and other controls of encryption

As the number and types of users increasingly resort to encryption, ensuing complexities may be tempered by the fact that trade and commercial activities rely on transmission protocols and standards in equipment. Standards are designed to be flexible enough to accommodate varying competitive products of newcomers and allow for interoperability, yet provide a point of commonality to facilitate trade among diverse parties.

An example of the process of setting standards for encryption is that which the US National Institute of Standards and Technology (NIST), in consultation with the NSA, undertook to establish DES in 1977 for protecting non-classified sensitive data. As the US federal government was the predominant user of computers, government was able to establish DES as a regulatory standard (for the public good). But DES was also a *de facto* standard (driven by market forces) as most businesses traded with the US federal government, the largest user and purchaser of telecommunications and computer equipment. However, a voluntary consensus standard (developed and adopted by industry and users who participate in standards-setting organization) dominated the process of establishing DES as NIST solicited advice and comments

from private industry users. It was an open process which seemed to have worked well, unlike the subsequent development of the Escrowed Encryption Standard (EES) which NIST adopted as a voluntary federal standard in 1994. The EES comprised a classified algorithm (called Skipjack) used on tamper-resistant computer chips with escrowed keys. The 'Clipper Chip' scheme meant that commercial and business sector firms would freely receive encryption keys from government, copies of which would be held in escrow by government agencies until required for law enforcement purposes. Industry, as well as civil liberties advocates, sceptically regarded the development of this standard, which, unlike DES, did not involve participation from the non-governmental sector. Even though the scheme was voluntary, its take-up was slow.[15] Having learned from the 'Clipper Chip' experience, the US government agencies are adopting the consensus standard approach in creating the Advanced Encryption Standard (AES) to replace DES. In August 1998, NIST shortlisted fifteen submissions made to a solicitation for AES designs.[16]

In contrast to the development of a federal standard which like DES will probably be used worldwide, many larger information technology companies might invest their high revenues to hire the best computer scientists and mathematicians to develop proprietary encryption systems. Yet depending on the industry, proprietary encryption may inhibit trade if it is not compatible with those of supplier subcontractors or trading partners. While both military and civilian sectors may have proprietary encryption systems, the civilian commercial sector may have to make choices and compromises for the purpose of trade and commerce which the military, diplomatic and intelligence services do not.

Though industry is trying to provide its own solutions to deal with the much larger proportion of computer fraud, there are impediments to improving security in the commercial sector. These include poor-quality security software, inadequate tools for detecting attacks, non-disclosure of security incidents primarily by commercial organizations and financial institutions who wish to retain their reputation, widespread societal ignorance of the threats and risks, and competition between commercial organizations as well as other information technology firms seeking to provide IT security.[17]

Related to standards issues is the degree to which international regulation of encryption would also have to be compatible with national legislation. According to the US national cryptographic study in 1996, varying national policies on cryptography which make it difficult to conduct secure international communications may hinder implementing national economic policies to open markets and reduce commercial and trade barriers.[18] While harmonizing of national legislation seems unlikely, policy guidelines by international organizations is an alternative process to facilitate interoperability of trade practices. For example, the OECD 'Cryptography Policy Guidelines' of March 1997 in effect promoted the use of encryption but its regulatory content was considered too weak to do much more than register the desire for enhanced use of encryption.

Though the relaxation of export controls is taking place within the United States and other Wassenaar Arrangement countries, many countries do not have legislation

governing the use or control of encryption, while others are erecting import controls. Some of these governments have a political interest in controlling telecommunications infrastructure, let alone encryption. Some governments in the Middle East have been trying to control the import of telecommunications hardware. Elsewhere, countries impose varying restrictions on persons wishing to access the Internet, for example China requires Internet users to register with the police. China is also developing its own-style World Wide Web in which information considered not in its national interest, for example on Taiwan and Tibet, will have been filtered out. In Russia, the Federal Security Bureau (FSB, formerly the KGB) is reported to have requested the state communications agencies to direct all Internet service providers to install a black box in their main computers and build a dedicated high-speed optical fibre data link from their offices to the FSB headquarters. This system is intended to improve investigative activity but Internet users are expected to encrypt their e-mail with widely available software.[19]

Some traders of IT products and services are concerned that controls on encryption might be exploited by government for taxation purposes. This appears to be evident in the debate over tariffs on electronically traded goods which are as important to the development of electronic commerce as the issues of its security. The ministerial meeting of the World Trade Organization (WTO) in Geneva in mid-1998 reached agreement among 132 members countries not to impose new tariffs on electronic commerce; the OECD ministerial meeting in Ottawa from 7 to 9 October 1998 reinforced this theme agreeing that traditional tax principles rather than a special regime should be applied to electronic commerce.[20] These decisions can be seen to reflect the dominance of the United States in IT and therefore also its structure of taxation in relation to trade. For example, interstate trade in the United States is not subject to retail taxes while trade between countries within Europe is.

Perhaps as a challenge to this dominance by the United States, the EU Data Protection Directive, which member states were required to implement by 25 October 1998, could empower the EU to prohibit the transfer of personal data about Europeans to countries which do not have adequate protection of privacy. As the United States relies on industrial self-regulation of privacy, there could be disruption of transatlantic electronic commerce or prohibition of MNCs collecting information from European subsidiaries.[21] This tension between the United States and European countries over security and tariffs in trade exemplifies the exertion of US 'structural' power because of its dominance in IT to obtain policy successes when it might not otherwise have what Susan Strange has called 'relational power': namely, the power to enforce decisions.[22]

Conclusion

The debate on controls on encryption highlights the degree to which in the 1990s national interest has become more focused on trade and economic security. During the Cold War, the export of IT was severely restricted for reasons of national military security. In the period after the Cold War, it is seen by many countries to be in their national interest to

export these technologies, including encryption capabilities, for purposes of protecting and promoting industrial interests and thus economic security.[23] Differentiating the use of encryption for digital signatures and authentication from that for confidentiality has provided a means for the major players in industry and government to forge ahead on developing more appropriate policies on the controls of cryptographic products. Encryption is only one of several ways to protect communications and stored data, and it is not as all-powerful and as monolithic in capability as the media or public perceptions might suggest. This is because encryption has received more attention than other means of communications security. A study of the way encryption technologies are used, together with related government policy, is a useful tool to understand broader issues concerning the ways in which governments try to maintain control over communications as part of fulfilling security responsibilities. The pressures of the global trading environment have meant that governments are no longer able to maintain export (or import) controls except on specific advanced or proprietary encryption capabilities, and therefore will develop other ways to meet their national security responsibilities in protecting and obtaining information.

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Chapter 7
International trade and workers' rights
More than a conditional link?

Gijsbert van Liemt[1]

Introduction

Few trade issues are as controversial as those linked to workers' rights. Proponents of such a linkage (workers' rights advocates, many trade unionists, among others) argue that the international exchange of goods cannot and should not disregard the conditions under which these goods are being produced, and that the international community has a legitimate role in the promotion of basic workers' rights such as the freedom of workers to bargain collectively and the freedom of children not to be exploited. They are not suggesting a global minimum wage (as many critics claim they do), but argue that when workers are unable to bargain for the best wages and working conditions possible, this could be interpreted as 'social dumping'. Finally, they point out that when workers in exporting countries are seen to be enjoying certain basic rights, it is easier to convince workers in import-competing industries of the benefits of lower trade barriers.

Critics (many trade specialists and developing country governments, among others) oppose the link with labour standards because it disrupts the healthy growth in international trade and unnecessarily complicates already highly complex trade negotiations. They question whether there exists a set of universally agreed minimum labour standards as these are culture specific. Insisting on their universality might lead to poor countries adopting inappropriate labour practices and may be irreconcilable with the principles of state sovereignty and non-interference in domestic affairs. Proponents of such a link would be more concerned about a loss of their own privileged position and a refusal to adapt to new realities, than by genuine feelings of solidarity. Lastly, they point to the tuna-dolphin case[2] to illustrate that actions taken against countries with different domestic policies are not compatible with WTO-GATT rules.[3]

Conditionality (making market access conditional on respect for workers' rights), a key feature of most discussions on trade and workers' rights, is responsible for much of the controversy. 'Northern' trade unions see the possibility to restrict market access as a necessary measure of last resort for ensuring that exporters respect certain basic workers' rights. These exporters, operating in market segments where competition is fierce and margins thin, strongly oppose this threat of trade sanctions. So controversial is conditionality that it overshadows most other elements of the

trade-workers' rights debate, including that of the universality of 'core' workers' rights. Privately exporters may agree that these are universal rights, but their opposition to trade conditionality and their scepticism about the (lack of) fairness with which it might be applied leads them to disagree in public. Unavoidably, conditionality will also have a prominent place in this chapter. But there are more dimensions to trade and workers' rights, as indeed there are to the place of labour in globalization. The critical issue is, as this chapter will argue, the need for a social 'level playing field' in an increasingly integrated world economy.

The chapter is organized as follows. The next section argues that solidarity is at the root of the international concerns about working conditions and workers' rights in poor, exporting countries. However, economic arguments also play a role; to deny workers certain basic rights could constitute an unfair trade advantage (but the magnitude of that advantage may be hard to establish, as the third section argues). Conditionality is at the heart of the discussion. It is also highly controversial. The US GSP (Generalized System of Preferences) example in the fourth section illustrates why this is so. The discussion on trade and workers' rights centres around a select group of 'core' or 'basic' workers' rights. The fifth section asks whether these basic rights are universally accepted as such.

Trade sanctions are the prime source of leverage. But sanctions are not without costs. What, as the sixth section asks, are they meant to achieve; and do they achieve what they are meant to? A multilateral arrangement might be able to accommodate some of the drawbacks usually associated with the trade-labour link. There is, however, currently little interest to do so in the International Labour Organization (ILO) or the World Trade Organization (WTO), the two organizations most frequently mentioned in this respect (the seventh section). Much more than the GATT, the WTO is engaged in intensive scrutiny of national policies to assess their possible trade-distorting effects. Certain policy measures in the social domain now risk being labelled a subsidy. This expanded definition of subsidies means, as the eighth section argues, that the WTO may no longer be able to avoid the 'fair trade' debate.

The chapter concludes that, in view of the opposition of most WTO—ILO constituents, a formal, multilateral trade—labour link is unlikely to come about soon. In the medium term, however, such a link cannot be discarded. As international and national lobbies become more vocal, more companies adopt codes of conduct, and more countries adopt GSP conditionality schemes, the calls for multilaterally agreed arrangements may well become louder.

Globalization and labour (1)

The internationalization of production and investment affects labour in several ways. It opens up new job opportunities. It also threatens jobs in import-competing industries. And it accelerates the speed of structural change, and thus the need for rapid adjustment. Globalization also affects labour standards, which are set through legislation or collective agreement. Labour, the immobile production factor, and the nation state (which

generates regulation) are widely seen as having to compete to attract internationally mobile capital and technology. Labour standards thus suffer from regulatory competition.[4] Also, workers' bargaining power is under threat as capital has acquired the option of exit and labour has not.

The pressure on labour legislation and labour's weakened bargaining power are pretty much universal features. But their potential effects on labour standards are particularly serious in the developing countries where, on the whole, labour protection is at a lower level than in the more developed economies. In certain developing countries (but not necessarily in those that trade the most), labour standards are particularly low. Workers in low-income countries tend to receive low wages. Also, when wages are low, people need to work long hours in order to make ends meet. Safety and health conditions are usually inferior to those in rich, industrialized countries. History has shown that as economies develop, wages go up, working hours come down and safety and health considerations receive more attention. However, low wages and poor working conditions need not necessarily, or exclusively, be the result of a country's low level of development. On the whole, wages reflect the general level of productivity. But they may be kept *artificially* low when the labour movement is suppressed or controlled. Collective bargaining may not be permitted, legislation may be inadequate and existing laws may not be enforced.

International solidarity can play two roles in raising labour standards. Where poor working conditions are simply the result of a low level of development, greater capital flows and increased market access in importing countries can help economic and social development in exporting countries. Where, on the other hand, these conditions are also caused by inadequate legislation, a weak enforcement of the law, the absence of democratic controls, or workers being unable to bargain for the best wages and working conditions possible, complementary actions—such as linking respect for labour standards to market access—can make a difference. As a rule, these actions aim at strengthening the position of domestic pressure groups in what is essentially a domestic bargaining process.

Solidarity or unfair trade advantage?

Solidarity is not the only argument for a trade-labour link. There is also an economic argument. Exporters would have an unfair advantage when workers are denied certain basic rights such as the right to bargain for the best wages and working conditions possible under the circumstances. The solidarity or moral argument emphasizes that core workers' rights are human rights. It is morally wrong to exploit or to repress trade unions. Whether this also provides exporters with a competitive advantage is of secondary importance. The moral argument is fairly straightforward (although the underlying presumption that core workers' rights are universal is not accepted by all—see below). The moral argument considers labour rights in the exporting country as a whole.

The economic argument, in contrast, focuses on the (manufactured) export sector. The distinction is important because the most blatant cases of exploitation are not generally found in manufacturing industries, which produce for export. The worst

offences are usually found in plantations and mines, construction industries and small service firms working entirely for the domestic market. Serious violations of workers' rights also occur in export industries, 'but this often indicates that conditions are even worse in other sectors'.[5]

The economic argument must take account of several variables including long- and short-term effects, and the interests of individual firms compared with those of society as a whole. For instance, when children receive a lower wage than adults at the same level of productivity do, their use may give the firm that employs them a competitive advantage. But it is a moot point whether society as a whole benefits from letting children spend their formative years in low-productivity jobs instead of educating them for subsequent employment in high-productivity jobs. Similarly, the effects on competitiveness of trade union action must distinguish labour surplus from full-employment economies. Finally, the economic argument must also consider whether legislation helps non-union members (through, for example, the legal extension of collective agreements to non-union establishments) or discriminates against them (the 'closed shop').

The economic case for a trade-labour link

The validity of the economic argument critically depends on two factors: what are the effects of non-respect for basic workers' rights on labour costs, and how important are the latter for a country's or a sector's competitiveness? The second factor (the role of labour costs in competitiveness) is part of a larger and well-researched debate that need not be repeated here. The first question is particular for the current debate: does the absence of the freedom to bargain collectively, the use of child and forced labour, or discrimination in employment and remuneration provide exporters with a competitive advantage, and if so by how much?[6]

These questions are of critical importance for the outcome of the debate on the trade-labour link. Yet they have been the subject of comparatively little research. The use of forced labour might well constitute a competitive advantage, and discrimination in employment a disadvantage. With child labour, once account is taken of differences in levels of productivity, the outcome is likely to be less clear cut. Also, children are more docile, but whether this is an advantage or disadvantage must be seen in the light of the nature of the products they make and how these are produced.

Freedom of association has basically two effects which are summarized in a recent OECD study.[7] On the one hand, unions raise costs when they protect the rights of their members to the detriment of non-members and the unemployed.

The study found strong empirical evidence that forming a union introduces a distortion between union and non-union workers in terms of a wage (and fringe benefits) premium. On the other hand, the study noted that in the absence of free bargaining rights, wages might be maintained at artificially low levels compared with what market forces would justify. On the whole, the study found that, on the basis of

'sparse and incomplete data', core labour standards did not play a significant role in shaping trade performance.

Solidarity and sovereignty

International action can help reinforce the efforts of domestic actors to redress or improve what they see as an unacceptable situation. Exchanges of experiences and information provide these local actors with better tools to pursue their actions. The mobilization of international public opinion can help indirectly as it places pressure on governments to pay more attention to the demands of domestic pressure groups. Consumer pressure has led to a growing number of companies adopting codes of conduct.[8] Social labels attached to handmade carpets guarantee that these have been made without child labour. Such initiatives provide consumers with more (socially responsible) choice and place pressure on producers to improve working conditions. Coercive action (conditionality) takes this international solidarity one step beyond the voluntary actions described above. When governments show little sensitivity to domestic and international actions of a voluntary nature, or when effective domestic actions are virtually impossible owing to the repressive nature of the regime, coercion has been suggested as a measure of last resort.

Conditionality can be expressed in positive and negative terms. In the former case, a party that fulfils certain conditions or complies with certain minimum requirements is rewarded with a more favourable treatment. In the latter case, a party that does not fulfil certain conditions or fails to comply with certain requirements is 'sanctioned' through the reduction or the elimination of a favourable treatment.[9] Conditionality runs counter to the spirit and the principles of the GATT-WTO. The MFN (Most Favoured Nation) principle provides that international trade should be conducted on a non-discriminatory basis. Therefore, in international trade relations and under current GATT-WTO practice, importing countries can only apply conditionality under their GSP and in their relations with non-GATT-WTO members. An example is the US GSP labour conditionality procedure.

Workers' rights conditionality in the US Generalized System of Preferences (US GSP)

The GSP allows duty-free access for a selected number of products from developing countries. Many OECD countries operate such a programme. However, until recently, the United States was the only country to have a labour clause attached to it.[10] The labour clause was introduced in 1984 at the insistence of Congress which wanted US trade negotiators to pursue respect for international labour rights as vigorously as market-access and intellectual property rights. The clause states that in extending preferences the President should not designate or maintain the designation of any country as a beneficiary if 'it has not taken or is not taking steps to afford internationally recognized worker rights to workers in the country'.

Concerned individuals and organizations could henceforth request the administration at public hearings to review the status of labour rights among

beneficiary countries. They can formally petition for action against US trading partners that seek 'to get ahead in international trade through the systematic repression of basic rights of workers'. From 1985 to 1995, 101 workers' rights petitions were filed. Of these, sixty-three petitions relating to thirty-nine countries were accepted for review. Of the sixty-three cases reviewed, twelve ended in the withdrawal or suspension of GSP benefits for ten countries, fifty-one resulted in a decision that the country concerned was 'taking steps' to afford workers' rights.[11]

The GSP procedure is not uncontroversial. Developing countries resent the conditionality aspect. In the United States, much of the controversy is rooted in the different expectations held by GSP officials and workers' rights advocates. The former generally believe that the workers' rights provisions have been pursued and have provided leverage to get beneficiary developing countries to initiate changes 'to the best degree possible, given other trade and foreign policy concerns'. The latter, however, would have liked country practice cases more vigorously pursued and sanctions more frequently exercised.

A major point of discord centres on the discretion left to the administration in the interpretation of the words 'taking steps' to meet international standards, which are open to interpretation. The administration has been accused of having accepted, for certain friendly or strategically located countries, undertakings of a vague and general nature as evidence that appropriate steps were being taken. The United States has also been criticized for its rather vague definition of international labour rights. The criticism of its GSP conditionality programme encouraged the US government to have workers' rights placed on the international trade agenda. On several occasions the US government has, unsuccessfully, suggested that a working party to study these issues be established in the GATT.

Needless to say, what OECD-based trade unions and other NGOs see as international solidarity is perceived in a totally different light by the governments of the countries which are the potential target of such sanctions. They consider such actions as interference in their domestic affairs and an attack on the sovereignty of the state; the insistence of Western governments on the universality of certain basic workers' rights resembles a 'new type of imperialism'. In fact, moral questions are invoked by both sides, with one side insisting that the international community has the obligation to insist on respect for these rights, and the other arguing that it is morally wrong for one country to attempt to shape the institutions of other societies.

Is the concept of basic workers' rights a universal concept?

The discussion of trade and workers' rights centres around a group of core or 'basic' workers' rights: freedom of association, the right to bargain collectively, freedom from forced labour and from child exploitation, and non-discrimination in employment and pay. The question whether these are universally accepted basic rights is complex but of great relevance to the discussion of the trade-labour link. Most would agree that they are. It is the rationale for the existence and the actions of the ILO (the International Labour Organization). However, several outside the OECD area (governments among them) take

a different view. They see the insistence on these rights as a new form of imperialism, a way to impose 'Western' values on countries and people with a different cultural background and at a lower level of development.

The ILO is the UN organization concerned with social development. The ILO's main means of action is the promotion of labour legislation through the adoption of international conventions, and to ensure that these are complied with. Member states voluntarily submit themselves to international scrutiny: they are free to ratify (or not) each convention. But once they do so they become subject to a supervisory procedure. This supervision takes place through regular reporting. There is also a complaint procedure. None of the ILO supervisory bodies may impose sanctions .of any kind, though their conclusions are sometimes regarded as political or moral sanctions ('mobilization of shame').

The ILO argues that its conventions have been adopted in a forum in which virtually all countries participate, and that they are designed to be of universal application. The principles contained in each convention are universal; flexibility of provisions ensures that they can be applied progressively with due regard to the stage of social and economic development of the country concerned.[12] In addition, its core conventions have been *voluntarily* ratified by a large number of countries. By 1996, ILO Convention 29 on forced labour had been ratified by 135 ILO member states, C. 98 on the right to organize and collective bargaining by 124 states, C.87 on freedom of association by 112 states, C.100 on equal pay by 123 states, and C.111 on non-discrimination by 119 states.

Those who question the view that core workers' rights are universal argue that many ILO conventions were adopted before they were independent and became a member of the ILO. They point at the divergence in ratification by region. West European nations have ratified far more ILO conventions (over fifty, on average) than developing Asian countries (less than twenty, on average). The United States has ratified no more than eleven conventions (and only one of the core conventions). A strict interpretation of Islamic law could be incompatible with the principle of non-discrimination.[13]

The supposed distinction between 'Western' and 'Eastern' values is particularly topical. The gist of this position is that human rights as propounded in 'the West' are founded on individualism and therefore have no relevance to Asia, which is based on the primacy of the community. As Steiner and Alston have argued, however, this argument is vulnerable on at least two accounts. First, it overstates the individualism of Western society and traditions of thought. Second, Asian governments assume that they or the state are 'the community'. However,

> the Community and the State are different institutions and to some extent in a contrary juxtaposition. The Community, for the most part, depends on popular norms developed through forms of consensus and enforced through mediation and persuasion. The State is an imposition of society, and unless humanised and democratised…it relies on edicts, the military, coercion and sanctions. It is the tension between them which has elsewhere underpinned human rights.[14]

Sanctions and the threat of sanctions

OECD-based NGOs (and trade unions in particular) have argued that to halt violations of workers' rights, trade sanctions should be considered as a measure of last resort. Governments of potential target countries are, understandably, against the use of sanctions. NGOs in these countries are divided on the issue, aware that what is intended as an act of solidarity could well have significant negative effects on employment. 'Sending' country companies question the effectiveness of sanctions. They feel that their governments underestimate the damage sanctions do to commercial relations.

Governments that would be applying the sanctions have to find a balance between principles and interests. They cannot afford to take a narrowly focused position, as many NGOs do. They must consider the impact on the commercial and bilateral relationship. Interstate relations are not just concerned about human rights and workers' rights. They cover a whole range of issues, from landing rights for the domestic airline to access to government procurement contracts, not to mention trade and investment promotion. On the whole, states are keen to develop good contacts with other states because both parties expect to benefit from such good relations.

Diplomats and other foreign office personnel can be expected to be reluctant to engage in fact finding, criticizing (let alone openly criticizing) those with whom they are charged to maintain good relations. However, an analysis of the procedures surrounding the annual (US) State Department Country Practice Report[15] somewhat nuances this view, at least where it concerns fact finding and reporting. When the US State Department started its yearly reporting, many were opposed to embarrassing friendly nations with public critiques. However, as de Neufville[16] has argued, the reports became influential through the process of preparing, presenting and publicly debating their analysis. Clearly, there were tensions among the reporting obligation, the mission to maintain diplomatic relations with nations, and other foreign policy objectives. However, she also found that, within the State Department, progressively much of the original scepticism and resistance dissipated. The requirements to produce the reports systematically increased the awareness of these issues throughout the Department as the analysis and review process forced questions to be asked internally that would not otherwise be addressed.

Governments have imposed sanctions for a number of reasons: to protect workers' and human rights, to halt nuclear proliferation, to promote political stability, to settle expropriation claims, and to combat international terrorism, among others. The imposition of sanctions addresses three groups of audiences: to the target country it says the sender does not condone such actions; to allies it says that words will be supported with deeds; to domestic audiences it says that the government is sensitive to the concerns expressed by its citizens. Above all, sanctions are thus meant to send a signal. They are rarely expected to solve anything. Whether and how effective sanctions are as a policy instrument is the subject of much discussion. Alston is very sceptical. In his view, sanctions (to improve human rights) 'address only a small part

of the overall problem, are readily manipulated for extraneous purposes, and have rarely proved to be particularly efiective'.[17]

In fact, the *threat* of sanctions and the publicity surrounding the procedure may be the true source of leverage. Governments concerned about their international image do not want their workers' rights situation to be criticized in public:

> [G]overnments do not want a US determination that they are not providing their workers with rights they should have. Governments do not want it pointed out that they are not enforcing their own laws. This sensitivity is, thus, the source of the controversy over these provisions in GSP, as well as the source of some degree of its leverage.[18]

Indeed, the fact that governments knew that 'their case' was being reviewed under the US GSP has, on occasion, led to sudden, remarkable improvements in the labour rights situation in these countries. There is evidence that several countries have moved to reform their labour code following the announcement by the GSP subcommittee that a GSP review would be initiated. It is important to note that such threats can have both desired and undesired effects as the example of US trade sanctions and child labour in Bangladesh[19] showed.

US trade sanctions and child labour in Bangladesh

Spurred by US-based NGOs, in 1992, US Senator Tom Harkin introduced the *Child Labour Deterrence Act* that would ban the importation into the United States of products from industries which use child labour. This caused alarm in Bangladesh which, in 1991–2, depended for over 60% of its export earnings on garment exports, much of it to the United States. Immediately, the Bangladesh Garment Manufacturers and Exporters Association (BGMEA) urged its members to dismiss all child workers. Within a few months, BGMEA could report that there were virtually no children left in the industry. Around 20,000 children had been dismissed. The threat of sanctions had clearly been successful.

There were, however, other dimensions to the problem. The children who had been dismissed (most of them girls) were too old to go back to school. There were no suitable alternative jobs available. Their families needed the money. In Muslim Bangladesh, the garment sector is one of the few occupations in which females have been able to move out of the home and into the workforce. Mothers brought their daughters to work so that they could ensure that the girls were not mistreated and that their virtue was protected. The girls only performed light work; but long working hours was a problem.

With no clear alternative, the children staged a demonstration demanding that they be given their jobs back. It was then that local, US and international organizations (such as ILO and UNICEF) representing different viewpoints retention of child garment workers, removal of child workers, and those advocating a wider solution—met with the BGMEA to find a way to mitigate the effects of the dismissal on the

children. After long negotiations it was agreed that the BGMEA would delay the deadline for the dismissal of the children in favour of their gradual removal tied to the availability of educational facilities. No new children would be hired. UNICEF would fund the schooling of the youngest. Sanctions must thus be distinguished from the threat of sanctions. The threat of sanctions provided a degree of leverage to improve conditions. However, once the sanctions have been imposed this leverage is lost.

Sanctions: the perspective of companies in the 'sender' country

Companies in sender countries are, on the whole, critical of the apparent ease with which politicians propose or impose sanctions. For obvious reasons, American companies are particularly critical. Between 1993 and 1996 alone, no less than sixty-one US laws and executive actions were enacted authorizing unilateral economic sanctions for foreign policy purposes. Thirty-five countries were targeted. American business is concerned about the economic effects of this 'light switch diplomacy', that is to say, the belief that foreign trade is a tactical instrument of foreign policy, and that major commercial relationships can be turned on and off. Business relations take a long time to mature. 'Who wants to deal with an unreliable supplier, especially when the supplier is not the only game in town?'[20]

Sanctions: small and large economies

Imposing sanctions is usually the 'privilege' of large, powerful economies (with considerable bargaining power). Smaller, weaker economies (with little bargaining power) tend to oppose the use of sanctions, if only because they stand the greatest chance of being the target.[21] Hufbauer *et al.* also found that economic sanctions seemed most effective when aimed against erstwhile friends and trading partners. In contrast, sanctions directed against target countries that had long been adversaries were generally less successful. In all, sanctions had the greatest chance of being effective when the subject was a small economy that was highly dependent on the American market. Large, powerful economies are less easily pushed. This point was driven home in a painful way for the United States on the issue of renewing the MFN status accorded to China.

US trade conditionality and China's MFN status[22]

China is not a party to the GATT-WTO. Each year, therefore, the US Congress must renew the authorization to provide MFN status to China (and other countries which are not party to the GATT-WTO). This renewal had been routine since 1980 when it had been extended for the first time. After 1989, however, Congress felt that this could only be done if China was taking steps to improve the domestic human rights situation. The Chinese government strongly objected to this type of pressure being exercised, It argued that the United States would suffer more than China if its trading privileges were revoked. It mobilized American exporters and would-be exporters to press this point in

Washington. It placed (or threatened to place) orders with non-American companies which might otherwise have gone to American companies. And it released several prominent prisoners.

However, this annual ritual became increasingly strenuous as China's economic and political power increased and its assertiveness in the international arena grew. Then, in May 1994, President Clinton announced that he would renew China's MFN trading status *without* reference to its human rights record. Difficult though it was for him to lower the banner of human rights, on which he had campaigned for the presidency, his concerns had to be balanced against other factors. 'China has an atomic arsenal and a vote and a veto in the UN Security Council', he said.

> It is a major factor in Asian and global security. We share important interests, such as in a nuclear-free Korean peninsula and in sustaining the global environment. China is also the world's fastest growing economy. Over $8bn US exports last year supported more than 150,000 American jobs.[23]

In addition to this essentially pragmatic decision he raised a fundamental issue: 'Will we do more to advance the cause of human rights if China is isolated, or if our nations are engaged in a growing web of political and economic co-operation and contacts?'

The multilateral approach to labour conditionality

Autonomous procedures such as the US GSP conditionality are comparatively easy to establish. They are popular with NGOs because they allow them a good deal of leverage. But these procedures have been criticized for being particularly vulnerable to trade-offs against strategic interests. They also lack the moral authority of multilateral procedures. The interests of smaller countries would seem to get a fairer hearing in a multilateral than a bilateral setting.

That is not to say that these multilateral fora are immune to similar conflicts between interests and principles. Criticism focuses on their 'democratic deficit'. The power that is being transferred to the WTO as a result of the Uruguay Round Agreement is a source of concern to those who see the WTO as the 'watchdog of the interests of powerful Northern nations and their multina-tionals'.[24] Othersbelieve that the WTO 'would strengthen and formalise a world economic government dominated by giant corporations, without a correlative democratic rule of law to hold this economic government accountable'.[25]

Large countries also have reservations about passing the power of decision making to a strong, well-coordinated multilateral organization. Big nations do not necessarily find it in their interest to subordinate their national objectives to a powerful world community. Particularly on such a sensitive subject as trade conditionality, with potentially heavy political overtones, big countries may be reluctant to cede their authority to an international body whose actions will inevitably be guided by political considerations of its own.[26]

Despite such misgivings, most agree that the moral force that results from an agreement reached amongst all or, at least, a large majority of nations is superior to a unilaterally imposed arrangement. It is the reason why those in favour of labour conditionality have wanted the issue to be taken up in a multilateral context. A multilateral agreement would guarantee that procedures and objectives are seen as fair by all involved. It would apply to all participating countries (contrary to the GSP conditionality, which applies only to 'beneficiary countries'). The GATT-WTO and the ILO are most frequently mentioned in this respect. The two organizations have a dispute settlement procedure (in the GATT-WTO) and an elaborate supervisory procedure (in the ILO).

Nevertheless, these two organizations are at present ill-equipped for operating some kind of labour conditionality scheme. The GATT-WTO's mandate is to work towards the elimination of trade barriers; labour conditionality would add a trade barrier. Similarly, the ILO's mandate is to promote respect for labour standards and not to apply sanctions to countries that do not respect them. It believes that through social dialogue at the national and international level it can help achieve sustainable social and economic development. Moreover, the WTO does not pretend to have any authority in the labour field; similarly, the ILO claims no authority in the trade field.

There have of course been initiatives at least to start a discussion. We mentioned the US government's proposal to set up a working party in the GATT, but this has come to nought. More significant perhaps has been the tuna-dolphin ruling which illustrates current GATT-WTO thinking regarding the conditions under which traded goods are produced. The GATT panel clearly stated that each country should have the right to determine its own regulations regarding the production process of traded goods and that the presence or absence of these regulations could not justify trade restrictions by other Contracting Parties.

Globalization and labour (2)

The efforts to establish a link between trade and workers' rights at the multinational level have not been successful. Most WTO and ILO constituents object to such a link. The matter might be left to rest there were it not for the WTO's considerably expanded mandate, the implications of which have raised concerns in certain quarters. The WTO is designed to have a substantially larger role than the GATT. The WTO will administer not just the 'old' GATT, but also the agreement on services (GATS), and the agreement on the enforcement of intellectual property rights. Most importantly, the WTO will not just govern a trading system which largely restricts itself to policies at the border (as the GATT did) but also cover many aspects of domestic policy making to the extent that these affect international competition in goods and services.

With tariffs, the 'traditional' subject of negotiations, reaching very low levels, trade regulators are increasingly focusing on the much broader notion of non-tariff barriers. A growing range of domestic policy measures is being scrutinized for their effects on competition. As a result, the power of individual governments to take policy measures in many fields is being circumscribed by WTO concerns that these

could constitute an implicit or explicit subsidy. This scrutiny by the WTO (and other, regional, supranational bodies) weakens the discretion that national governments traditionally had to devise, after the normal democratic consultations, those measures they considered necessary and desirable. These measures might or might not have social objectives, but they were not considered to be of concern to other countries or supranational bodies.

The new, intensified, supranational scrutiny has changed this. It has broken up what Langille has called 'the two-way street of democratic legitimacy—the irrelevance of the political processes elsewhere and the legitimacy of resolution of labour policy issues domestically'.[27] Domestically, certain policy measures in the social domain now risk being labelled a subsidy, just like government activity elsewhere is now being scrutinized for its effects upon domestic politics. Taking this line to its logical conclusion, Langille argues that the *absence* of certain types of legislation in third countries could be labelled a negative subsidy, an unfair trading practice. This, he argues, should also be the subject of international scrutiny and considered for its effects on the 'level playing field'. 'Once governmental action or nonaction in labour policy…is problematized as a potential subsidy, then there is no alternative to engaging in the debate about the appropriate scope of market regulation (of labour relations for example)', leading him to conclude that the considerably expanded definition of subsidies leaves free traders no choice. They must now consider fair trade: 'Fair trade is free trade's destiny'. In his view, international trade talks provide the forum for regaining some degree of political control over the labour policy that was lost as a result of trade liberalization. 'Domestic labour standards will, to some extent, be established internationally. The issue is how, not whether they will be established internationally.'

Conclusion

The principal conclusion from the above is one of cautious satisfaction. International labour standards, which for long were considered to be basically the concern of trade unions and human rights groups, are now being considered by a much wider audience that includes high-profile consumer goods producers and academics, including trade specialists. Two of the world's best-known trade specialists have just published two volumes on 'Fair Trade'.[28]

Adequate labour legislation and the freedom to organize and to bargain collectively are necessary preconditions for a fair distribution of the benefits of international trade. To ensure that these preconditions are met is the responsibility of elected parliaments and other domestic actors (including progressive employers). Trade unions, human rights and consumer groups in importing countries have exercised pressure on governments of exporting countries and on (internationally operating) companies to pay more attention to the views of these domestic actors. Where this fails (or is impossible owing to the repressive nature of the regime), trade conditionality (making market access conditional on respect for workers' rights) has been suggested as a measure of last resort. Such conditionality may help redress

certain extreme situations but it is a relatively blunt instrument that can, but need not, have the desired effects. A principal dilemma is that the threat of sanctions seems to provide more leverage than actually imposing sanctions.

The US GSP conditionality is the prime example of trade conditionality. It is carefully designed, and comparatively transparent, but it leaves the US administration the ultimate judge of the trade-off between interests and principles. Currently, no multilateral trade—labour link exists. Given the broad opposition to the idea, there is unlikely to be one in the near future. Systematic reporting on a small group of core labour standards by widely respected bodies seems a good and effective way forward at the moment. The ILO's suggestion to present this small group as a 'Social Statute' ('Socle Social') with intensified supervision is a good initiative. Governments could in future, and on a voluntary basis, also use the WTO's trade policy reviews to provide information on progress in the implementation of the core standards.

There may never be a multilateral trade-labour link. The constituents of the ILO and WTO have successfully kept the issue off the (negotiating) table. Nevertheless, as international and national lobbies become more vocal, more companies adopt codes of conduct,[29] more governments adopt GSP condition-ality schemes, the 'Social Statute' becomes widely adopted, and subnational entities (cities, provinces, American states[30]) become more active in this field, the calls for multilaterally agreed solutions could well become louder.

Globalization is generally agreed to have two main effects. It accelerates the speed of structural change (and hence the need for more rapid adjustment) and it weakens the power of national structures and institutions. As these national entities pass on their decision-making powers to higher bodies such as the WTO (and the EU), a critical question arises of how transparent and how democratic these bodies are. Another potential problem is their segmented view of the world. Domestic trade measures can have social objectives;[31] domestic social measures may have effects on trade. The WTO judges these measures for their effect on trade and, as the case may be, labels them as trade distorting, subsidies, etc. Unless non-trade interests (including labour) are adequately represented or taken into account at the international level, there could well be a backlash against the operations of these supranational and international bodies and against efforts to achieve further (regional and global) economic integration.

Notes

1 I am grateful to Dean Spinanger, Steve Woolcock, Pitou van Dijck, Brian Hocking and Steven McGuire for comments.

2 In 1988, the United States tightened the embargo on tuna fish caught by using methods causing a high rate of dolphin mortality. Mexico objected to this attempt to limit the importation of goods *not because of their characteristics as products, but because of the way they were being produced*. It took the matter to the GATT, which ruled in Mexico's favour.

3 An earlier generation of trade negotiators took a less segmented view of the issue. The (Havana) Charter of the International Trade Organization (ITO) stated that 'Members

recognize that unfair labour conditions, particularly in production for export, create difficulties in international trade', and committed nations to eliminate such conditions within their territory. If complaints regarding low labour standards were taken to ITO dispute settlement, the Charter called for the ITO to co-operate with the ILO.

4 Alvin Klevorick, 'Reflections on the race to the bottom', in Jagdish Bhagwati and Robert E.Hudec (eds), *Fair Trade and Harmonization: Prerequisites for Free Trade?* (Cambridge, MA: MIT Press, 1996).

5 Gus Edgren, 'Fair labour standards and trade liberalization', *International Labour Review* 118:5, September-October 1979, p. 525.

6 A related question is whether withholding market access is used for protectionist purposes. For this to be the case it is necessary not just that respect for core standards raises unit import prices, but also that the export economy or economies concerned are responsible for a sufficiently large proportion of the imports of the commodity in question in the importing economies. Goete Hansson, *Social Clauses and International Trade* (London: Croom Helm, 1993).

7 OECD, *Trade, Employment and Labour Standards: A Study of Core Workers' Rights and International Trade* (Paris: OECD, 1996).

8 See, for example, Gijsbert van Liemt, 'Codes of Conduct and International Subcontracting: a "private" road towards ensuring minimum labour standards in export industries', in G.Gereffi, F.Palpacuer and A.Parisotto (eds), *Global Production and Local Jobs* (Geneva: International Institute for Labour Studies, 1999).

9 Since 1995 the EU GSP includes a 'special incentive' clause (in addition to an (amended) withdrawal clause), which offers supplementary benefits in compensation for the supplementary costs faced by countries wanting to apply more advanced social policies. *The possibility of withdrawing* GSP benefits was expanded to include slavery, forced labour and exports of products manufactured in prisons. See van Liemt, 'Labour in the global economy: challenges, adjustment and policy responses in the European Union', in O.Memedovic, A.Kuyvenhoven, W.T.M.Molle (eds), *Globalization of Labour Markets, Challenges, Adjustment and Policy Response in the European Union and Less Developed Countries* (Dordrecht and Boston: Kluwer Academic, 1998).

10 In fact, labour conditionality clauses are now attached to several US trade (and investment) programmes and provisions: the Caribbean Basin Economic Recovery Act (1983); the GSP Program (1984); the Overseas Private Investment Corporation (1985); the Multilateral Investment Guarantee Agency (1987); Section 301 in the Omnibus Trade and Competitiveness Act (1988); The Andean Trade Preference Act (1991); and Section 599 of the fiscal 1993 Foreign Operations Appropriations Act (1992). However, only the GSP Program has a review and decision process to implement sanctions designed to enforce the workers' rights provision. United States General Accounting Office, *International Trade Assessment of the Generalized System of Preferences Program* (Washington, DC, 1994).

11 Pharis Harvey, 'US GSP labor rights conditionality: "aggressive unilateralism" or a forerunner to a multilateral social clause?', Paper presented at the conference 'Labour and International Economy' organized by the International Institute for Labour Studies (Geneva, 14–15 March 1996).

12 Nicolas Valticos, 'The Asian states and international labour conventions', in R.St Macdonald (ed.), *Essays in Honour of Wanf Tieya* (Boston: Kluwer Academic, 1993).

13 Heiner Bielefeldt, 'Muslim voices in the human rights debate', *Human Rights Quarterly* 17:4, November 1995.

14 Henry J.Steiner and Philip Alston, *International Human Rights in Context: Law, Politics and Morals* (Oxford: Clarendon Press, 1996), p. 238.
15 A compendium of over a thousand pages presenting statistics and analysis of human rights in virtually all nations.
16 Judith Inez de Neufville, 'Human rights reporting as a policy tool: an examination of the State Department Country Reports', *Human Rights Quarterly* 8:681–99, 1986.
17 Philip Alston, 'International trade as an instrument of positive human rights policy', *Human Rights Quarterly* 4:1, Spring 1982, p. 155.
18 US GAO, *International Trade, Assessment of the Generalized System of Preferences Program,* p. 121.
19 Source: M.Abu Taher, Wahidur Rahman and Susan Gunn, *Child Labour and the Trade Debate: New Initiatives by Bangladesh,* unpublished mimeo.
20 National Association of Manufacturers, *A Catalogue of New US Unilateral Economic Sanctions for Foreign Policy Purposes 1993–96* (Washington, DC: NAM Trade and Technology Policy Department, 1997).
21 Gary Clyde Hufbauer, Jeffrey J.Schott and Kimberly Ann Elliot, *Economic Sanctions Reconsidered: History and Current Policy,* 2nd edition (Washington, DC: Institute for International Economics, 1990), p. 63.
22 Based on Steiner and Alston, *International Human Rights in Context,* and *Financial Times* 28–29 May 1994.
23 As quoted in the *Financial Times,* 28/29 May 1994.
24 Martin Khor, the director of the influential NGO 'Third World Network', quoted in 'Report of the ICDA workshop on the Social Clause', *ICDA Journal* 2:1, 1995, p. 81.
25 Ralph Nader, the American consumer advocate, in his testimony on the Uruguay Round of the GATT before the House Small Business Committee, 26 April 1994.
26 M.S.Daoudi and M.S.Dajani, *Economic Sanctions: Ideals and Experience* (London: Routledge, 1983), p. 167.
27 Brian Alexander Langille, 'General reflections on the relationship of trade and labor (or: fair trade is free trade's destiny)', in Bhagwati and Hudec, *Fair Trade and Harmonization,* p. 256.
28 Bhagwati and Hudec, *Fair Trade and Harmonization.*
29 See van Liemt, 'Codes of Conduct and International Subcontracting'.
30 For example, the Burma Selective Purchasing Legislation of the State of Massachusetts introduced in 1996 prohibits the State procuring from companies that do business with Burma, because human rights are not respected there.
31 See van Liemt, 'Labour in the global economy'.

Further reading

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Chapter 8
International trade and the environment

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The impact of human activities on the environment is increasingly causing serious concern. In terms of the degradation of land and water quality, the pollution of the local and global atmosphere, and the depletion of natural resources, most of the current trends reveal worsening environmental problems, suggesting that national and international environmental goals will not be met without extensive policy reform and significant changes in practices and strategies. The picture, however, is not entirely gloomy; the successful reduction, in almost all developed countries, of emissions of ozone-depleting chemicals and of the gases which cause acid deposition shows that environmental goals can be met -and, furthermore, can be achieved without negative economic effects.

The array of international environmental regulation is developing rapidly. As well as the framework offered by Agenda 21, the programme for action aimed at achieving sustainable development in the twenty-first century signed at the 1992 UN Conference on Environment and Development (UNCED), almost 200 multilateral environmental agreements (MEAs) now exist or are under negotiation, covering a wide variety of polluting or otherwise unsustainable behaviour. Several of these, such as the UN Framework Convention on Climate Change, have memberships which effectively encompass the entire international community.

Since trade and environmental policies both affect the use of natural resources, it is hardly surprising that the two are increasingly interacting. In theory, the objectives of trade liberalization and environmental protection should be entirely compatible. Both have as their aim the optimization of the efficiency of the use of resources, whether from the perspective of maximizing the gains from the comparative advantages of nations, through trade, or of ensuring that economic development becomes environmentally sustainable.

Indeed, each of the UNCED and Uruguay Round agreements claim to be in accordance with the other. The former states that: 'An open, multilateral trading system, supported by the adoption of sound environmental policies, would have a positive impact on the environment and contribute to sustainable develop-ment'.[1] Although the World Trade Organization (WTO) agreement itself contains no reference to environmental sustainability (other than a passing mention in its preamble), its founding conference agreed a work programme for a new Committee on Trade and Environment (CTE), designed to 'identify the relationship between trade measures and environmental measures, in order to promote sustainable development [and] to

make appropriate recommendations on whether any modifications of the provisions of the multilateral trading system are required'.[2]

Unfortunately, given the world's current political and economic systems, and the extent to which environmental externalities (the costs associated with resource use, e.g. pollution) are or are not incorporated into economic policies and pricing mechanisms, the objectives of trade liberalization and of environmental protection are not always reconcilable. In some cases the expansion of trade has demonstrably assisted environmental standards; in others it has not. The two sets of global and national regulations have evolved with almost no co-ordination, and are increasingly coming into conflict as regulations drawn up in pursuit of environmental sustainability have been challenged as erecting barriers to trade, notably in several cases brought before disputes panels of the General Agreement on Tariffs and Trade (GATT) and WTO.

Trade and environmental policies are inextricably and inevitably interlinked. This chapter aims to offer a brief guide to the major controversies: why trade may be good for the environment, and why it may be bad; what impact environmental regulation has on international competitiveness; what conflicts develop from the legal regimes; and how the relevant institutions and regimes interact.

Trade liberalization and the environment: positive and negative impacts

Positive impacts

According to the theory of comparative advantage, trade allows countries to specialize in the production of goods and services in which they are relatively most efficient. In other words, trade enables each country to maximize output for a given input of resources—which is also, of course, a movement in the direction of environmental sustainability.

Following from this principle, open trading regimes do tend to be associated with economically liberal policies in general, including less distortionary pricing policies; natural resources such as water, timber or energy are more likely to be realistically priced. Prices may still not reflect the true environmental costs of production and consumption but at least they are less likely to be subsidized. The poor environmental record of the socialist states in Eastern and Central Europe, where energy prices were artificially held far below world levels, partly because these countries were isolated from international markets, provides a warning to those who regard protectionism as likely to be helpful to the environment.

It is in this area that trade liberalizers can most obviously make common cause with environmentalists. Price-distorting subsidies remain an important factor in many areas of natural resource use, including energy, agriculture, forestry, textiles and fisheries. In the case of fishing, for example, it has been estimated that the current value of subsidies represents more than 75% of the total value of the global catch, while at the same time 60% of major commercial fish stocks are being fished at or

beyond their biological limit. The removal of such price distortions in the use of natural resources would benefit both trade and the environment.

Similarly, countries with open trading regimes are also likely to be those most open to the spread of new technology, which in general is likely to be less environmentally unfriendly. A World Bank study of the adoption of clean technology for wood pulp production, for example, found that 'openness is unambiguously environment-saving', reducing pollution by 10–20% over a period of over ten years.[3] The internationalization of production processes and the expanding activities of transnational corporations (TNCs) can similarly help to improve environmental standards; compared with domestic firms, TNCs generally have access to superior technology, invest more in research and development, and may often be vulnerable to NGO and shareholder pressure for high standards in their home countries.[4]

Open economies are also able to engage in and benefit from the growing world market in environmental technologies and services, currently worth an estimated $200 billion and forecast to grow by 50% during the current decade.[5] Adoption of strict environmental regulations in one country may even encourage a levelling up of standards in other countries, as manufacturers seek to expand markets for products which conform to the new requirements, and TNCs often prefer to standardize technologies.

Where trade liberalization reduces barriers to manufactures and services, and allows developing countries to diversify away from excessive reliance on exports of primary commodities, and to benefit from their comparative advantage in labour costs, environmentally unsustainable practices of resource extraction may be reduced or ended. The diversification of the Indonesian economy in recent years from timber and oil to textiles and electronics is a good example, as is the rapid development of the software industry in India. The ending of the practice of tariff escalation, by which developing countries face higher tariffs against exports of manufactured and processed goods than for raw materials and primary products (common particularly in the timber and wood products sector), is another example of the potential for the mutual supportiveness of trade and environment policies.

Finally, there is little doubt that the rapid expansion of trade since World War II has been largely responsible for the historically unprecedented rate of growth in income amongst the developed and newly industrializing nations. Rising living standards are generally associated both with a reduction in poverty and with the environmental degradation which accompanies it, and with an increasing concern for 'quality of life' issues and environmental protection. The higher national income provides the resources necessary to invest in cleaning up pollution, conserving energy, installing less environmentally unfriendly technology, and so on. For example, studies of levels of sulphur dioxide and particulate pollution in cities around the world show that once countries reach a national income of about $5000 per capita, the levels of these air pollutants tend to decline.[6]

The expansion of trade is important, therefore, not just for development, but for *environmentally sustainable* development. As the International Institute for Sustainable Development has pointed out,

> Making the transition to sustainable development will require substantial amounts of capital. And it is clear that little of this money will come from parsimonious Northern parliaments. For many countries, much of the new capital will have to come from increased trade revenues.[7]

Negative impacts

Notwithstanding these positive impacts, there are a number of reasons why trade can also contribute to a worsening of environmental standards.

First, in most cases the growth in economic activity which trade liberalization causes is itself likely to result in increased pollution and the unsustainable consumption of natural resources. This arises because modern economies fail to incorporate environmental externalities into economic pricing and decision making. An American study, for example, estimated that if the costs of air and water pollution, accidents and other health effects caused by the mining, transport and consumption of coal were factored in, its price would increase from about $46 per ton to over $200.[8] Since these environmental and other costs are not internalized, more coal is consumed than if they were. This is not, of course, a problem with trade *per se,* but with economic activity as a whole—but trade is a magnifier, and trade liberalization will amplify the environmental impacts of unsustainable patterns of economic activity.

In an ideal world, cost internalization would take care of the problem; the price of goods would reflect the environmental costs involved in their production and consumption, varying with the different environmental impacts they caused depending on where and how they were produced. However, calculating the precise environmental costs of processes and allocating them to particular industries is an enormously difficult procedure even on a national level. This problem lies at the heart of many trade-environment conflicts.

Even where attempts are being made to incorporate environmental externalities—through environmental taxation, for example, or regulation—the process is invariably proceeding at different speeds in different countries. Yet trade rules are necessarily set internationally, and the multilateral trading system may fail to allow for such differences in national efforts at achieving environmental sustainability, even when policies are aimed at controlling transboundary or global environmental problems—placing significant constraints on a country's ability to develop its environmental policy.

Although open markets in general encourage the spread of environmentally friendly technology, the extent to which the environmental improvements introduced by TNCs are sustainable is questionable. In an increasingly globalized economy, the turnover of investment in particular countries is increasing—TNCs may move out of a country as fast as they move in. This is particularly true, of course, in natural-resource-based industries where the resource base may be subject to exhaustion. TNCs may also see relatively low-standard developing countries as dumping grounds for second-hand equipment rendered unusable in higher-standard countries, and the

multilateral trading system may make it difficult to place controls on this trade even where the government of the country of import wishes to do so.

Finally, although it is often argued that rising national income leads to increasing expenditure on pollution control, and therefore to lower levels of emissions, the evidence for this is highly questionable. A closer examination of the data reveals that at best this may hold only for some pollutants (e.g. sulphur dioxide) but not for others (e.g. carbon dioxide), and that for many pollutants, if there is an income-related 'turning point', it is substantially above the income levels likely to be enjoyed by most countries for some time. Furthermore, there is never an automatic link between economic growth and pollution control; effective public policies for environmental protection are always required.[9]

Environment, competitiveness and investment

The impact of environmental regulation on economic competitiveness is a much debated and somewhat unresolved issue. A country with strict environmental regulations may fear that its economy will be undermined by competition from other countries with relatively more lax environmental standards. Competition from products which are cheaper as a result may force the country with higher environmental standards to reduce them to avoid a loss of market share, in a 'race to the bottom'. At its most extreme, this argument leads to the concern that entire industries facing tough regulatory regimes may depart for other countries with less strict standards—the so-called 'pollution havens'. Conversely, producers in low-standard countries may fear that they will be unable to comply with regulations and standards more appropriate to a rich industrialized nation and thus lose export opportunities.

The evidence so far for the existence of so-called 'pollution havens', however, does not seem to be very strong. A 1988 study[10] showed that in some particularly hazardous industries—asbestos, benzidine dyes and pesticides—there had been some movement to escape strict environmental standards. Indeed, some countries, including Ireland, Spain, Mexico and Romania, had deliberately set themselves up as pollution havens. In Mexicali, on the US—Mexican border, more than a quarter of factory operators said that Mexico's lax enforcement of regulations influenced their decision to locate there; most cited California's more stringent regulations as a major factor in their decision to move.[11] This tendency will be strongest in industries whose products are undifferentiated, and which are most subject to small, and environment-related, cost differences.

In general, however, the relocation effect appears to be weak. Pollution havens themselves are not immune to pressures for higher environmental standards. Where market growth in an industry is strong, most companies usually prefer simply to pass on higher compliance costs to their customers. Indeed, there is some evidence to suggest that foreign investment may flow in the *opposite* direction, away from pollution havens. Where companies have acquired a corporate commitment to high environmental standards, there may well be a reluctance to dilute these, or to be seen to dilute them, even in countries where they are not required. Fear of liability for

clean-up costs may deter industry from setting up in already polluted areas. Most importantly, in most cases the costs appear to be too limited to trigger such drastic action. For most industries pollution control costs rarely top 1.5% of total costs; only in a very few subsectors do they reach 3%, even in the United States, where standards are high and regulations not particularly cost effective.[12]

Indeed, it is argued that in a dynamic business environment, higher environmental standards may in practice act as a spur to innovation and competitive success. The example of Germany, where standards are high, and industry is highly successful in the international market for pollution control equipment, is often cited. Trade may be a key factor in the ratcheting-up of standards. An important factor in the German pressure for the adoption of strict vehicle fuel emission standards within the EU, for instance, was the fact that the German vehicle industry was already tooled up to produce cars fitted with catalytic converters for the American market, where strict standards had already been adopted.[13] Indian leather producers have been forced to change their tanning processes to meet European standards that forbid contamination with particular fungicides and dyes, with accompanying improvements to the local environment surrounding the tanneries and to the health of the leather workers.[14] Most studies show that the crucial factor in determining international competitiveness is the ability to innovate successfully; applied in the right way, environmental regulation can encourage the process of innovation.

Although these arguments may be economically sound, they are nevertheless politically difficult. Many industrialists and politicians clearly believe that environmental regulation will damage competitiveness, and act accordingly. 'It may be that for every firm that migrates to escape regulation', stated a 1993 study, 'a score of others have weakened or prevented regulation by simply threatening to do so'.[15] There may be not so much a race to the bottom as a disincentive to race to the top. The fear of companies moving to low-standard countries may produce a 'political drag' or 'regulatory chill' on further efforts to improve standards in relatively high-standard countries.[16] By definition, this is difficult to measure, so there is little empirical data; but there is plenty of anecdotal evidence. The tax rebates proposed for energy-intensive industries in the European Commission's 1992 proposal for an energy/carbon tax, and the requirement that the tax should not be implemented unless the United States and Japan took similar measures, provide a classic example.

Competitiveness arguments may carry more weight as the growing evidence of environmental degradation leads to pressure for stricter environmental regulation, and also as trade liberalization increases competition in global markets and exerts greater pressure on profit margins.

Environmental regulation and the multilateral trading system

Does trade help or harm the environment? Trade liberalization can contribute to environmental sustainability, but will not do so *automatically;* appropriate policies must be

implemented to ensure that one objective is not pursued at the expense of the other. Equally, however, it is impossible to separate the two; trade and environmental policies are inextricably interlinked. The question becomes, therefore: when the two objectives of trade liberalization and environmental protection conflict, how are they to be balanced? And how in practice do current international regimes manage?

As described in Chapter 13, the central aim of the GATT is to liberalize trade between contracting parties (WTO members). WTO members are not permitted to discriminate between other WTO members' traded 'like products', or between domestic and international production. Successive GATT rounds have extended these principles to ever wider ranges of traded goods and services, and reduced tariff and non-tariff barriers to trade.

The GATT does permit, however, certain unilateral trade restrictions in the pursuit of environmental protection under particular circumstances. Article XX ('General Exceptions') states that:

> Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures:
>
> …
>
> (b) necessary to protect human, animal or plant life or health;
>
> …
>
> (g) relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption.

So although the GATT in general frowns on trade restrictions, countries can ban or restrict the import of products which will harm their own environments—as long as the standards applied are non-discriminatory between countries and between domestic and foreign production. As the GATT Secretariat expressed it in 1992,

> GATT rules place essentially no constraints on a country's right to protect its own environment against damage from either domestic production or the consumption of domestically produced or imported products. Generally speaking, a country can do anything to imports or exports that it does to its own products, and it can do anything it considers necessary to its production processes.[17]

The WTO Agreement on Technical Barriers to Trade aims to encourage international harmonization of product standards and to avoid their use as disguised protectionism. Under paragraph 2.2 of the Agreement, technical regulations shall not be more trade restrictive than necessary to fulfil a 'legitimate objective' -defined as including environmental protection. Environmental grounds have indeed become more widely cited

as an objective and rationale for applying trade-restrictive regulations including, most notably, measures aimed at controlling air pollution and hazardous chemicals.[18]

It would appear, therefore, that the GATT poses no threat to environmental regulation as long as it is applied in a non-discriminatory manner. In fact, however, there are two cases in which there *might be* a strong environmental justification for behaving differently: where processes, rather than products, cause the environmental damage; and in the enforcement of MEAs.

Process and production methods

The problem with trade restrictions based on environmental regulations derived from process and production *methods* (PPMs), as opposed to product standards, stems from the meaning of the GATT term 'like product'. This has become one of the most difficult issues in the trade-environment arena. Originally incorporated into the GATT in order to prevent discrimination on the grounds of national origin, GATT and WTO dispute panels have interpreted the term more broadly to prevent discrimination in cases where process methods, rather than *product* characteristics, have been the distinguishing characteristic of the product and the justification for trade measures. In the well-known US-Mexico tuna-dolphin dispute in 1991, for example, the dispute panel ruled that the trade restriction in question (the US import ban on Mexican tuna caught with dolphin-unfriendly nets) was in breach of the GATT because it discriminated against a product on the basis of the way in which it was produced, not on the basis of its own characteristics—that is, it discriminated against a 'like product'.

In 1994, another GATT panel, ruling on an EU-US dispute over car imports, slightly relaxed the definition, considering that vehicles of different fuel efficiency standards could be considered *not* to be like products. However, it placed strict boundaries on this conclusion, arguing that Article III of the GATT referred only to a 'product as a product, from its introduction into the market to its final consumption'.[19] Factors relating to the manufacture of the product before its introduction into the market were, therefore, still irrelevant. Similar arguments were deployed in the reformulated gasoline case (US restrictions on imports from Venezuela and Brazil on the grounds of the environmental standards of the refiners) and the recent shrimp-turtle case (a US embargo on imports of shrimp from a number of developing countries whose fishing fleets did not use turtle-excluder devices). In each case the panel found that the trade measures could not be justified by the exemptions clause, Article XX, generally because they were not necessary to the achievement of the environmental goal. The panels believed that there were less trade-restrictive (or less GATT-inconsistent) measures also available which should have been employed instead —though whether these would have been as effective as the measures actually employed was not examined.

It is worth noting, however, that the term 'like product' is nowhere defined in the GATT, and in other areas the distinction between products and PPMs is not maintained. Both the Agreement on Subsidies and Countervailing Measures and the Agreement on Trade-Related Aspects of Intellectual Property Rights regulate some

aspects of how goods are produced, allowing importing countries to discriminate against products if they are produced using excessive subsidy or misappropriated intellectual property. GATT's Article XX(e) allows countries to discriminate against products produced using prison labour. Furthermore, the GATT Secretariat's first (1971) report on trade and environment stated that a

> shared resource, such as a lake or the atmosphere, which is being polluted by foreign producers may give rise to restrictions on trade in the product of that process justifiable on grounds of the public interest in the importing country of control over a process carried out in an adjacent or nearby country.[20]

There is an important distinction to be made between PPMs which cause pollution which is restricted to the country of production, and those which cause pollution which is transboundary or global. In the former case, PPM-based environmental trade measures are certainly difficult to justify. Different parts of the world vary widely in their ability to assimilate pollution, depending on factors such as climate, population density, existing levels of pollution and risk preferences. Environmental regulations suited to industrialized nations, with high population densities and environments which have been subject to pollution for the past 200 years, may be wholly inappropriate for newly industrializing countries with much lower population densities and inherited pollution levels—and yet trade measures based on PPMs could in effect seek to impose the higher standards regardless. Carried to its logical extreme, enforcing similarity of PPMs could deny the very basis of comparative advantage, which rests on the proposition that countries possess different cost structures for the production of various goods. It is hardly surprising that many developing countries view the motives of those wishing to introduce this issue to the debate as protectionist. Another argument rests on practicalities. By their very nature, PPMs cannot generally be determined by inspection of the products. Importers wishing to apply PPM-based controls must therefore enjoy the co-operation of the exporting country or country of origin in certifying how the goods are produced.

Where the pollution is transboundary or global, however, the argument is quite different. Differentiating, as the panels' interpretation of the GATT effectively does, between pollution associated with the *consumption* of a product and that associated with its *production* is more difficult to justify, and would rule out any trade measure aimed at protecting a country's environment, or any aspect of the global commons, from damage caused by transboundary pollution originating from production. PPM-based measures are, furthermore, becoming increasingly important in strategies for environmental sustainability. Particularly where the use of energy is involved (as it is in virtually every manufacturing and processing activity), the pollution caused stems from the PPM and not the product. Life-cycle approaches, and eco-labelling schemes based on them, have similarly focused attention on the way in which products are manufactured, grown or harvested as well as on product characteristics themselves; indeed, the whole point of eco-labelling is to provide information on differences in characteristics between like products.

Inclusion of PPM-based trade measures in MEAs may provide a solution, and in fact the Montreal Protocol (on ozone-depleting substances) includes provision for such measures, though they have not so far been deployed. GATT and WTO panels have repeatedly stressed the desirability of multilateral rather than unilateral action; part of the panels' argument against the US action in the shrimp-turtle case was that the United States had not attempted to enter into negotiations on a potential multilateral agreement before it imposed the import ban.

The negotiation of international treaties is frequently, however, a difficult and slow process. A number of participants in the debate[21] havetherefore called for the GATT to be amended to set out objective criteria under which trade measures directed against PPMs could be taken (including requirements such as non-discriminatory and transparent measures and evidence of significant transboundary environmental problems), subject to challenge under normal GATT rules. In effect, this represents a redefinition of the term 'like product' in the context of a world in which environmental policy requiring the control of PPMs may justify trade policies which are not protectionist in intent but may look so when viewed from the perspective in which the GATT was written fifty years ago.

Multilateral environmental agreements

As Principle 12 of the Rio Declaration states, international agreement is clearly preferable to unilateral action in tackling transboundary or global environmental problems. Almost 200 MEAs already exist, of which about twenty incorporate trade measures. These include three of the most important: the Basel Convention on hazardous waste, the Convention on International Trade in Endangered Species (CITES), and the Montreal Protocol on ozone-depleting substances. In the absence of any comprehensive framework of global environmental law, the negotiation of further MEAs will form an increasingly prominent part of the international agenda.

Trade restrictions required by MEAs have been designed to realize four major objectives:

1 To restrict markets for environmentally hazardous products or goods produced unsustainably.
2 To increase the coverage of the agreement's provisions by encouraging governments to join and/or comply with the MEA.
3 To prevent free-riding (where non-participants enjoy the advantages of the MEA without incurring its costs) by encouraging governments to join and/or comply with the MEA.
4 To ensure the MEA's effectiveness by preventing leakage—the situation where non-participants increase their emissions, or other unsustainable behaviour, as a result of the control measures taken by signatories.

Effectively, therefore, these MEAs restrict trade either because the trade itself is causing the environmental damage, and/or as an enforcement measure, to ensure that the

agreement's objectives are not undermined by non-participation. The Montreal Protocol, for example, requires parties to ban imports of CFCs and other controlled substances from non-parties. On the face of it, this would appear to conflict with the GATT, since it discriminates between the same product imported from different countries on the basis of their membership of the Protocol. It is widely accepted, however, that the inclusion of this measure in the Montreal Protocol has contributed significantly to its success in attracting signatories.[22]

This topic became one of the most important items of debate on the CTE in the run-up to the Singapore WTO conference in 1996, with members putting forward proposals designed variously to define under what conditions trade measures taken pursuant to an MEA could be considered to be 'necessary' under the terms of GATT's Article XX, or to establish a degree of WTO oversight on the negotiation and operation of trade provisions in future MEAs.[23] No consensus was reached about the need for modifications to trade rules.

It is worth noting, however, that no complaint has yet arisen within the GATT or WTO with respect to trade measures taken in pursuit of an MEA, and this may well continue to be the case; in instances such as the Montreal Protocol, where the trade provisions were designed to encourage countries to accede, this has been so successful that there are virtually no non-parties left against whom trade measures could be taken in any case. On the other hand, it is quite likely that future MEAs—such as the convention on persistent organic pollutants or the Kyoto Protocol on climate change—may benefit from the inclusion of trade restrictions. It is obviously desirable that negotiators are not inhibited from discussing them by the fear of a potential GATT challenge, and in a number of instances countries opposed to the aims of the MEA in question have attempted to do just that. A resolution of the issue, of the clash between two international regimes each of which is valuable, is therefore highly desirable.

Institutions and politics

Effectively the CTE's discussions on the relationship between MEAs and the multilateral trading system revolved around the question of which legal regime—the GATT or the MEA—should be superior. Those opposed to modifying the GATT frequently complained that what was being sought was the creation of a hierarchy of international agreements, with MEAs superior to the WTO, or at least to part of it. The particular fear of developing countries is that this approach may weaken the WTO and help erect, or maintain, trade barriers against developing country exports. As Egypt's main negotiator put it:

> Developing countries have shown and proven their interest and their positive approach towards the protection of the environment. What they have argued against is the inclination of some to use environment as a protectionist device. The latter's attempt to portray developing countries as being hostile to the environment is more for the purpose of concealing their real intentions: to use environment as a

> means of disguised protectionism, to legitimise inconsistent trade measures within the WTO and to undermine multilateral cooperation, together with the inclusion of positive measures as agreed by the international community in the Earth Summit in Rio.[24]

Although this may appear to be an exaggerated concern, particularly in the context of MEAs, the history of protectionism against developing countries, and the presence of protectionist elements in several unilateral trade measures taken for ostensibly environmental purposes,[25] lends some credibility to this attitude.

The problem, of course, is that what the opponents of GATT amendment were arguing for was in effect precisely the reverse, that is the creation of an implicit hierarchy of international agreements with the WTO superior to MEAs. Many of the proposals put forward during the CTE discussions proposed additional criteria which trade measures in MEAs should meet—including, for example, 'effectiveness', 'proportionality', 'least-trade restrictiveness', and so on, concepts largely derived from arguments used by GATT and WTO dispute panels in the relevant cases. WTO panels would judge, for example, whether a particular environmental measure was effective, and, if so, how effective; and also whether there were other environmental policy measures that could have been pursued that would have been as effective but less trade restrictive—or, conceivably, less effective though also less trade restrictive.

Although it is open to panels in disputes raising environmental issues to seek advice from appropriate expert sources, there is no *requirement* that this should be done (though it is becoming more common, for example in the recent shrimp-turtle and beef hormone disputes) or that the panellists themselves should have any environmental expertise. Furthermore, dispute panels have in general ignored the political and social context in which regulations are set; it is conceivable, for example, that a panel could decide that market-based instruments such as taxes or tradable permits would be less trade restrictive than command-and-control regulations, even though the national legislation under challenge might have no experience with and no framework for such policy measures. Or, they could ignore political realities; the first tuna-dolphin panel, for instance, while finding against the US trade restrictions partly on the grounds that multilateral agreements would have been preferable, seemed entirely unaware that the United States had been attempting to negotiate just such an agreement since 1972. The danger of the creation of this hierarchy lies in the power it would give to a trade organization, the WTO, to rule on matters that are in practice outside its remit and expertise. In practice, this is more or less the current position.

An alternative approach is to create some kind of superior balancing mechanism. This is effectively the system that operates inside the European Union, where trade liberalization and environmental protection are both objectives of the Treaty of Rome. Any conflict between the two objectives can be resolved by the European Court of Justice, which has the power to rule on the appropriate balance between trade and environmental measures in any particular case—for example, in the Danish bottles dispute of 1986, where the Court upheld the core of the Danish law requiring a

collection system for drinks containers while striking down some of the details of the regulations as unnecessarily trade restrictive. The creation of an equivalent balancing system at a global level would of course require substantial reform of the entire system of international institutions, and is not a realistic prospect for the foreseeable future. Having said that, there have been calls for such a reform, perhaps using the International Court of Justice as the superior body, and recent proposals for a new World Environment Organization (for instance by Chancellor Kohl at the UN General Assembly Special Session, 'Rio Plus Five', in June 1997) have had the objective of creating a balancing institution to the WTO at least partly in mind.

In the absence of such an institution, the trade—environment debate seems likely to continue much as it has done in recent years, with the main focus continuing to rest on the CTE. It is difficult to believe, however, that future discussions in the CTE will ever proceed much further than the current impasse. One major problem is that most participants in the CTE, particularly those from developing countries, are drawn from a trade perspective and background, and in general trade liberalization is a more important objective for most governments than environmental protection. The shared values, assumptions and operating modes of such a group provide a powerful underlying momentum in the direction of further trade liberalization, and against any measure which is seen as running counter to this trend, whether or not it is properly understood. The environmental argument is thus weakened before it is even put forward.

A more fruitful way forward may be the inclusion of particular proposals, such as a GATT amendment on MEAs, as one element of a package of measures of benefit to the causes of trade liberalization and development as well as environment (such as, for example, the further liberalization of trade in agriculture)—adopted as part of the proposed Millennium trade round. If the political will is there, it should not in principle be impossible to resolve the conflicts inherent in the pursuit of the two desirable objectives of trade liberalization and environmental protection.

Notes

1 United Nations Conference on Environment and Development, Agenda 21, Chapter Two, Section B.
2 WTO: Trade and Environment Decision of 14 April 1994.
3 David Wheeler and Paul Martin, 'Prices, policies and the international diffusion of clean technology: the case of wood pulp production', in Patrick Low (ed.), *International Trade and the Environment* (Washington, DC: World Bank, 1992), p. 214.
4 See OECD, *Foreign Direct Investment and the Environment: An Overview of the Literature* (Paris: OECD, March 1998), pp. 5–6.
5 OECD, *Foreign Direct Investment and the Environment,* p. 6.
6 Gene M.Grossman and Alan B.Krueger, 'Environmental impacts of a North American free trade agreement', in Peter M.Garber, *The Mexico-US Free Trade Agreement* (Cambridge, MA: MIT Press, 1993).

7 International Institute for Sustainable Development, *The World Trade Organisation and Sustainable Development: An Independent Assessment* (*Winnipeg:* IISD, 1996), p. 1.
8 Robert Cullen, 'The true cost of coal', *Atlantic Monthly* December 1993, p. 38.
9 See Paul Ekins, *The Kuznets Curve for the Environment and Economic Growth: Examining the Evidence* (London: Birkbeck College, 1995 (mimeo)).
10 H.Jeffrey Leonard, *Pollution and the Struggle for the World Product* (Cambridge: Cambridge University Press, 1988).
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25 For example, the US tuna import embargo in the tuna-dolphin disputes was determined partly on a retrospective comparison of the US fishing fleet's dolphin kills with those of the exporting countries' fleets—that is, it was impossible for the exporters to know in advance what target they were supposed to aim for. It is difficult to regard this as anything other than straightforwardly protectionist.
26 Charnovitz, 'GATT and the environment: examining the issues', p. 207. In fact, the US ban on tuna imports subsequently stimulated progress on reaching such an agreement, finally signed in February 1998 (see 'Agreement reached to end longstanding tuna-dolphin dispute', US Information Agency, *Press Release* 9 February 1998).

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Part II

Actors and processes

Introduction

As the trade agenda has become more crowded, so the cast of actors involved in international trade politics has become larger. It has become commonplace to conceive of the state as an actor that is steadily losing political ground to other actors such as firms, non-governmental agencies, or supranational bodies like the World Trade Organization (WTO). The state is by no means being eclipsed by these new actors; no other form of political or economic organization rivals it in terms of public legitimacy or in the capacity to coerce compliance from civil societies. Rather, the picture is one of states—the primary actors in international trade—increasingly finding that other voices can have an important influence in the conduct of international trade politics. The aim of this part is to explore these newcomers to the international scene and their relationship to the more 'traditional' players.

Firms have always played an important role in the development of trade policies. As McGuire's chapter explains, the state-firm relationship continues to be one of mutual dependence. The state needs the employment, technology and investment that firms bring, while firms themselves recognize that government has a key role to play in the provision of public goods underpinning competitiveness. Jan Aart Scholte's chapter explores the rise of civil society—here conceived of as an umbrella term for a variety of NGOs—as an influential force in world trade. While some observers may view this development as an intrusion of self-interested groups into a state-based multilateral forum, Scholte reminds us that the legitimacy of the multilateral system is at risk if it is perceived as acting contrary to the interests of society.

Cloutier's chapter provides an interesting blend of old and new trade politics. In this case, the new issue of environmentalism is manifest in the EU's waste packaging policies. Cloutier analyses with special attention paid to the interaction between government and interest groups. Pigman's chapter explores an issue that lies at the heart of any discussion of the relationship between states and supranational organizations like the WTO: the issue of sovereignty. Pigman concentrates on the US ratification of the Uruguay Round agreement to explore the conflicting views about the constraints and limitations on state action that are posed by the increasing regulation of the international trading system. Finally, Robert Wolfe provides the reader with an overview of the development and operation of the WTO.

Chapter 9
Firms and governments in international trade

Steven McGuire

This chapter seeks to understand the interaction of firms and states in the development and conduct of international trade policy. The steady, if geographically uneven, internationalization of business can be seen as a key development which has profoundly altered the content and conduct of firm-state relations. The growth of multinational enterprises (MNEs) and, now, international strategic alliances is significant for trade relations because it demonstrates the importance of technological development and changing patterns of production for changes in trade preferences of firms. Firms now confront government with a bewildering array of policy demands, many of which would not strike someone as having much at all to do with trade politics. What is distinctive about these policies is the degree to which they centre on domestic arrangements of states rather than on external economic policies. Modern trade politics is as much about what goes on inside states as between them. Trade policy now is a bundle of industrial and regulatory policies and this has brought firms and states into new types of interaction over new issues.[1] In contrast to earlier decades where there was a clearer distinction between the outside world of trade and the inside realm of the domestic economy, industrial policy questions are now inextricably bound up in trade issues. A state's industrial policy can be an important element of trade politics because it implies an effort on the part of the state to alter market outcomes. Thus, firms' competitive prospects in the international economy can be shaped by state policies. The link between corporate activity—whether it be inward investment, trade or acquisition—and regulatory regimes, whether national or international, is very tight. Moreover, it means that firm-firm activity, such as a merger, can now occur simultaneously with a government-government negotiation about the revised regulatory regime to cope with the putative corporate arrangement. Thus, international trade matters are less and less about 'trade' as conventionally defined. Rather they are about the complex interplay between corporate strategies and government regulatory regimes. Thus, it is misleading to say that firms simply demand an ever more deregulated marketplace. True, liberalization has been the predominant theme of political economy in recent years. However, in many ways the international economy is more, not less, regulated than ever; more areas of business activity are coming under national or supranational scrutiny. Intellectual property protection, health and safety standards, to say nothing of competition policies, were not on the trade agenda thirty years ago; now they are.

That firms have preferences on commercial matters is neither new nor controversial; both the international political economy and the public policy literature provide important insights into firm activity on particular issues. Much of international political economy (IPE) work on multinationals explored the extent to which firms ruthlessly exploited a state's need for the economic benefits that firms bring.[2] While this critical view of the MNE concentrated on firms' relations with developing states, the critique was also applied to the developed world. A more nuanced view of firm activity accepts that multinationals can exploit their relationships with state authority but also argues that firms can also depend on governments for a great deal. This view arises from the observation that firms are not borderless entities which lead a nomadic existence in search of the lowest tax rates, the most lax labour standards or the most liberal pollution regulations. Instead, the 'home base' of a firm can provide key competitive ingredients in the form of education systems, tax incentives for research and other policies.[3] For example, Germany's excellent vocational training proved very important for the development of Germany's engineering sector; American leadership in computers owes much to US defence spending and excellent research universities.

An interesting question concerns the degree to which MNEs are developing a political role quite independent of states, and could be seen as emerging rivals to states in the international system. Firms have always been political actors; their control over resources always gave them input into government policy. However, some scholars argue that the international system is now characterized by a multiplicity of actors, where states are only one source of power. The ideological ascendancy of economic liberalism has seen states come under pressure to offload a variety of governmental functions onto private or quasi-private actors. This has led to work examining the rise of private regulatory regimes. This privatization of the international system should not be overstated, but the thrust of the argument—that firms play a crucial role in the shaping of international trade politics and state-centric views cannot grasp the dynamics of the process—is powerful.

When international trade was truly about trade between countries, the firm-state relationship revolved around protection of the home market. The policy process revolved around the question of what tariff rate was needed to sustain domestic producers. Essentially, this was the model of late nineteenth-and early twentieth-century trade politics when trade, as opposed to investment, was the important feature of cross-border commerce. Firms were largely confined to their home markets, although this period did witness the birth of the multinational corporation. As a result, trade politics was about tariff protection for domestic firms. However, tariffs were to lose their centrality to trade politics; protectionism of the late 1920s was widely regarded as having caused the Great Depression and, indirectly, World War II as economic collapse spurred the rise of fascist parties in Europe and elsewhere. After 1945 a generation of political leaders emerged and, with the ruinous consequences of the 1920s fresh in their minds, pressed for a liberalization of international trade. The vehicle for this liberalization, the General Agreement on Tariffs and Trade (GATT), enjoyed an astonishing track record of reducing tariffs. In a series of multilateral

negotiations—rounds—held in the 1960s and 1970s, the average tariff in industrialized countries was cut dramatically. By the time the Tokyo Round negotiations concluded in 1979, tariffs had ceased to be much of a policy concern.

As firms become more engaged in the international system—when their corporate strategy changed to embrace exports—their trade policy preferences likewise shift. In general, it is observed that firms come to advocate an open international trading system. A tariff-free system clearly benefits large exporters—it makes their products cheaper in export markets. It is important to underline that firms do not merely advocate the liberalizing of foreign markets; export dependence pushes firms to advocate free trade as the policy for their home base as well. It is not immediately clear why this would be the case since the ideal situation for an exporter would be to have tariff-free foreign markets yet remain safely behind barriers at home. However, these firms have to consider that foreign markets might only be freed up, or remain liberalized, if the same liberalization applies to all countries, including the home base. Firms would have to worry that if their home market does not opt for liberalization, foreign markets may be closed off in retaliation. Helen Milner's work provides the best illustration of the shift in corporate trade preferences that flow from firm dependence on exports. She shows how, in both the United States and France, industrial sectors typically associated with protectionism altered their behaviour over time. The process was not quick but, as a sector came to export more, it saw advantage in advocating free trade.[4]

Internationalized production—the domestication of international trade

The salience of firm preferences for free trade had, to a large extent, diminished by the early 1990s. This reflects the reality that tariff barriers have ceased to become an important issue in international trade. However, other government instruments that affect exports remain in place in the form of a myriad of non-tariff barriers (NTBs). These include such policies as government procurement regulations that favour domestic firms over foreign ones, or national standards which disadvantage importers. These matters were placed on the international agenda by the United States, which by the 1970s was seeing its dominance of the international economy eroded by Japan and the European Community. Moreover, the economic strains induced by the 1973 oil crisis provided many countries with an excuse to erect a variety of trade barriers, a process known as the 'new protectionism'.

The Uruguay Round has not stopped firms from claiming that foreign states and firms do not 'play by the rules'. This woolly—yet widespread—perception that rival firms benefit from government-sponsored policies of support shapes firm policy preferences in favour of a complex mix of deregulation and intervention. The policy package is designed to enhance the competitive position of home firms by providing them with intangible assets needed for international competition and relatively open markets to exploit this asset. Thus, the traditional division between trade policies and industrial and technology policies is eroding quickly. The same can be said about a

number of other policy areas, particularly taxation, competition, and health and safety regulations. Ostry has suggested that we might come to a situation of almost absurd dimensions where virtually all areas of national economic policy come to have a trade dimension.[5] We are not there yet (and may never get there) but there is a growing realization that domestic economies are more deeply affected by trade issues than ever. The expanding and increasingly complex trade agenda can be grasped by examining, first, the rise of regulation as a trade issue, and, second, the rise of the 'knowledge economy'.

The politicization of regulatory regimes

A key aspect of firm-state trade relations is the extent to which trade negotiations are focusing on the conflicts between differing methods or conceptions of regulation. Again, this is a function of the interpenetration of domestic and international political economies. As firms move abroad, they are confronted with new types of regulation, as well as different conceptions about the role of regulation. Compliance with various types of regulations represents a transaction cost; firms have an incentive to minimize these costs whenever possible. Firms may view regulation as another type of NTB where the intent is to protect a home market from imports via arbitrary bureaucracy. Bringing national forms of regulation onto the international trade agenda may from a firm's perspective be quite sensible, but international regulation strikes at the very heart of state autonomy and sovereignty. As Mattoo and Subramanian note, securing compliance with multilateral trade rules, while preserving the ability of states to pursue domestic political objectives, is a central issue for the WTO.[6] Broadly, globalization has resulted in a creeping multilateralization of regulatory issues. This process is uneven and should not be overstated, but increasingly national authority is contested and states face pressures to alter their regulatory practices. But multilateralization is itself fraught with difficulties, not least of which concerns *how* to make different regulatory regimes compatible. This is why international trade is seeing an increase in the number of regulatory regimes, rather than a settlement on one type.

Nationally based systems can operate as trade barriers, although only states which are not WTO members enjoy the full extent of this freedom. WTO members, by contrast, can have their regulations subjected to the WTO dispute settlement process. National treatment is a cornerstone of the WTO system, but the extent to which states will actually refrain from discriminatory regulatory practices is uncertain. If a state feels that it is vulnerable to international economic activity, it might resist application of national treatment in regulatory matters. The WTO's power to discipline regulatory matters is considerable, but nonetheless limited. It can only take action after a complaint from a WTO signatory (i.e. the WTO cannot self-initiate cases) and it can only tell the offending state that its regulations violate its WTO obligations; it cannot dictate the form or content of national regulations.[7]

Mutual recognition is the process whereby states agree that, if a product or service satisfies regulatory authorities in one state, it satisfies them for all other parties to the mutual recognition agreement (MRA). This mode of international regulation is a

feature of the European Union's Single Market, but has been applied to European-American trade relations through negotiations for a series of transatlantic MRAs. MNEs were heavily involved in the initiative to lower transatlantic regulatory barriers and this reflects business's view that regulations represent costs that should, where possible, be limited. The Trans-Atlantic Business Dialogue (TABD) was created as a vehicle for MNE interest in the talks and the deep involvement of private sector actors in the process is a signal characteristic. One TABD official justified the early and extensive MNE involvement on the grounds that, rather than wait for the inevitable regulatory squabbles, business could help solve problems before they arose by 'attempting to set the regulatory agenda'.[8]

Mutual recognition can go some way to reducing firms' concerns about the costs of complying with multiple regulatory regimes. For a pharmaceutical firm, for example, the ability to certify a drug only once, not two, three or ten times, has obvious appeal. But it is not clear whether the MRA approach can have wide applicability. Arguably, the MRA process works in the EU-US context because the two regulatory regimes are already highly compatible; what disagreements there are occur at the margins. But would an MRA work between two states where one, for example, has an extensive intellectual property regime while in the other it is virtually non-existent? It is worth noting that the EU has, or is negotiating, MRAs with only six states (Japan, the United States, Canada, Australia, New Zealand, Switzerland), all of which are advanced industrialized states.[9] This is a challenge for trade politics: how do you go about devising a system that is suitable for a myriad of legal systems, cultures and economic policies?

Such difficulties would bedevil efforts to develop supranational regulatory regimes as well. However, that has not stopped some observers from arguing that increased supranational regulation is the best option for both firms and states in the globalized economy. Proponents of this view argue that as firm operations become ever more global, issue areas like competition policy essentially 'leave the reach' of national regulators. This is because an increasing number of industries are truly global; that is, the competitive position of the firm cannot be sustained in one market alone, but depends on its performance in several markets. This may be due to high fixed costs for research and development (R&D) (commercial aircraft, pharmaceuticals) or production (automobiles, oil and gas), which cannot be recouped in a national (or regional) market alone.[10] This dependence on numerous markets can provide firms with an incentive to argue for the creation of supranational regimes as the simplest means of reducing the costs associated with contesting a global market. However, it is not clear that firms are clamouring for increased supranationalism. Supranational regulation will be most welcomed by firms if it accords closely with their preferred, national style of regulation. Thus, American firms are not likely to accept international competition rules heavily influenced by, say, Indian or Chinese firms. Likewise, should the United States recover its appetite for multilateralism in the form of increased scope for the WTO, foreign firms and governments will be alert to the creation of international rules which seek to 'lock in' American conceptions of

regulation to the benefit of American firms. In short, a 'who's standard?' problem could confound any effort to agree a supranational framework.

Foreign direct investment

Foreign direct investment provides a useful illustration of the degree to which globalization raises questions about regulatory issues. The rapid growth of foreign direct investment (FDI) has been an important feature of the international economy in recent years and provides an interesting example of how national regulatory regimes can come under pressure. As Ostry notes, FDI growth has outstripped the expansion of trade: 'Between 1985 and 1995, FDI outflows increased by nearly 20 per cent, twice the rate of growth of exports or output'.[11] The inclusion of FDI as a trade issue could seem incongruous since FDI has been historically treated as a substitute for trade, not part of it. However, a linkage between trade flows and investment has developed for two reasons. First, a proportion of trade consists of intra-firm transfers of goods and services. For the United States, 'nearly half of manufacturing exports and over 60 per cent of imports flow within the multinational firms'.[12] More importantly, inward investment arises from the need for firms to have a presence in the developing regional economies. Regional arrangements like NAFTA or the EU place greater barriers to imports than to foreign companies operating within the region under 'national treatment' regimes. Thus, firms prefer to invest rather than export. Even in parts of the globe that lack an institutionalized regional arrangement, firms still regard a presence on the ground as preferable to arm's-length investment such as portfolio investment. A reason for preferring market presence to portfolio investment is to gain access to foreign technology, a matter that will be discussed in greater depth below.

Critics of MNE activity argue that firms can and do exploit host countries' needs for investment and their resources. Firms play off one state against another in a competition to offer the firm the most attractive package of inducements. These inducements can include very liberal labour regulations, public subsidies in the form of tax breaks or relaxed planning permission. Yet even these incentives may not keep a firm rooted to the locality; another jurisdiction can tempt it away with a still more lucrative package. Thus the incipient threat of relocation keeps wages low and maintains a regulatory environment that is MNE-friendly. Moreover, MNEs maintain control over their technology and so do not transfer know-how to the host state's economy. These latter criticisms are increasingly seen as misplaced, even in developing states that were regarded as the most vulnerable to MNE exploitation; however, the problem of inducements cannot be so easily dismissed.

Traditionally, FDI was rationalized simply because of the employment the investment generates. The UK has aggressively sought inward investment—particularly in high-technology industries like semiconductors—as a means of replacing declining sectors such as shipbuilding and coal. In recent years, the UK has attracted about one-third of all FDI going to the EU and in 1997 a record 46,179 jobs were created.[13] However, there is growing awareness of other benefits brought by inward investment. Proponents of inward investment argue that foreign firms bring

significant benefits by contributing to economic stability and technological advancement. Portfolio investment can leave domestic economies vulnerable to capital flight; it is easy for investors to withdraw their cash. In the case of FDI the commitment of the MNE is manifest in the location of personnel and plant: '[I]nvestors are both less likely and less able to flee at the first sign of trouble'.[14] Firms can sink roots into the local economy, diffusing skills and technology.[15] The Asian NICs, for example, made very effective use of inward FDI as a mechanism for diffusing technology through the economy.[16] Even developed economies like the UK and Canada have seen that FDI can act as a *de facto* technology policy, either replacing declining domestic industries or acting as competitive spurs to home firms.

However, as more and more states seek to utilize FDI as key development policy, *how* states do this has become a trade issue. Essentially, if states jockey with each other for investment, a situation could arise where a ruinous international competition develops. In this game of 'regulatory arbitrage', a state may offer an exceptionally attractive package to lure inward investment away from another state.[17] In this situation there are, in fact, two welfare considerations. Inducements may divert investment away from where it is really needed and taxpayers may find that their government has paid over the odds to attract the FDI.

In May 1995, the OECD initiated a negotiation among its members on an international regime designed to regulate FDI. The process was called the Multilateral Agreement on Investment (MAI). The MAI negotiations had three aims. First, to lock in the process of liberalization for FDI. Second, the agreement was intended to provide greater protection for investors by developing international rules and a dispute settlement procedure. Finally, it would curb the use of subsidies and inducements to regulate state competition for FDI.[18] Although the OECD-led process seemed only to confirm fears that the MAI negotiation was an effort to increase developed countries' hold over the global economy, developing countries could benefit from an investment regime. Robust international rules should encourage firms to locate more investment in developing states because of a reduced fear about arbitrary government policies.

The MAI talks stalled in early 1998, in part because of state concerns that the agreement represented too much of an extension of corporate power into national decision making. Moreover, non-governmental organizations also mounted effective opposition, arguing that the MAI represented a dangerous extension of business's regulatory agenda at the expense of other, non-market considerations. However, it is unlikely that the regulation of FDI can be forestalled indefinitely. Firms themselves are increasingly aware of the transaction costs associated with FDI and seek to minimize these through an expanded voice on trade matters. NAFTA, for example, allows individual firms to sue governments for alleged violations of trade agreements. This ability of firms to act in a private capacity, rather than petition their home government to bring a complaint, was held up as a model for the MAI.[20] The old model of FDI had an MNE locating important functions, such as research and development, in its home base. It thus minimized the risk associated with the loss of an overseas affiliate with political or economic instability. This is changing, however,

as some firms operate an ever more spatially diffuse operation where R&D facilities can be located in several countries aside from the home base. Countries have long craved getting these high-value-added facilities as part of inward investment. But the price to be paid is more formal regulation and guarantees to the firms that their investments will be safeguarded. In short, a more stringent FDI regime including an enhanced legal status for firms—seems an inevitable price to pay for the continued expansion of inward investment activity.

The importance of the 'knowledge economy'

In many states industrial policy used to be about propping up declining industries such as steel or shipbuilding. Governments would pour billions into sectors in a vain attempt to save them from falling victim to international competitive pressures. In this guise, industrial policy is a backward-looking, defensive response to changing international economic conditions. Competitiveness policy, in contrast, is underpinned by a faith in new technology. As such, it attempts to develop and encourage sunrise industries such as semiconductors, aerospace and biotechnology as well as service industries like banking.

Thus, technology has become an important element in any discussion of international commercial relations. In part this is because the economies of leading states are more 'technology intensive': that is, a higher proportion of their output is accounted for by high-technology industries or service sectors that make extensive use of information technology. The OECD calculates that in 1993 some 25% of OECD manufactured exports are high-technology products, up from 17% in 1980.[21] Trading success is more and more built, not on formal protection in the guise of tariffs, but on the competitive advantages conferred upon the firm by it own, or its government's, effort. This effort can include the creation of new products or processes which rely on technological development.

The notion that technologically advanced (or knowledge-based) sectors are better for the national economy has become popular and politicians feel that their state must develop indigenous high-technology sectors as a motor for economic growth. High-technology manufacturing is considered less prone to competition from low-wage economies owing to the enormous expense of research, development and production. It is also thought to offer spillover benefits to the domestic economy. Many political leaders would agree that a state can best improve its standard of living by developing what Porter has termed 'structurally attractive industries'.[22] Thus, state policies in recent years have moved towards a complex mix of deregulatory policies as well as more interventionist ones. These 'innovation' or 'competitiveness' policies seek to accommodate a firm's need for an open, dynamic market with its need for a public infrastructure capable of supporting the firm's innovative activities.

Provision of infrastructure

This public infrastructure must be capable of supporting technologically advanced product development. This requires investment in human capital and research and development.

As industries become more technologically intensive, they need more educated and intelligent workers. Knowledge is an intangible asset; it cannot be held or observed as tangible assets like machinery can. A pharmaceutical or biotechnology firm relies to a great extent on the talent of its research scientists. Investment banks often rely on 'star' bankers to generate both profits and publicity for the firm. If they are not able to generate new products, the firm founders. Thus, these firms need to recruit—and retain—talented people. Unsurprisingly, governments have faced increasing pressures to improve the general educational levels of their workforces. New growth economics appears to provide considerable empirical evidence to support the view that states which invest more in education enjoy higher rates of economic growth than those that fail to make this investment.[23]

Apart from concern about education infrastructure another policy demand is for the maintenance of government-sponsored research and development, as well as money to upgrade plant and machinery. Firms object to any suggestion that governments ought to get out of the business of funding such work. A number of incentives are at work here. The first is simple self-interest: firms, like individuals, would always prefer to spend someone else's money rather than their own. Clearly any winding down of government research spending implies that firms wishing to remain competitive must rely on their own resources. Second, firms argue that, since their overseas rivals do receive government research support, it would be irresponsible of their own government to withhold the same assistance to them. In spite of the apparent ascendancy of free market economics—which views any government support for business with some suspicion—state support for research and development remains a durable feature of government expenditure. However, government-sponsored research programmes can be, and are, still rationalized on the grounds of market failure—so that obstacles to private investment (such as long payout periods or appropriability problems) will result in underinvestment in necessary and potentially lucrative sectors. For example, the US government is supporting R&D designed to lower the cost of launching commercial payloads into space. Depending on the type of technology developed, the costs will run into billions and this investment would take years to recoup. Unsurprisingly, private investors may shy away from this type of investment, but since the funding holds out the possibility that the Americans may develop a competitive edge in an emerging technology, the state is provided with a rationale for action.

Scope for trade conflict

In an industry where the first-mover advantages of pioneer firms may be durable, government interventions in support for local firms, such as tax incentives or R&D funding, may be vital in ensuring that domestic firms win out over foreign rivals. Trade is seen as a zero-sum contest between economies where a gain for one implies a loss for another. Governments are tempted—or are urged by firms—to develop industrial policies that will allow these firms to vanquish the international competition. Foreign states cease to become trading 'partners' and become trading 'competitors'.[24] Strategic trade theory,

developed in the early 1980s to analyse competition in imperfectly competitive markets, appeared to offer politicians and business leaders an intellectually defensible case for greater government intervention on behalf of firms. Imperfectly competitive markets offer the promise of economic rents accruing to the firm (and its state) that succeeds in gaining a first-mover advantage in a sector. The Wintelist school of international political economy offers a related rationale.[25] Drawing its inspiration from Microsoft's 'Windows' and the Intel Corporation, Wintelism argues that, in certain industries at least, standard setting is the key to market dominance. Windows dominance in the software market is explained by the tendency of the standard setter to crowd out competing products. Where interoperability is key, the pressure for user groups to adopt one brand over another means that the favoured product gains enormous market share. In this environment, government support for firms can be a catalyst for such standard-setting behaviour.

To the extent that innovation policies are designed to bolster the competitiveness of domestic firms at the expense of foreign rivals, they can produce trade conflict. Japan's postwar success has been ascribed to the sophisticated use of industrial policy first to establish Japanese firms in various sectors and then move them into commanding positions in international market shares for medium-and high-technology goods. Much of the trade friction between the United States and Japan during the 1980s grew out of American perceptions that Japan had targeted sections of American industry, notably semiconductors, automobiles and supercomputers. The chronic US trade deficit with Japan resulted from the successful prosecution of industrial targeting by the Japanese. The impact of these policies has been well detailed, and debated, in the American political economy literature.[26]

The intense American concern with foreign trade policies is indicative of the asymmetry apparent in the global political economy. The United States with its vibrant technological base is bound to be the benchmark, indeed the target, for the industrial policies of other states. It is instructive to note that this 'targeting' debate largely revolves around two countries with greater capacity for technological autarky than most: Japan and the United States. Japanese firms do show a greater reluctance to develop alliances than American or European firms, and their trading patterns show a greater propensity to engage in inter- rather than intra-industry trade.[27] Among industrialized states, intra-industry trade—trade in similar goods—is a significant feature. The implication that is sometimes drawn from Japan's relatively low levels of intra-industry trade is that the Japanese target industries and seek to eliminate competition rather than share out market niches—as would happen in intra-industry trade. Japanese firms prefer export strategies and, when that generates conflict with the importing state, use FDI to avoid trade sanctions like anti-dumping actions. Even if one accepts this explanation for American-Japanese trade friction, its applicability for other trade relationships is limited. For many other countries, thoughts of dominating an industrial sector via targeting are sheer fantasy. What is important is to offer enough support so as to allow domestic firms to gain reasonable success on the world market—often by participation in alliances and other co-operative arrangements (discussed below).

Scope for trade co-operation

Although they can provoke trade conflict, knowledge-based sectors simultaneously provide a basis for firm co-operation, rather than rivalry. Technology complicates life for the firm as the increasing complexity of production overwhelms the firm's organizational capacity. In this circumstance, the firm cannot remain a master of all aspects of its product; increasing specialization requires a greater reliance on expert subcontractors and suppliers. Thus modern technology exhibits a tendency to generate *interdependencies* among firms and for the firm itself to become less a hierarchy than a network of interacting units. As products become more complex, and the process of developing them more uncertain, firms which try to be a master of all trades find themselves unable to cope. The civil aircraft industry provides a good example of this phenomenon. Major firms like Boeing, Airbus or even smaller players like Bombardier recognize that, while they do indeed build the airliner, the process is rather more complex than that. These firms are in essence brokers or chief negotiators who, in addition to adding their own technological assets, essentially co-ordinate a design and construction effort involving dozens of firms. Indeed, the programme management skills implied in this role are themselves valuable competitive assets in modern defence contracting. A similar development is seen in the computer industry where products are the result of co-operation among a network of firms even if the product is branded as one company's work.

This increased technological sophistication and the pressures on the firm that it implies have led to the development of a new form of corporate organization, the international strategic alliance (ISA). ISAs represent an important development in the international political economy and are concentrated in high-technology industries like biotechnology, aerospace, advanced materials and electronics, as well as in service sectors like law and airlines. Alliances are co-operative arrangements between two or more firms. Each firm brings a specific asset—technology, production skills and market access—into the arrangement. What distinguishes them from other types of firm co-operation is their global scope. Partners are selected on the basis of their contribution to the global strategy of the firm.[28]

These alliances are proliferating, especially among the advanced industrialized states which possess the necessary technological bases. Dunning notes that American firms concluded over 2000 agreements with European firms in the late 1980s[29]. This was doubtless due to the creation of the Single European Market in 1992. American firms, as well as Japanese MNEs, shifted strategies in anticipation of the SMP. Trade became less important than obtaining a presence in the European market, both via FDI and, in some technological sectors, via ISAs. However, the proliferation of alliances among the Triad does not merely reflect the need for a presence in regional markets like the EU. For European firms, alliances with some American companies also reflected the need to tap American technologies in areas of relative European weakness such as biotechnology. Networks of firms obviate the need for a firm to master numerous technologies associated with the product: it can instead concentrate on what it does best and 'trade' that asset for those of other firms. Alliances are not

replacements for FDI; they are one more element in the corporate strategies of internationalized firms.

If firms wish to participate in technologically based ISAs, then they have to have something to offer, some competitive asset which makes them valuable to prospective partners. This, in turn, places pressure on the firm to invest more in R&D, either by drawing on its own resources or by a combination of these and public sector funding. Firms argue that, in the absence of an effective national research base, their opportunities in the international trading system will be compromised. This implies state support for R&D through a variety of sources such as universities, government research laboratories or a variety of subsidy programmes designed to encourage the development of firm-specific technological advantages that can be transformed into greater market share.

The political problem that arises from innovation policies is that economic and technological pressures produce a conflicting set of incentives for policy makers—and firms. On the one hand seizing the technological high ground via a nationally based innovation policy can be very attractive as it would provide those home firms with significant competitive advantages. This is the argument made by the Wintelist school: where standard setting is vital, then government intervention can be key. The counter argument is that international business relies more and more on networks of firms and is underpinned by an essential interdependency. This situation requires an open market for technological co-operation among firms. Trade policy outcomes should preserve that ability of firms to tap foreign markets. Discriminatory innovation policies threaten this access and should be avoided.

Conclusion

Trade politics is no longer about goods that arrive at the dock of a country and are sold to its consumers. The growth of international business has brought about a new type of trade politics where firms are concerned with the domestic arrangements of states, and this produces a variety of conflicting pressures on policy makers. On the one hand, incentives for economic openness flow from the advantages to be gained from welcoming FDI and in seeing your domestic firms tap foreign markets in search of new technologies to enhance their competitiveness. However, on the other hand the possibilities of seeing domestic firms capture first-mover advantages and dominating key industries (whatever they might be) can prove irresistible for politicians and business leaders. Thus, it is simplistic to view contemporary firm-government relations as a simple effort to deregulate the international economy. Rather a complex process of deregulation, regulation and selective government intervention is evident.

Notes

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2 Alan Rugman and Alain Verbeke, 'Multinational enterprises and public policy', *Journal of International Business Studies* 29:1, First Quarter 1998, p. 117.
3 Michael Porter, *The Competitive Advantage of Nations* (London: Macmillan, 1998), pp. 126–8.
4 Helen Milner, *Resisting Protectionism: Global Industries and the Politics of International Trade* (Princeton, NJ: Princeton University Press, 1988).
5 Sylvia Ostry, *The Post-Cold War Trading System: Who's on First?* (Chicago: University of Chicago Press, 1997), p. 119.
6 Aaditya Mattoo and Arvind Subramanian, 'Regulatory autonomy and multilateral disciplines: the dilemma and a possible resolution', *Journal of International Economic Law* 1:2, June 1998, p. 303.
7 David Vogel, *Barriers or Benefits: Regulation in Transatlantic Trade* (Washington, DC: Brookings Institution, 1997), p. 5.
8 Maria Green Cowles, 'A Conference Report', *The Limits of Liberalization: Regulatory Cooperation and the New Transatlantic Agenda* (American Institute for Contemporary German Studies, Johns Hopkins University, 1997), pp. 3–4.
9 World Trade Organization, *Trade Polity Review—The European Union* (Geneva: WTO, 1998), p. 141.
10 Michael Porter, *The Competitive Advantage of Nations,* p. 53.
11 Sylvia Ostry, 'Technology, productivity and the multinational enterprise', *Journal of International Business Studies* 29:1, First Quarter 1998, p. 86.
12 Ostry, ibid., p. 87.
13 'Inward investment hits new record despite strong Pound', *Financial Times* 15 July 1998, p. 22; UK Department of Trade and Industry, *Competitiveness: Creating the Enterprise Centre of Europe* (*London: HMSO,* 1996), p. 139.
14 Bruce Kogut, 'International business: the new bottom line', *Foreign Policy* 110, Spring 1998, p. 155.
15 Kogut, ibid.
16 UNCTAD, *Sharing Asia's Dynamism: Asian Direct Investment in the European Union* (New York: UNCTAD, 1996), p. 91. Despite current problems, the ability of Taiwan, Korea and Japan to develop advanced technologies was a feature of their development.
17 Phillip Genschel and Thomas Plumper, 'Regulatory competition and international co-operation', *Journal of European Public Policy* 4:4, December 1997.
18 Michael Daly, 'Investment incentives and the Multilateral Agreement on Investment', *Journal of World Trade* 32:2, April 1998, p. 5.
19 Gilbert Winham, 'International trade policy in a globalizing world', *International Journal LI:* 4, Autumn 1996, p. 642.
20 The first case of this type was recently settled out of court. The Canadian government agreed to compensate an American chemical firm for damages it suffered from a Canadian ban on a type of fuel additive. See, 'Canada to pay $13 million to settle imports dispute', *Financial Times* 21 July 1998, p. 6.
21 George Papconstantinou, 'Technology and industrial performance, *OECD Observer* . February/March 1997, p. 10, fig. 5.

22 Michael Porter, *The Competitive Advantage of Nations,* p. 36.
23 Norman Gemmell, 'Reviewing the new growth literature', *New Political Economy* 3:1, March 1998, pp. 129–34. Gemmell cautions that, while studies have demonstrated a positive correlation between economic growth and educational attainment, the results are nowhere near robust enough to guide policy makers on the specific type of educational policies that ought to be pursued.
24 Academics bitterly debate the efficacy of competitiveness policies. The key issue here is that politicians and business groups often believe the policies to be effective.
25 Michael Borrus and John Zysman, 'Globalization with borders: the rise of Wintelism as the future of global competition', *Industry and Innovation* 4:2, December 1997, pp. 141–66.
26 For example, Laura Tyson, *Who's Bashing Whom? Trade Conflict in High-Technology Industries* (Washington, DC: Institute for International Economics, 1993); Jeffrey A.Hart and Assem Prakash, 'The decline of "embedded liberalism" and the rearticulation of the welfare state', *New Political Economy* 2:1, March 1997, pp. 65–78.
27 Klaus Heidensohn, *Europe and World Trade* (London: Pinter, 1993), Chapter 6.
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Further reading

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Chapter 10
The World Trade Organization and civil society

Jan Aart Scholte with Robert O'Brien and Marc Williams[1]

Global governance and civil society

The creation of the World Trade Organization (WTO) has reflected and reinforced an important structural shift, in the face of large-scale globalization, from statist to post-sovereign governance. At the close of the twentieth century, regulatory activities are no longer always centred on or subordinated to the state. Instead, much governance has become spread across a host of substate (such as municipal and provincial authorities), state and suprastate (regional and transworld) institutions, as well as a number of private organizations such as credit-rating agencies and foundations. None of these sites of authority holds a clear, complete and consistent primacy over the others.[2]

Contemporary accelerated growth of supraterritorial flows has made sovereignty (in its traditional sense of absolute, supreme, comprehensive, unilateral state control over a given territorial jurisdiction) unworkable. Recent intensified globalization has broken the Westphalian mould of politics. To be sure, the end of sovereignty has in no way meant the end of the state. On the contrary, many states (especially those of the OECD countries) have in recent history grown in size, acquired new policy instruments and expanded their competences. However, the unprecedented proliferation since mid-century of global communications, global ecological problems, global finance, global production, global markets, global organizations and global consciousness has made *sovereign* statehood impracticable.

In these circumstances, regulators have devised numerous substate, suprastate and private sector mechanisms to supplement or even in some respects to supersede rule by states.[3] A key challenge in our contemporary globalizing world is to construct effective and democratic governance out of what has become multilayered and often fragmented authority. How can policy formulation, implementation and review be properly co-ordinated in decentred governance? How can post-sovereign conditions be fashioned to yield adequate popular participation, open debate, consultation and representation as well as transparency and democratic accountability?

As other chapters in this book demonstrate, the WTO is a prominent instance of growing suprastate governance in the globalizing world of the late twentieth century. Not surprisingly, given the substantial growth in both the range and the authority of global trade law, many civic groups have developed considerable interest in the WTO.

As an important influence on the distribution of resources worldwide, the institution has come to occupy a prominent place on the agenda of numerous business lobbies, labour unions, farmers' organizations, environmentalist groups, women's associations, development co-operation groups, consumer unions, human rights advocates, think-tanks, and other elements of civil society. Many of these non-state actors have sought direct contact with the WTO, bypassing government authorities in order to interrogate and lobby the multilateral institution itself.

This increase in approaches from civic organizations to the WTO has flowed in part from the recent enormous growth in civil society across most of the world. In the present context, 'civil society' refers to a broad collectivity of non-governmental, non-commercial, more or less formal organizations. It encompasses all those groups that, from outside official circles and firms (though sometimes closely linked with them), pursue objectives that relate explicitly to reinforcing or altering existent rules, norms and/or deeper social structures.

One leading researcher of civil society has described (albeit perhaps with some hyperbole) 'a global "associational revolution" that may prove to be as significant to the latter twentieth century as the rise of the nation-state was to the latter nineteenth'.[4] For example, in the 1990s Kenya has counted some 23,000 registered women's groups, and more than 25,000 registered grassroots organizations have operated in the state of Tamil Nadu in India.[5] Significant parts of this expanding civil society have involved transborder affiliations. The number of active transborder civic groups (e.g. of religious believers, professionals, human rights campaigners, etc.) has increased more than tenfold since 1960, to a total of 16,000 in 1997.[6] Many local and national civic organizations, too, have incorporated global networking into their activities.

Since the 1970s, most of the major public global governance agencies have experienced a notable growth of direct exchanges with local, national and trans-border civic associations.[7] Almost all organs of the United Nations system have acquired expanded external relations departments, and many UN agencies have instituted liaison committees with participants from civil society. Proposals have furthermore circulated for the creation of a UN People's Assembly composed of civil society representatives next to the General Assembly of state delegates. Already civic groups have in the 1990s convened global meetings with fair regularity, for example alongside the Group of Seven summits, the Annual Meetings of the International Monetary Fund (IMF) and the World Bank, and *ad hoc* UN conferences on various global issues. A broad consensus has by now emerged that civil society and global governance institutions should have relations with each other. On the other hand, there is far less clarity, let alone agreement, on how these relations should be conducted, and to what ends.

Given this wider context of contemporary world politics, WTO staff and national trade ministry officials ought not to have been surprised to encounter substantial civil society interest in the new multilateral organization. Indeed, a prominent business association, the World Economic Forum (WEF), was instrumental in launching the Uruguay Round of trade negotiations that produced the WTO. Major gatherings of

civic groups have accompanied each of the two WTO Ministerial Conferences held to date: at Singapore in December 1996; and at Geneva in May 1998. Civil society organizations have furthermore undertaken studies of the WTO, disseminated information about the new organization, arranged policy dialogues with WTO staff, and so on.

In fact, the Marrakesh Agreement of 1994 explicitly acknowledges interest and involvement by civil society in the institution. Article V(2) stipulates that the new agency should make 'appropriate arrangements for consultation and cooperation with non-governmental organizations'. The GATT never acted on similar provisions in the (unratified) Havana Charter of 1948 for 'consultation and co-operation with non-governmental organizations'.[8] In contrast, the General Council of the WTO has already (in July 1996) elaborated formal guidelines for increased relations with non-governmental organizations (NGOs).[9] In July 1998 the Director-General, Renato Ruggiero, announced further measures to improve contacts with civic groups.[10]

Benefits and pitfalls

Before examining specific relationships between the WTO and civil society, it is relevant to reflect in general terms on the possible effects of those exchanges. Civil society is inherently neither good nor evil. It can both improve and harm policy. It can both enhance and detract from democracy. In short, civil society's contributions to post-Westphalian governance depend very much on the particular features of individual civic associations and official institutions and the wider socio-historical conditions in which these actors operate.

Unlike the World Bank and UN development agencies, the WTO does not engage so-called 'operational' civic groups in the delivery of services. However, civil society offers the global trade regime at least six other potential benefits:

1 Civic associations can provide the WTO with information (both data and analysis) that is useful in policy formulation, implementation and review.
2 Civil society groups can stimulate debate about WTO policies, particularly by offering alternative perspectives, methodologies and proposals. Such challenges push the WTO better to clarify, explain, justify and perhaps rethink its positions.
3 Civic organizations can provide channels through which stakeholders may voice their views on trade issues and have those opinions relayed to WTO staff. With this input officials can better gauge the political viability of proposed measures or programmes.
4 Civic associations can play an important role in democratically legitimating (or indeed delegitimating) WTO activities. For example, civil society can influence the respect accorded (or denied) to WTO views and the ratification (or rejection) of WTO-sponsored trade agreements.
5 Civil society bodies can serve as important agents of civic education, increasing public understanding of the WTO and its policies. Many civic associations have in this vein prepared handbooks and information kits, organized workshops, circulated

newsletters, written press articles, maintained Internet sites, developed curricular material for schools, and so on.

6 Relations between the WTO and civic associations can reverberate to have more general democratizing effects. For example, citizens' groups that are denied access to their national governments may be able to gain a voice through global channels such as the WTO.

However, the benefits just reviewed do not flow automatically. If badly organized and executed, relations between civil society and the WTO can also have detrimental effects on policy and democracy in the global trade regime. In a negative vein:

1 The collection of civic associations that develops relations with the WTO might not adequately or fairly represent the various constituencies with a stake in the global trade regime. Civic contacts could thereby reproduce and even enlarge inequalities and arbitrary privileges connected with nationality, class, race, gender, religion, and so on.
2 The WTO could treat overtures to civil society as merely a public relations exercise. The institution would thereby not only miss out on the valuable inputs indicated above, but also alienate many if not most of its potential civic partners.
3 Interventions from civil society into global governance of trade could be misdirected and/or ill-informed. Such low-quality involvement can unhelp-fully disrupt institutional operations and policy development.
4 The WTO could through its exchanges with civic groups become embroiled in local and national politics of which it has little understanding, perhaps undermining democracy in the process.
5 The WTO could focus its exchanges with civil society on supportive groups to the neglect of challengers. As a result, the institution would get a false sense of popular endorsement of its policies. Indeed, such marginalization of critics (deliberate or unconscious) could generate a severe backlash against the global trade regime.

In sum, relations between civil society and the WTO can have far-reaching consequences —positive or negative—for the design and operation of the global trade regime. Given the previously described dynamics of politics in the contemporary globalizing world, it seems most unlikely that contacts between the WTO and civic associations will decline, let alone disappear. On the contrary, most indications suggest that these interchanges will further proliferate in the years to come. The challenge before the WTO and civil society is therefore to develop their mutual relationships in ways that minimize the pitfalls and maximize the benefits outlined above.

Civic interest in the WTO

Civil society encompasses huge diversity. The multitude of civic associations exhibits widely differing constituencies, institutional forms, sizes, geographical coverage, resource

levels, organizational cultures, orientations, goals and tactics. In short, due caution is necessary when generalizing about civil society groups.

That said, we may loosely distinguish three types of civic organizations in terms of their general approach to the WTO. One group, whom we might call 'conformers', accepts the established discourses of trade theory and broadly endorses the existing aims and activities of the WTO. A second group, whom we might call 'reformers', accepts the need for a global trade regime, but seeks to change reigning theories, policies and/or operating procedures. A third category of civic associations, whom we might call 'radicals', seeks to reduce the WTO's competences and powers or even to abolish the institution altogether.

Corporate business associations, commercial farmers' unions and economic research institutes have usually taken a conformist approach to the WTO. Prominent business groups that have supported the WTO-based global trade regime include the aforementioned WEF, the International Chamber of Commerce, and the European Round Table of industrialists. With a narrower agenda, US-based organisations such as the US Dairy Foods Association, the Pork Producers Council, the National Farmers' Alliance, and the American Sugar Alliance have urged a rapid liberalization of trade in agricultural products. Think-tanks that have promoted a broadly conformist line on the WTO include the Brookings Institution and the Institute for International Economics. In the juridical field, bodies such as the International Law Association Committee on International Trade Law have also made a professional input.

This is not to say that conformist civic organizations have approved of each WTO rule, procedure and decision. On the contrary, business lobbies have frequently sought to revise or overturn a WTO measure to their commercial advantage, and mainstream researchers have often queried certain WTO actions and analyses. However, these disagreements have remained within the conventional framework of trade debates, namely on a spectrum running from liberalism to mercantilism. Conformists therefore 'speak the same language' as WTO staff and most national trade officials. For these circles, arguments about trade regulation do not go beyond issues concerning the balance between free trade and protectionism and the degree and speed of liberalization. Conformers only interrogate the outputs of the existing global trade regime, not its foundations.

In contrast, reformers in civil society aim to change the thinking, rules and procedures of the WTO. Most reformist activities have sought to redress alleged undesirable effects of the existing trading order: for example, in respect of labour conditions, underdevelopment of the South, environmental degradation, consumer protection, and gender inequalities. Many of these lobbyists have concurrently campaigned for a democratization of WTO operations: for example, in terms of wider participation and greater public release of information.

Trade unions and human rights advocates have spurred efforts to incorporate protective labour standards into the global trade regime.[11] These reformers maintain that trade liberalization coupled with market globalization has greatly weakened the power of workers *vis-à-vis* managers and investors. In order to safeguard basic labour

rights and restore a fair balance of class interests—so these civic groups argue—the WTO needs a social clause that commits states to respect seven key conventions of the International Labour Organization (ILO).[12] Leading voices from organized labour in this campaign have included the International Confederation of Free Trade Unions (ICFTU), the World Confederation of Labour, and several International Trade Secretariats. Certain human rights groups have also engaged the WTO on issues of labour protection: for example, the Washington-based International Labor Rights Fund; the Montreal-based International Centre for Human Rights and Democratic Development; and the Brussels-based SOLIDAR alliance. Significantly, some trade unions and NGOs in the Third World have viewed this lobbying with scepticism as an effort to perpetuate the privileges of workers in the North at the expense of development in the South.

Indeed, many development NGOs with interests in global economic governance have expanded their advocacy work beyond the Bretton Woods institutions and UN development agencies to encompass the WTO as well. Given that WTO rules severely restrict the autonomy in trade policy of already weak states in the South, these civic groups have worried that the Uruguay Round and subsequent accords might well compromise possibilities for equitable human development. Prominent NGOs in trade-and-development debates have included Oxfam, Third World Network and the Harare-based International South Group Network.[13] These issues have also occupied a number of development think-tanks, including the North-South Institute (Ottawa), the Brazilian Institute for Social and Economic Analysis (IBASE, Rio de Janeiro), and so on.

Some of the most persistent efforts in civil society to reform the WTO have come from environmental NGOs. These critics maintain that a liberal trade regime tends to exacerbate ecological degradation: (a) by encouraging a relaxation of national environmental protection measures in order to maintain international competitiveness; (b) by promoting production for export (more environmentally damaging) rather than for home consumption; (c) by stimulating, with increased exports, unsustainable levels of natural resource exploitation;and (d) by (implicitly) sanctioning trade in toxic wastes. Environmentalists have sought, first, to get sustainable development concerns on the WTO agenda and, second, to institute restrictions on trade where it causes ecological damage. Leading reformist environmental NGOs in dialogue with the WTO have included the International Centre for Trade and Sustainable Development (ICTSD, established at Geneva in September 1996), the World Conservation Union (IUCN), the World Wide Fund for Nature, the International Institute for Sustainable Development, and the Center for International Environmental Law.

A fourth issue of notable concern in campaigns to reform the WTO has been consumer protection. Advocates in this area argue that the existing liberal global trade regime has greatly enhanced the power of large (usually trans-border) firms. They affirm that global competition policy and a binding code of conduct for global companies are needed to constrain this corporate power in the public interest. Prominent civic associations in this campaign have included UK-based Consumers

International, India-based CUTS, and the International Organization of Consumer Unions.

Meanwhile certain other NGOs have sought to bring gender awareness to the WTO. Employing feminist political economy, they are concerned that the global trade regime, like the modern economy generally, contains structural biases against women.[14] Some voices in the global women's movement have therefore called *inter alia* for gender assessments of WTO rules and for attention to gender issues in the WTO's trade policy reviews.[15] These associations created an Informal Working Group on Gender and Trade at the Singapore Ministerial Conference and convened again at the Geneva Ministerial Conference. Prominent actors in these (to date fairly limited) efforts have included the New York-based Women's Environment and Development Organization (WEDO) and the Brussels-based campaign, Women in Development Europe (WIDE). WEDO has produced several booklets on the global trade regime, and WIDE organized a Women and Trade Conference in Bonn in May 1996.[16]

The issues discussed so far relate to policy content, but many civic activists have sought also to change the operating procedures of the WTO. In particular they have advocated a democratization of the organization by giving citizens increased access to, and influence in, its proceedings and decisions.[17] Some reformers have argued in this vein that relevant representatives in civil society should participate directly in WTO policy deliberations, trade policy reviews, and dispute settlement procedures.[18] Pursuing a complementary line, the Swiss Coalition of Development Organizations has urged the establishment of a WTO Parliament with legislative competence or, in the interim, the formation of a parliamentary group with an advisory role *vis-à-vis* the WTO. Other proposals have called for a more transparent WTO, that is, one which has open hearings, increased (and more timely) publication of official documents, and greater dissemination of information, particularly in the South.

Whereas reformers aim in one way or another to alter the WTO, radicals in civil society regard the existing global trade regime as incorrigible. They therefore advocate its contraction (back to the original parameters of the GATT, for example) or complete abolition. In the mid-1990s, radical groups campaigned against ratification of both the Uruguay Round accords and the North American Free Trade Agreement. In February 1998 many of the same opponents formed a loose worldwide network called Peoples' Global Action against 'Free' Trade and the World Trade Organization. The PGA has called openly for 'the disappearance of the WTO'. Its rejectionist stance may be broadly likened to the position of the 50 Years Is Enough coalition towards the IMF and the World Bank. Indeed, participation in the two networks has overlapped to some extent. Radical circles also include environmentalists like Greenpeace who—in contrast to the reformist associations named earlier—refuse to talk with the WTO.

The preceding survey amply confirms the observation made at the start of this section that civil society relations with the WTO encompass a large diversity of organizations, activities and approaches. The distinction of conformist, reformist and radical groups is not always neat in practice, of course. For example, some economic

research institutes have straddled conformist and reformist positions. Meanwhile many development NGOs have fluctuated between radical and reformist positions. Nevertheless, the three-way categorization of conformers, reformers and radicals remains analytically useful in mapping the politics of civil society in regard to the WTO.

WTO overtures to civil society

How has the WTO reacted to the various initiatives from the civil society associations described above? The institution has during its short history already taken some steps to implement Article V of the Marrakesh Agreement. In brief, the WTO has: (a) adjusted its language to recognize civil society; (b) undertaken various outreach initiatives towards civic associations; (c) increased its public dissemination of information; and (d) made some alterations to substantive policy that (partly) meet civil society demands. These four positive developments are detailed below. On the other hand, as the next section will elaborate, the WTO has to date done relatively little to institutionalize relationships with civil society or to involve civic associations directly in policy deliberations. Nor has the organization so far made much use of contacts with civil society to gauge the political viability of its policies.

In its discourse, the WTO has joined other global governance agencies in acknowledging the importance of civil society inputs to policy. For example, in his address to the Singapore Ministerial Conference, Ruggiero highlighted the presence of many 'representatives of non-governmental organizations, the business sector, and the media'. He went on to argue that:

> a world trading system which has the support of a knowledgeable and engaged global community will be in a far stronger position to manage the forces of globalization for everyone's benefit.[19]

At the Geneva Ministerial Conference, too, Ruggiero and several government leaders publicly endorsed the idea of increased relations between the WTO and civil society. In this vein President Clinton proposed 'a forum where business, labour, environmental and consumer groups can speak out and help guide the further evolution of the WTO'.[20] At a time when UN bodies and the Bretton Woods institutions are continually speaking of 'stakeholders', 'ownership' and 'participatory development', the WTO can hardly speak another language.

The shift in discourse has been more than rhetorical in so far as the WTO has taken various initiatives to establish dialogue with civic groups. Its staff has provided many briefings to and received multiple representations from business associations, labour unions and NGOs. More elaborately, the Secretariat has since June 1994 organized four annual symposia with representatives of civil society on trade and sustainable development issues. In September 1997 two dozen NGOs from four continents participated in a Joint WTO/UNCTAD Symposium on Trade-Related Issues Affecting

Least-Developed Countries. At the Ministerial Conferences the WTO has provided civil society representatives with office space and media facilities.

The organization has also responded to demands from civil society for greater release of information concerning WTO policy making. The production of official publications has expanded, and staff have since 1995 constructed an elaborate Website.[21] In July 1996 the General Council adopted Procedures for the Circulation and De-Restriction of WTO Documents. Under these guidelines, reports of dispute panels are now made public as soon as they are adopted. The WTO also publishes completed trade policy review reports and summaries of the proceedings of the Committee on Trade and Environment. Some important documentation continues to be restricted, but the WTO releases far more information than the GATT ever made available. As one NGO representative recently described the situation, 'The WTO has evolved from opaque to translu-cent'.[22] At the Second Ministerial Conference, Ruggiero pledged to consider how moves towards greater transparency could be taken further. Following the measures announced in July 1998, the WTO Secretariat has alerted member governments to all documents, position papers and newsletters submitted to it by civic organizations.

Several other turns in WTO policy have also responded to demands from civil society. For example, the expansion of trade liberalization measures to cover intellectual property matters, telecommunications, financial services and so on has (at least partly) met the wishes of various business lobbies. On another front, the WTO has sought to appease trade unions by putting labour standards on its agenda and by deepening its collaboration with the ILO. In response to development questions, the WTO has maintained a Committee on Trade and Development and in October 1997 convened a High-Level Meeting for Least-Developed Countries. In recognition of ecological concerns, ministers assembled at Marrakesh decided to launch a wide-ranging work programme on trade and environment in the WTO. (In contrast, the GATT Group on Environmental Measures and International Trade, formed in 1971, met only once, in 1993, to discuss the results of the UN Conference on Environment and Development.) On questions of unfair business practices in global markets, the Singapore Ministerial Conference established a WTO working party to study the interaction between trade and competition policy. These and other policy developments have often fallen short of what civic groups (reformists in particular) aim for,[22] but changes there have been.

Shortfalls in relations

Contributions from civil society to the global trade regime have clearly increased in both quantity and quality in the 1990s. Nevertheless, major additional advances would be required before civic inputs could realize their full potential (on the lines described earlier) to increase policy effectiveness and democracy in the WTO. The following paragraphs outline three major shortcomings in current relations between civic associations and the WTO, namely unequal access, shallowness and limited reciprocity.

These flaws have caused WTO-civil society exchanges to suffer significantly from the possible pitfalls noted earlier.

A first major way that WTO-civil society contacts have thus far failed to maximize their potential contributions to policy enhancement relates to biased participation. The various elements of civil society have not enjoyed equal opportunities to engage with the WTO. In a rough ranking, conformers like business associations have usually had easiest access. Thus, for example, 65% of the civic organizations accredited to attend the Singapore Ministerial Conference represented business interests.[23] Certainreformist groups such as trade unions, environmental NGOs and development NGOs have generally come (a rather distant) second. Many other civic bodies, including most grassroots associations, have had no direct access to the WTO at all.

Other inequalities in access have favoured organizations based in the North over groups located in the South and the East. In class terms, civic contacts with the WTO have principally involved urban-based, university-educated, computer-literate, (relatively) high-earning English speakers. A few development NGOs have attempted to incorporate 'voices from the base' into their advocacy work on the WTO, but for the rest underclasses have been locked out of exchanges with the institution. The dialogue has also shown a gender bias, with disproportionately large participation from men in both the WTO staff and civic groups (especially business, academic and labour associations).

A second major shortcoming in WTO-civil society relations to date has been their overall shallowness. Although, as seen above, the WTO leadership has become convinced in general terms of the importance of civil society in emergent global governance, the organization has for the most part lacked clearly formulated objectives and carefully constructed channels of communication for its interchanges with civic groups. On the whole the WTO's engagement of civil society has occurred through improvisation. Its External Relations Division has remained small, and its staff have lacked expertise in respect of civil society. In contrast to the World Bank, the WTO has established no liaison committee with civic groups. In contrast to the United Nations, the WTO has made no arrangements for permanent accreditation of civic organizations, as opposed to *ad hoc* admission to specific events. No civil society associations have participated as *ex officio* observers on WTO committees. Nor have civic groups been systematically involved in trade policy reviews or dispute settlement procedures. To this extent the WTO has done little to bring civil society into policy making. Indeed, in contrast to the IMF and the World Bank, the WTO has given civic associations no mention in its first annual reports.

Approaches from civil society towards the WTO have often suffered from similar shallowness. Relatively few associations have—like the WEF, the ICFTU, Third World Network and the ICTSD—pursued sustained, focused, carefully researched efforts to understand and shape WTO policies. Most civic groups with concerns about global economic governance have shown only haphazard and superficial interest in the WTO, becoming active only around a particular conference, set of negotiations or trade dispute.

A third general limitation in WTO-civil society relations—namely, a lack of veritable 'dialogue'—has mainly affected the institution's contacts with reformers and radicals. These interchanges have often lacked sufficient openness and reciprocity, where the WTO on the one hand and activists on the other are fully ready to listen to, learn from and be changed by each other. Such 'dialogues of the deaf' were particularly acute, for example, in early contacts between free traders at the WTO and environmentalists who automatically linked trade liberalization with increased environmental degradation. Exchanges between the WTO and reformist groups have tended to become more cordial in the late 1990s. However, parties to WTO-civil society exchanges are still not as prepared as they could be to consider positions other than their own.

In sum, relations between the WTO and civil society have to date often succumbed to the potential dangers highlighted earlier. First, the exchanges have not been democratically representative. On the contrary, they have tended to reinforce structural inequalities in world politics. Second, on balance the WTO has not yet taken its contacts with civil society that far beyond public relations exercises. Third, on the whole civic groups have not provided the WTO with sufficient precisely formulated and carefully researched inputs. Fourth, the WTO has not given careful thought to the possible repercussions of its contacts with civil society on national and local politics in its member countries. Fifth, the WTO has for the most part skewed its contacts toward conformist groups, to the relative neglect of its reformist and radical critics, thereby obtaining an artificially optimistic assessment of the popularity and viability of its policies.

To note shortfalls in relations between civil society and the WTO is not to advocate an abolition of these links, of course. As stressed before, the dynamics of contemporary governance are such that those exchanges are in effect irrepressible. We cannot return to a Westphalian world where 'international organizations' dealt only with states. The unavoidable challenge is therefore to forge relation-ships that maximize the contributions of civil society to effective and democratic global governance.

Constraints

In order to prescribe measures for improved relations between civil society and the WTO, one needs first to assess the causes of the problems. In a word, the shortfalls just described have arisen primarily from resource limitations and deeper structural forces. That is, the shortcomings in WTO-civil society relations have not resulted in the first place from the personalities and attitudes of individual officials and lobbyists, but from the political, economic and cultural context in which they work.

In terms of resources, the WTO has thus far lacked the personnel, funds, stores of information and co-ordination capacities to realize the full potential of relations with civil society. At present the organization has only a modest staff of about 500 to handle a vast global trade agenda. (In comparison, the IMF currently employs around 2600 persons, whereas the World Bank payroll nears 5500.) In terms of disposition,

the professional staff of the WTO are overwhelmingly economists without formal training in socio-political issues such as the organization and operations of civil society. Meanwhile the WTO runs on a total administrative budget of less than $100 million per annum, hardly a sum that allows for major overtures to civil society. (In comparison, the World Bank operating budget is some $1375 million, while the IMF travel budget alone currently amounts to $77 million.) In view of these personnel and funding limitations, it is not surprising that the WTO has accumulated little information on civil society. Its staff are therefore usually very poorly briefed on the civic groups that they meet. Nor has the organization developed any mechanisms to co-ordi-nate its work on civic associations with national governments and other global governance bodies that have more experience in these contacts.

In most cases, civic groups suffer from even more precarious resource situations than the WTO. In terms of personnel, civil society organizations rarely have more than one or two staff with detailed knowledge of the global trade regime. Major business associations and certain think-tanks have operated with fairly substantial and reliable funding, but most trade unions and NGOs have worked on shoestring budgets and/or short-term grants. Most civic groups have (partly owing to the inaccessibility of many official documents) lacked sufficient data and analysis to mount fully informed campaigns for policy change at the WTO. In addition, civil society groups have developed few arrangements (aside from loose networking as seen in the PGA) to exchange information on and co-ordinate lobbying of the WTO. As a result, the limited resources of civil society have rarely been optimally employed.

That said, improved staffing, funding, information flows and co-ordination would not by themselves maximize the benefits of exchanges between civil society and the WTO. Indeed, certain conditions of social structure have, if anything, stood as greater barriers to a fuller development of the dialogue.

For example, difficulties of access to the WTO for civic organizations have resulted in part from the culture of secrecy that has traditionally enveloped both global economic governance in general and global trade regulation in particular. Recent WTO moves towards increased disclosure mark an important shift towards greater openness, but the embedded culture of secrecy has slowed the process and is unlikely to dissolve quickly.

The previously described inequalities of civil society access to the WTO have also reflected deeper structural conditions: in this case pervasive entrenched social hierarchies in contemporary world politics between countries, classes and genders. Such structures of subordination have figured centrally in producing a lower allocation of resources and opportunities: to South-based civic organizations relative to North-based groups; to labour unions relative to business associations; to women relative to men; and indeed to civil society relative to official circles.

The power of neoclassical economic orthodoxy has been another important structural force against a more inclusive, deeper and more open dialogue between the WTO and civil society. So-called 'neoliberal' ideology has dominated social knowledge in the late twentieth century, particularly following the dissolution of communist regimes and the collapse of postcolonial socialism. In this situation of near

monopoly, ideas of market rationality and comparative advantage have readily reigned as unquestioned truths, and staff of the WTO have faced little pressure to give alternative perspectives a serious hearing. This knowledge/power structure has put reformers and radicals at a marked disadvantage in civil society relative to conformers.

A fourth structural inhibition to greater development of relations between the WTO and civil society has been the persistent hold of the sovereignty norm. Although, as indicated at the start of this chapter, states have lost their effective capacity to exercise sovereign governance, governments have continued to cling jealously to the claim that they always have the complete and final say in regulation. Most civic activists and WTO officials, too, have continued to work under the spell of the sovereignty myth. They have therefore generally directed their contacts first at states rather than at each other, and both civic groups and the WTO have usually limited their direct exchanges to an intensity that governments would tolerate.

Finally, and partly as an extension of the sovereignty issue, structural conditions have limited dialogue between the WTO and civil society in so far as civic groups have generally experienced difficulty establishing their legitimacy. In the Westphalian international system to which contemporary globalization has brought an end, states were normally regarded as the only legitimate actors in world politics. Today's post-Westphalian situation allows for a multiplicity of agents, but non-state entities must still work hard to establish their credentials. Civil society associations can best secure their legitimacy in terms of democratic practices; however, most civic groups have to date attended insufficiently to questions concerning their representativeness, consultation processes, transparency and accountability. Indeed, some of the organizations that have pressed hardest for a democratization of the WTO have done little to secure democracy in their own operations. This has allowed the WTO and states to take civil society less seriously than they might otherwise have done.

Towards the future

If—as seems probable—globalization continues at substantial rates into the next century, then governance is likely to become increasingly quadrilateral, between substate authorities, states, suprastate agencies and civil society associations. As indicated above, civic inputs can contribute greatly to policy efficacy and democracy in this situation of multilayered governance. Yet such benefits do not accrue automatically. It is understandable that the WTO and civil society have allowed the early development of their relations to be largely haphazard and improvised. However, the next phase requires more concerted and carefully constructed efforts. What sorts of practicable measures are available to take relations between civil society and the WTO forward in the short to medium term? Five general suggestions follow from the analysis presented above.

In the first place, the parties can aim to clarify and specify their objectives. What, more precisely, are they trying to achieve by engaging with each other? The WTO in particular needs more explicit policy aims in regard to civil society.

Second, further steps can be taken formally to institutionalize relations between the WTO and civil society. Drawing on the experience of other global governance agencies, the WTO can devise mechanisms for permanent accreditation, observer status in relevant committees and panels, a regular cycle of consultations (extending the practice of the annual symposium with environmentalists), etc.

Third, both the WTO and civil society can improve relevant staff capacities. For example, the WTO could appoint several specially designated 'civil society liaison officials'. Other relevant staff could take short training courses on relations with civic groups, for example, as are currently being developed by the United Nations Staff College in Turin. Likewise, more civil society capacity is needed—particularly among marginalized groups—regarding the global trade regime.

Fourth, the parties can make more efforts to co-ordinate their activities in WTO—civil society exchanges. For example, the WTO could join the sixteen other global governance agencies that subscribe to the UN Non-Governmental Liaison Service. It could also exchange information and advice concerning civil society with other multilateral institutions that have more experience in these relationships. Meanwhile civic groups with interests in the global trade regime could do more in the way of exchanging information, sharing tasks, co-ordi-nating initiatives and so on.

Fifth, both civic organizers and WTO officials can consciously nurture attitudinal changes that promote more constructive dialogue. For instance, all participants in the relationship can make more deliberate efforts to include otherwise marginalized circles. The WTO and civic groups can also cultivate greater mutual recognition, respect and reciprocity. In addition, both civil society organizations and the WTO can become more sensitive to issues of their democratic accountability. To this end, all parties could *inter alia* do more to publicize their activities to each other and to the wider public.

None of the steps just described need be particularly costly or difficult. Given the substantial benefits of well-developed WTO—civil society relations—in terms of increasing information, stimulating debate, educating citizens, legitimating regimes and democratizing politics generally—such initiatives are surely worthwhile.

Notes

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Chapter 11
New issues, new actors in EU commercial policy making

Michelle Cloutier

Interest intermediation and the EU Packaging Directive

This chapter contains several elements addressed in more detail elsewhere in this volume. It deals with the impact of 'new' policy issues, specifically environmental policy, on trade policy. It also addresses the issue of state sovereignty as it describes the supranational policy-making process of the European Union (EU). The main focus of this chapter, however, is on the role of non-state actors on trade and environmental policy making in the EU; this focus serves to remind us that an examination of internal political processes helps us understand how externally oriented policies, like trade policies, develop. These non-state actors include the institutions of the EU that do not specifically represent member state interests—specifically the European Commission, the European Parliament, and the European Court of Justice (ECJ); these are the 'institutional' non-state actors.[1] The other non-state actors studied in this chapter are 'societal' actors—mainly industry associations and environmental interest groups. While providing a glimpse into general EU policy making, the chapter concentrates upon a particular directive, the 1994 Packaging and Packaging Waste Directive (Dir 94/62. OJ L 365/10 1994, hereafter Packaging Directive), that had both environmental and trade policy antecedents.

EU policy making: a brief primer

The EU policy-making process can be divided into two stages: policy initiation (or agenda setting) and decision making. Traditional intergovernmental approaches to the EU—which assert the primacy of states in the political process - focus their attention on the second, or decision-making, stage in which the Council reads, negotiates and votes on Commission proposals. Intergovernment-alists do not explore the first stage of agenda setting, since they see this task as having been delegated to the Commission through the member states' authority. This assumption is problematic, even though it seems to simplify what is in reality a very complex policy-making process. While it is true that the Commission often responds to member state recommendations, these recommendations are often very general in nature. The Commission frequently takes the initiative of turning these vague policy direction statements from the European Council or Council of Ministers into specific European policy.[2] The Commission plays a much larger role in

agenda setting than simply taking the member states' suggestions and turning them into policy proposals. The policy initiation stage is, in the opinion of both scholars and EU officials, the most crucial stage of the policy process.[3] If it is indeed true that approximately 80% of a policy is set before it reaches the Council, then determining which actors help shape policies as they are formulated is an important key to explaining EU policy making.[4]

In the second stage of policy making, the decision-making stage, the Council of Ministers still dominates the process. However, with the expansion of the Parliament's role in the decision-making process after the Single European Act (SEA) and again after the Treaty on European Union (TEU, or the Maastricht Treaty), the influence of actors other than the member states in the decision-making stage has become greater. For legislation dealing with the Single Market, which establishes free movement of goods, people and capital within the EU, the Parliament now possesses what is essentially a veto power over proposed legislation when it disagrees with the Council's Common Position.[5] As the following case study demonstrates, one cannot ignore the influence of non-state actors, either institutional or societal, when studying EU policy making. Perhaps even more importantly, interest groups acting at the European level can no longer afford to ignore the Commission and Parliament at either the policy initiation or decision-making stages of the policy-making process if they wish to influence EU trade and environment policy.

The Packaging Directive: tracing the policy process

Packaging, and packaging waste, the subjects of the 1994 Packaging Directive, have both environmental and trade impacts. First, as most goods produced by any firm, in any country, are packaged, national legislation on packaging requirements has an impact on trade. For example, if one state requires all packaging to contain a certain percentage of recycled material, that state may bar packaging materials from other states that do not meet these requirements. This poses a trade barrier inconsistent with the Single Market. Second, if a state has legislation on how to dispose of packaging waste that is stricter than other states, there may be an impetus for firms to ship their waste to other states with less stringent requirements. Trade in waste itself has been the subject of important ECJ rulings, where environmental standards have clashed directly with the concept of free movement of goods within the EU.[6]

The 1994 Packaging Directive had several antecedents in both Community and member state legislation. The first Community Directive on waste was the 1975 Framework Community Directive on Waste (Dir 75/442, OJ L 1975, 194/39), which, as a Framework Directive, left a great deal of leeway for implementation and interpretation by the member states.[7] The Community's first attempt specifically to regulate packaging and packaging waste was the 1985 Directive on Containers of Liquids for Human Consumption (Dir 85/339, OJ L 1985, 176/18: The 'Liquid Containers' Directive). During the 1980s, waste from packaging began to place an increasing burden on the environment, exposing the inadequacies of the 1975 Framework Waste Directive. Member states began to take matters into their own hands, with

Germany developing the strictest packaging and packaging waste legislation.[8] The Danish bottle return system was another example of a national attempt to regulate waste, The Danish requirements were stricter than those in the Community's Liquid Containers Directive, which came into force after the Danish bottle legislation, and posed a trade barrier to other states who did not meet the Danish minimum requirements for reuse and recycling. The Commission took Denmark to the ECJ for a breach of Article 30, the primary article governing free trade in the EU.[9] In the *Danish Bottles* case, the Court held that the intent of the Danish law was to protect the environment, and as such, it could override Article 30.[10] The results of the case made it clear that the Community needed a harmonized approach to packaging waste. Such legislation was needed in order to set reasonable and clear reuse, recovery and recycling objectives that would not interfere with the primary objective of the Community, the formation of the Single Market. The Packaging Directive began as a simple attempt to amend the 1985 Liquid Containers Directive. Over time it grew to include all packaging and packaging waste, and became a model for post-Maastricht policy and policy making at the nexus of Single Market and environmental policy.

The initial steps towards developing a European Packaging Directive began in 1990. Early that year, Commission officials had begun to consider the amendment of the 1985 Liquid Containers Directive, in order to improve the reuse and recycling of these types of containers. Then, at a Council of Ministers meeting in May 1990 (OJ C 1990, 122/2), the Council asked the Commission to come up with a proposal to address the environmental problems caused by waste from packaging, and to try to harmonize the burgeoning legislation of the individual member states. The EC had already moved away from handling environmental problems on a case-by-case basis, developing a wider framework approach to pollution prevention which was embodied in the 4th Environmental Action Programme.[11] Thus, when the Commission took up the Council's request, it was in the context of the overall packaging problem, embedded in pre-existing Community legislation. The EU drew both on its years of environmental policymaking experience and on its efforts to reconcile trade and environmental policy in the internal market to develop a directive that had two principal aims. The dual purpose of this directive was to protect the environment while avoiding trade imbalances or barriers among the member states in packaging and packaging waste.

Policy initiation

In July 1990, the Commission set up a project group of Commission officials and independent experts. It held its first meeting on 17–18 October 1990.[12] As a general rule, because of the wide range of environmental issues they must deal with, many of the DG XI Commission civil servants often do not have previous expertise in a particular policy area. This original project group was consistent with the Commission's tendency to bring in outside experts to deal with the technical aspects of proposed legislation.[13] The project group produced a discussion paper in March 1991 from which it planned to develop a final proposal for a Packaging and Packaging Waste Directive.[14]

At the same time as it was developing this directive, DG XI was in the process of developing and refining the Fifth Environmental Action Programme, which stressed greater dialogue at the initial stages of policy proposals between the Commission and those responsible for implementing the policy on the ground.[15] To put this into effect even prior to publishing the Fifth Action Programme, DG XI instituted a new procedure for developing the packaging policy proposal. Prior to this directive, DG XI had generally invited interested parties to present information or opinions to the working group for a proposal.[16] However, this consultation was loose, fragmented and informal. During the spring of 1991, DG XI instituted formal consultation meetings where it invited the interested parties to participate in the formulation of the proposed directive. This formal consultation had the effect of bringing DG XI officials, industry representatives, member state delegates and environmental and consumer group advocates to the policymaking table. While it can be argued that the less well-organized and understaffed environmental organizations remained at a disadvantage compared to the more cohesive industry associations, the new consultation procedures of DG XI ensured that the opinions and expertise of all involved parties were considered in the Commission's development of the proposal. The first two DG XI drafts of the proposed directive reflected the concerns both of industry, as implementers of the directive, and of environmentalists, who wanted a strict hierarchy of waste management options, and high targets for recycling and recovery.

After the formulation of the second draft, the policy-making process reverted back to a more typical mode of policy development within DG XI. Instead of being invited to formal consultations, interested parties competed with each other for the 'ear' of DG XI. When DG XI requested opinions on its second draft of the directive in September 1991, it was inundated by submissions by trade and industry, and the lobbying of DG XI became intense and competitive.[17] This competition was mainly between industry and environmentalists, but also included regional, local and member state representatives.

Porter's study of lobbying and the Packaging Directive shows that of 279 enti-ties that lobbied DG XI during the development of the directive, 196 were from trade and industry.[18] Consumer groups, trade unions and environmental groups accounted for only 5.7% of total lobbyists to DG XI from July 1990 to December 1993, while industrial and trade interests accounted for over 70%.[19] As the proposed directive proceeded through its drafts in DG XI it became more and more favourable to the position of trade and industry and less and less 'environmental'.[20]

The sheer number of industrial lobbyists may help account for their influence on the proposal.[21] However, other factors that put the environmentalists at a disadvantage must also be considered. While the Community's problem of disposing of packaging waste was very real, its impact varied across the member states. Where it generated any public interest, it was at the local or regional rather than European level. Put simply, the issue of packaging waste did not capture the public's attention as other issues such as the ozone hole or acid rain had. This meant that environmentalists' lobbying position, already weaker than that of industry because of

their smaller organizations and comparative lack of resources, was not backed up by strong public opinion calling for strict recycling and recovery targets.

When the development of the proposed directive reverted to open lobbying, the environmental groups had to compete with the stronger, better organized industrial groups. While many companies in the packaging industry made individual representations to DG XI, they were also represented by larger sectoral associations. These included the Association of Plastics Manufacturers of Europe, the European Organization for Packaging and the Environment, and the European Recovery and Recycling Association, all of which had major industrial players among their memberships.[22] Generally speaking, these associations have the money and other resources to prepare effective position papers, send highly qualified experts to meetings, and otherwise remain apprised of developments in any number of proposed pieces of EU legislation. Environmental associations, like the European Environment Bureau, are often so short staffed that they cannot send a representative to an important debate or meeting, or may miss important developments in a proposal because their attention is focused elsewhere.

Industry waged a successful battle within DG XI, and within the Commission as a whole, to water down the directive in its favour. Industry did not want to bear the costs for a strict packaging waste program at the European level. Its main fear was that the directive would resemble the German Packaging Waste ordinance, which had cost firms in Germany a great deal of money because it made firms responsible for their packaging from 'cradle to grave'. If such legislation were enacted at the European level, manufacturers would have been responsible for their products' packaging even if the products were shipped from one state to another. The recovery costs for such packaging would have been astronomical. Their main point of contention was with DG XI's strict hierarchy of waste management options, with recycling at the top, which would have reduced their options in terms of waste disposal. In addition to lobbying DG XI directly and participating in the consultations there, industry representatives also lobbied Directorates more amenable to industry's point of view. Industry was better placed than environmentalists to lobby widely in the Commission because of its organizational strength and its capacity to generate needed information about implementation for the Commission.

The other Directorates, as typifies Commission legislative drafting, gave their opinion and input to DG XI on its drafts. Since any draft directive must pass muster in the Commission as a whole, DG XI eventually had to give up some of its goals, such as the waste management hierarchy. It did, however, maintain high targets for recovery and recycling over the objections of industry and several of the member states. By the time that the Commission presented the proposed directive to the Council, Parliament, and Economic and Social Committee in August 1992 (OJ C 263, 1992), the influence of societal actors had played a major role in shaping the policy on which the member state representatives would later vote.

Decision making: the Council and the Parliament

During the decision-making stage of policy making, the Council of Ministers, the representative body of the member state governments, and the European Parliament, the only directly elected institution of the EU, consider and vote on the Commission's proposed directives. The Commission proposed the directive based on Article 1 100a, the article governing the operation and completion of the Single Market. This meant that the Council would vote on the directive by qualified majority voting, in accordance with the SEA of 1987 (the SEA was still in effect at the time of this reading). This also meant that the Parliament would have the opportunity for a second reading of the proposed directive after the Council had developed its common position. Although its opinion was not, in this pre-Maastricht period, binding on the Council, the Parliament would thus keep its hand in the game far longer than it did prior to the SEA. The Parliament's greater role in the decision-making process through this second reading made it a much more important target for lobbying groups at the European level. The second reading allowed societal groups, as well as the Parliament, greater opportunity to influence policy in the decision-making stage than was possible before the SEA.

The Parliament is often seen as being the 'greenest' European institution. This may be due in large part to the fact that the Environment Committee of the EP is one of the strongest, best respected committees in the Parliament, and its amendments to proposals are generally taken seriously and accepted by the Plenary of the Parliament when it meets in Strasbourg. The Environment Committee, headed by Ken Collins, an MEP from Scotland who has chaired the Committee since 1979, was primarily responsible for the reading of the packaging proposal in the Parliament. Collins' informal relationships outside the Parliament with member state representatives, industry and trade groups, and environmental organizations were as important to the functioning of the Committee as the lobbying done by these groups on a more formal basis through documents and official position papers.

In addition to encouraging informal links with members of other EU institutions, the open institutional structure of the Parliament allowed a great deal of societal interest representation. The Environment Committee was particularly open to meeting with and hearing from interests both within and outside its own viewpoint. By one estimate, over half of the lobbyists to the Parliament during this first reading represented associations of industrialists, and another 26% of the lobbyists were either from individual companies or were consultants to indus-trialists.[23] Despite the heavy lobbying from industry, however, the Environment Committee remained committed to a pro-environmental stance.

The Plenary of the Parliament adopted seventy-five of the seventy-nine amendments presented by the Environment Committee in June of 1993. The Commission, which can then accept or reject the amendments, adopted approximately half of the Parliament's amendments in September 1993, which it then presented to the Council of Ministers (OJ C 285, 1993). The Commission rejected a Parliamentary amendment calling for the strict hierarchy of waste management options that trade and industry had lobbied strenuously against in both the

Commission and Parliament. The environmental working groups within the Committee of Permanent Representatives (COREPER) in the Council then took up the amended proposal.[24]

The Council of Ministers has a well-deserved reputation as a closed, secretive circle. There is no requirement for the votes in the Council to be made public. According to those in Brussels, in order to know what goes on behind the closed doors of the Council, one must establish ties with someone dealing with the proposal, either in the COREPER working group, or within the appropriate national ministry. These relationships also go the other way—from the national representatives to the other institutions. During the development of the Packaging Directive, Germany, Denmark and the Netherlands, because of their strict national legislation on packaging and packaging waste, looked to the Greens in Parliament as allies in getting higher EU requirements for recycling and reuse of packaging. Some member state representatives used their links with MEPs from their country who in turn tried to influence their government's position on the directive. These relationships reveal the mutual dependence between the Council and the Parliament that has grown since the implementation of the SEA and the advent of the co-operation procedure between the Council and Parliament.

The Council itself is closed to societal lobbying by European-level interest groups. In order to lobby the Council, one must lobby the national government representatives responsible for a particular policy area. However, national-level interest groups often form interstate coalitions to pressure the different member states on an issue, forming networks often ignored by EU scholars. Even though the Council is closed to direct lobbying, environmentalists regard the position of industry within it as privileged, especially compared to that of the environmentalist or consumer groups. National industry representatives often form part of the national delegations sitting at the Council table, since they may be part of a panel of 'experts' or technicians on a subject.

From the beginning, Germany, the Netherlands and Denmark were allied against the rest of the Council, since each of them had, or wanted, strict recycling or recovery legislation at the national level. They feared that the Packaging Directive would mean a retrenchment of the policy and a lowering of their standards. The votes of these three states, however, were not sufficient to stop the passage of the directive. The Council's common position, adopted against the votes of the three 'green' states, lowered the targets for recycling and recovery substantially from the Commission's proposed directive. However, as a compromise, these 'greener' states were allowed to pass more stringent national standards, providing these did not interfere with the internal market. At the same time, the less environmentally progressive states such as Portugal, Greece and Ireland were given extra time to implement the directive, and were allowed to derogate with lower targets because of their low levels of packaging consumption. The Council presented its common position to the Commission and Parliament in March 1994.[25]

Under the SEA, as noted above, the Parliament was given the right of a second reading under the co-operation procedure. During the time that the Council was

considering the amended directive, the Maastricht Treaty came into force (in November 1993). This meant that when the Parliament took up the Council's common position in March 1994, the Packaging Directive, having been based on Article 1 100a, was now subject to the new 'co-decision' procedure. As a result, if the Council rejected the Parliament's position after the second reading, it would have to adopt its common position, without the Parliament's amendments, by unanimity, or face a Conciliation Committee of the Council and Parliament. Given the firm minority position of the three 'green' states, such a unanimous vote was impossible, and the MEPs knew it.

While the Environment Committee was indeed a powerful and determined force within the Parliament, there were other equally determined committees, such as the Industry Committee, which were opposed to some of the 'greener' amendments to the directive. Trade and industry groups extensively lobbied these other committees and party groupings during the second reading. Many varied groups took advantage of the openness of the Parliament to disseminate their views as widely as possible. Interviews with Parliamentarians reveal that the second reading of this directive was one of the most volatile periods of lobbying that Parliament had ever seen. In addition to the traditional lobbying of committees and party groups, lobbyists broke into MEP offices to steal documents. Then, having full knowledge of what the 'other side' wanted, they used this information to formulate their countering positions, somewhat redefining the meaning of the word 'pressure' in pressure pluralism.

The Environment Committee once again attempted to include an amendment specifying a strict hierarchy of waste management options, but this amendment was rejected by the Plenary. Golub attributes the demise of this amendment to the pressing influence of the member states, asserting that the Commission had rejected the amendment after the Parliament's first reading to make the adoption of the directive more palatable to the member states.[26] However, other evidence shows that industry groups had previously lobbied both the Commission and Parliament, strenuously opposing such a hierarchy at each stage of the directive's formulation.[27] In addition, according to a member of the Green Group, the amendment was rejected by the coalition of Conservative and Christian Democratic parties in the Parliament's Plenary. These groups were more interested in passing a directive with few repercussions for trade and industry, rather than the most environmentally progressive directive possible. The rejection of the amendment in the Plenary had less to do with national positions on the hierarchy, and more to do with keeping industry throughout Europe from bearing the cost burden of recycling and reuse efforts.

One should not discount the importance of the Parliament's second reading, and the presence of societal actors in the policy-making process during that reading. As described above, the activities of various lobby groups within the Parliament took on a new intensity at this stage. Whether they were trying to influence specific committees or political groupings, lobbyists felt compelled to try to influence the directive at this late stage, their last chance to have any influence over the directive. Prior to the SEA (for internal market policy) and TEU (for a wider range of policies), once a proposal returned to the Council for its opinion on the Parliament's first

reading amendments, the policy process was closed to societal interests. While the most important stage at which to try to influence a directive remains the policy initiation stage, the Parliament's second reading gives societal groups a chance to influence European policy much later in the process than was possible prior to the implementation of the Parliament's second reading.

In its second reading during the spring of 1994, the Parliament adopted nineteen amendments to the proposal, and forwarded the amended proposal to the Commission (A3–0237/94). One of the amendments addressed the hierarchy of waste management options that the Commission had rejected after the Parlia-ment's first reading. Another contentious amendment from the Parliament dealt with economic instruments, such as 'eco-taxes'. This amendment stated that member state economic instruments should not create distortions in competition or 'obstruct the free movement of goods or discriminate against imported goods' and should 'avoid new forms of protectionism'. The Parliament was not only pushing for the adoption of economic instruments at the Community level, but also using a lever against one of the member states, Belgium, in order to bring it to vote against the proposal. Belgium had adopted an eco-tax on packaging in order to fund its collection and recovery systems for packaging waste which might have posed a barrier to trade and competition. Under the language of the Parliamentary amendment, it would have to reject the Parliament's amended proposal in order not to endanger its own interests. Because of this latter amendment, the Parliament essentially forced the Council into a Conciliation Committee, where the two institutions could deal with each other on an equal footing.

The Commission accepted all nineteen of the Parliament's amendments. It also included a statement in its explanatory opinion concerning the fact that new forms of protectionism arising from member state use of economic instruments did indeed pose 'one of the essential potential dangers relating to these instruments' (COM (94) 204, p. 5). Finally, the amended proposal became the 'Modified Proposal Concerning the *Parliament and Council* Directive on Packaging and Packaging Waste', reflecting the Parliament's co-decision role in the policy process after Maastricht.

The Commission, after adding its opinion and the Parliament's amendments, sent the modified proposal to the Council on 25 May 1994. As expected, Belgium, the Netherlands, Denmark and Germany rejected the amended proposal, and the Council and Parliament convened a Conciliation Committee in order to work out the differences between Parliament's opinion and that of the Council. According to both environment COREPER members and Parliamentarians, the Council opposed fewer than six of the nineteen amendments proposed by the Parliament, but the key disagreement was, as the Parliament had expected, the amendment on economic instruments.

The negotiations in the Conciliation Committee took place between the Chair of the Environment Committee and the President of the Council rather than between the twelve representative members of the Parliament and the twelve members of the Council. Thus, the final bargaining on a proposal that reaches the conciliation phase is not intergovernmental, but rather interinstitu-tional. The outcome of the Committee

reflected a compromise between the Parliament and the Council. The Packaging Directive includes an article on economic instruments which allows the member states to adopt economic instruments *in the absence of* such instruments at the Community level, a position reflecting the Parliamentary rather than the Council position. In addition, the final Packaging Directive contains a statement on a preferred hierarchy of waste management options that is in the Parliament's language, replacing the language of the Council's common position.[28]

Compromise and commitment

The final outcome of the Packaging Directive reflects several compromises typical of EU policy making. Many scholars, especially those coming from international relations backgrounds, still prefer to treat the EU as if it were an international organization in which the member states are the only arbiters of policy. As the tracing of the Packaging Directive has shown, this is simply not the case. Nor are the individual member states able to control the final outcomes of directives as they were prior to the SEA which, by replacing unanimity with qualified majority voting (QMV) in the Council, has made it more difficult for states to block policy they disagree with. The advent of the co-decision procedure, with its Conciliation Committee between the Parliament and Council for Single Market legislation, further reduced the power and influence of the individual member states. In the case of the Packaging Directive, the outcome of the Conciliation Committee reflects both an interinstitutional compromise between the Council and Parliament, and a compromise among the member states. In an intergovernmental negotiation, the preferences of the member states' institution should have prevailed, yet much of the language of the final Packaging Directive came from the Parliament and the Commission. Finally, in areas that fall under QMV rules in the Council, member states have given up a great deal of individual sovereignty over policy making and implementation. In an intergovernmental state-centric institution, dissenting states would not be required to adopt, as national law, directives they opposed, as the three dissenters were in the case of the Packaging Directive.

In addition to the compromise among the institutions and the member states, the decision-rule changes of the SEA and TEU have opened up the policy process to societal actors. In the case of the Packaging Directive, it is clear that industry had a great deal of influence during both stages of policy initiation and decision making. In the policy initiation stage, industry was both able to participate with DG XI in policy formulation through the formal consultation procedure, and later to lobby it and other Directorates General (DGs) effectively. The Commission's proposed Packaging Directive steadily became more reflective of industry's interests as it developed. In the decision-making stage, industry was especially effective in influencing the wider body of Parliament during its second reading of the directive. Only the strength of the Environment Committee within the Parliament allowed the amendments on eco-taxes and a strict hierarchy of waste management options to pass in the Plenary.

Industry associations were not the only societal actors involved in the Packaging Directive. Environmentalists also participated in DG XI's formal consultations at the

earliest stages of policy formulation. DG XI's commitment to environmental protection and its ongoing relationship with environmentalists ensured that, while changes in the proposed directive reflected industry's point of view, the Commission's targets for recycling and recovery in its final Proposed Packaging Directive remained high. Environmentalists, however, are not as well organized and equipped for lobbying in the EU as are industry associations. The industry organizations at the European level are better staffed than their environmental counterparts, and the member organizations at the national or local levels that they represent also tend to be better staffed and funded. The informal relationships that environmental organizations have with members of the Commission and Parliament counterbalance their lack of money and staff to a large degree, but environmentalists are not the ones who implement the policy on the ground. Since industry must implement the Community's legislation, its input into directives is vital; hence the Commission's efforts to set up formal consultative committees within DG XI at the early stages of policy formulation.

The Packaging Directive reflects one final, and important, compromise: between Single Market policy and environmental protection policy. This directive had to reconcile both policy aims. Because of the lack of Community leadership in the area of packaging waste, several member states already had taken matters into their own hands. Their legislation threatened to pose, or already had posed, barriers to trade among the member states. Strict recycling and recovery requirements in one country could mean that industry in another country would not be able to afford to export products to the first country because of the high costs of managing the ensuing packaging waste. In addition, there was the very real threat that the countries with strict legislation on recycling and recovery would be unable to manage the input of waste to their treatment facilities and would ship the waste to other states with more lenient regulations.

The Packaging Directive was an attempt to preserve and protect Europe's environment as landfills reached capacity in many member states. It was also an attempt to harmonize packaging waste legislation, over time, across the Community to prevent trade imbalances and to avoid the creation of pollution havens in states with less stringent environmental legislation. Environmentalists were unanimously disappointed in the final result of the Packaging Directive, as were the Greens in the Parliament. They saw the requirements set out by the Packaging Directive for recycling and recovery as a sell-out to industry. They were unhappy even with the concession given that member states may set higher targets, because it was accompanied by the requirement that they be able to handle the recovery and recycling operations themselves. However, this requirement effectively eliminates the incentive of shipping waste to other countries. While environmentalists may still feel that industry is the enemy, the informal working relationships between industry associations and members of DG XI and the Environment Committee in Parliament show that the representatives of the Community's institutions would rather work in concert with industry than at cross-purposes with it. Industry associations such as the European Recovery and Recycling Association (ERRA) began to participate

immediately after the passage of the Packaging Directive with the Commission in order to harmonize labelling requirements on packaging across the Community. Industry representatives interviewed in researching the development of the Packaging Directive displayed a clear commitment to environmental protection in their operations. Even in the development of this directive, the industry associations with moderate views that recognized the environmental impact of their operations were more likely to have their positions reflected in either the Commission's proposal or the Parliament's amendments.[29]

The Community's commitment to sustainable development is demonstrated in its Fifth Action Programme as well as in its international commitments to policies centred on that concept. In addition, the inclusion of environmental protection in other policy areas after the SEA reinforces the idea that environmental protection and free trade are not incompatible. Community legislation does not entirely remove the member states' ability to act in environmental policy. To be sure, it circumscribes it, but it limits the disparities in legislation that might lead to a 'race to the bottom' in environmental legislation. In the Packaging Directive, as well as in most environmental legislation with a Single Market impact, member states' economic conditions are taken into account. While the 'greener' states may derogate from Community legislation by setting higher targets that do not interfere with the functioning of the Single Market, the less developed member states are allowed a transition period in which to apply Community legislation. While there are admittedly still many problems with implementation and enforcement, this multispeed approach to environmental legislation has had the net effect of raising the floor of EU environmental legislation, without lowering the ceiling.

Notes

1 As Sbragia notes, the Court, Commission and Parliament have a non-territorial dimension that co-exists with and is stronger than the territorial dimension in these institutions. The territorial dimension is paramount in the Council of Ministers and European Council. Alberta Sbragia, 'The European Community: a balancing act', *Publius: The Journal of Federalism* 23, Summer 1993, p. 28.

2 The Commission has the sole right of policy initiation, but the member states, through the Council of Ministers or European Council, can make policy recommendations to the Commission.

3 See, for example, Robert Hull, 'Lobbying Brussels: a view from within', in Sonia Mazey and Jeremy J.Richardson (eds), *Lobbying in the European Community* (Oxford: Oxford University Press, 1993); John Peterson, 'Policy networks and European Union policy making: a reply to Kassim', *West European Politics* 18:2, April 1995, p. 403.

4 Hull, 'Lobbying Brussels'; Peterson, 'Policy networks', p. 403.

5 Article 100a of the Maastricht Treaty deals with Single Market legislation. Environmental policy having an impact on the Single Market falls under this article.

6 The most important have been the *Titanium Dioxide* case (Case 300/89, *Commission v. Council),* the *Waste* case (Case 155/91, *Commission v. Council*), and the *Belgian Waste* case (Case 2/90 *Commission v. Belgium*).

7 Later amended by the 1991 Waste Directive Dir 91/156, OJ L 1991, 78/32. Such Framework Directives that lacked specific targets or left implementation and target setting to the member states were typical of pre-SEA environmental legislation. The unanimity decision rule in the Council meant that many of these directives represented lowest common denominator (LCD) solutions to problems.

8 Germany, the Netherlands and Belgium either had recently adopted or were formulating packaging waste legislation of their own, some of which would have posed non-tariff trade barriers to packaging from other member states. For an in-depth description of the various national packaging waste plans of the member states, see Sergio Mastropierro, *The Evolution of Waste Legislation in Belgium, France, Germany and the European Union and Their Impacts on the Management Systems of Packaging Waste* (Brussels: European Postgraduate Programme 1993/1994 in Environmental Management, The European Recovery and Recycling Association, 1994).

9 Whatever causes a barrier to trade, or the movement of one of these, is unacceptable under Article 30 of the Treaty of Rome. In theory, any environmental measure by one state that either restricts the import of other states' goods, or makes them more costly, would be incompatible with the internal market.

10 The Treaty provides a provision in Article 36 for member states to restrict trade if such trade poses a threat to the protection of human health, animals and plants. Article 36 of the Treaty also states that such restrictions or prohibitions should not 'constitute a means of arbitrary discrimination or a disguised restriction on trade'. European Communities, *Treaty Establishing the European Community* (Luxembourg: Publishing Services of the European Communities, 1961).

11 Stanley P.Johnson and Guy Corcelle (eds), *The Environmental Policy of the European Communities,* 2nd edition, International Environmental Law and Policy Series (London: Kluwer Law International, 1995).

12 M.H.A.Porter, *The Lobbying of the European Commission over the Packaging and Packaging Waste Directive* (Brussels: European Recovery and Recycling Association, 1994), p. 23.

13 The Commission as a whole often seeks the help and information of outside experts. In addition, the Commission needs to develop a proposal that has a chance of passing through both the Council of Ministers and Parliament for final adoption into EU law. For this reason, many Directorates in the Commission are open to the advice, opinion and expertise of outside parties.

14 Porter, *The Lobbying of the European Commission,* p. 23.

15 Commission of the European Communities, *Towards Sustainability: A European Community Programme of Policy and Action in Relation to the Environment and Sustainable Development* (Brussels and Luxembourg: Office for Official Publications of the European Communities, 1993).

16 The meetings were held between DG XI and the representatives of specific interests in order to garner both information and support for the proposed directive. Meetings with the member states' representatives were held on 25–26 April, with trade and industry groups on 29 April, and with environmentalists and consumer groups on 2 May. Porter, *The Lobbying of the European Commission.*

17 Porter, *The Lobbying of the European Commission,* p. 25.

18 Porter acknowledges the significant overlap in membership of industry representatives: they endorse their individual company position, belong to European-level trade and industry associations, and they participate in national industry organizations. Porter, *The Lobbying of the European Commission,* p. 14.

19 Porter, *The Lobbying of the European Commission,* p. 15.
20 Porter, *The Lobbying of the European Commission,* p. 25; Jonathan Golub, 'State power and institutional influence in European integration: lessons from the Packaging Waste *Directive*', *Journal of Common Market Studies* 34:3, September 1996, pp. 313–39.
21 It is interesting to note that until the early 1990s, according to Laurens Brinkhorst, former Director-General of DG XI, industry mainly lobbied through other DGs more favourable to industry's position. Today, however, one long-time Commission official estimates that 95% of visitors or lobbyists to DG XI now represent industry. He believes that despite the environmental focus of DG XI, the long-term effect of constant industry lobbying, information and influence has an influence on the outlook of Commission civil servants.
22 Porter, *The Lobbying of the European Commission;* Golub, 'State power and institutional influence', p. 319.
23 See Ingrid Rigler, *The Packaging and Packaging Waste Directive: Lobbying at the European Parliament* (Brussels: European Recovery and Recycling Association, 1994), for a detailed analysis of those who lobbied the Parliament, and when.
24 This working group had actually been considering the Commission's proposal of August at the same time as the Parliament's first reading, but the Council cannot deliver its common position until the Parliament has given its first reading.
25 Golub argues that the lower targets of the Council's common position reflect the continuing power of the member states in the EU governance process. However, given the dissenting positions of Germany, the Netherlands and Denmark in this matter, I believe that it is not the individual member states that retain the power, but rather the Council as an *institution* that continues to wield power and influence. See Golub, 'State power and institutional influence'.
26 Golub, 'State power and institutional influence'.
27 Porter, *The Lobbying of the European Commission,* pp. 27–9; Rigler, *The Packaging and Packaging Waste Directive.*
28 OJ L 365/10 1994 (Art. 15). The Packaging Directive states that 'reuse and recycling should be considered preferable in terms of environmental impact'. The Council's position read that 'reuse, recycling and recovery can be *considered as equivalents* for the purposes of reducing the environmental impact of packaging' (COM (94) 204, emphasis added).
29 Porter, *The Lobbying of the European Commission;* Rigler, *The Packaging and Packaging Waste Directive.*

Further reading

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Chapter 12
States, sovereignty and trade

Geoffrey Allen Pigman

The nation state has traditionally been viewed as the key actor in the politics of international trade. In this traditional view, the government of a nation state articulates the political interests of its constituents in making trade policy and negotiating (or choosing not to do so) with other governments and international actors to achieve policy objectives. A more contemporary view holds that nation states have had their power eviscerated by the rise of transnational capital, technology and international organizations. The broad aim of this chapter is to investigate whether either view is valid for trade politics in the contemporary world economy.

Trade politics has grown up together with the development of the nation state since the seventeenth century. Governments, as they expanded their control over territory, populations and economic resources, increasingly used their power to regulate flows of goods, services, capital, knowledge and labour across established borders. Governments' trade policies, and their means of implementation, came to result from an interaction between domestic political forces and between those forces and the governments of other states. In order to claim authority to wield power over trade, as with other aspects of international relations, governments had to rely upon devices to legitimize that authority against competing claimants both within and external to the state. Such devices included the use of notions of state sovereignty and the construction of legal systems to delineate and control economic activity, both within the state and with external actors. Governments have been able to secure popular support for a notion of sovereignty and a legal system that served their interests, which themselves are framed through processes of political bargaining, by influencing public discourse on trade and other international economic issues. By presenting trade issues and choices to the public in particular ways, government leaders have been able to shape public discourse and thereby affect the policy preferences formed by their constituents.

The emergence of an integrated international economy in the nineteenth century led to tremendous growth in international trade, but also to increasingly severe clashes between nation states over trade and other economic issues. Many perceived the collapse of the international trading system in the 1930s as a major contributing cause of World War II. This in part motivated governments in 1947 to engage in an extensive programme of international trade co-operation, wherein they pooled or shared their power to create a rule-based international trading system, the General

Agreement on Tariffs and Trade (GATT). Yet in the period since World War II, the set of phenomena often described as 'globalization' has posed more fundamental challenges to the nation-state-based international trading system. One of the most profound effects of this tremendous increase in flows of goods, services, capital, knowledge and labour across traditional state borders in the late twentieth century has been to problematize the nature of the state itself and, in particular, what constitutes sovereignty. As dominant material interests have shifted in response to structural changes, such as the evolution of production, information, transport and communications technology, the prevailing notion of state sovereignty has changed, with important consequences for trade politics. The emerging constellation of dominant economic interests in late twentieth-century industrial states has brought this about by reconstructing the discourse of sovereignty to privilege a different view of state sovereignty in political debate.

The 1994 debate in the United States over the ratification of the agreement reached in the GATT Uruguay Round of multilateral trade negotiations that created the World Trade Organization (WTO) illustrates and explains this process well. Many of the objections to US membership in the WTO, voiced both in Congress and amongst political elites, the media and academics, centred around the idea that by accepting the jurisdiction of the WTO in trade disputes with other states decisions would be binding and take precedence over rulings of US courts. The US government would thus be surrendering a vital element of US sovereignty to a supranational or transnational body. Proponents of the Uruguay Round generally, and of the WTO in particular, argued that creation of the WTO was directly in US national commercial policy interests because the enhanced trade dispute resolution mechanism it embodied would result in speedier, fairer resolutions of US trade complaints against other states. Moreover, WTO decisions would be binding, compulsory and more enforceable than panel findings in GATT disputes to date. This particular debate over the sovereignty implications of US WTO membership can be seen as part of an overall discourse of sovereignty[1] that historians have tended to place in the context of a lengthy history both in American political discourse and in Enlightenment philosophy of political economy. The employment of the sovereignty discourse in the debate over the WTO represented a new manifestation of a long-running 'place-based' American fear that has not significantly declined, notwithstanding major structural changes in the international system and international economy.[2] The continuing presence of such fears of loss of sovereignty indicates that the project of reconstructing the discourse of sovereignty in the US context is incomplete and may remain so. As such it may still pose a threat to long-term US participation in the WTO and willingness to abide by its rules and decisions.

US interests in the Uruguay Round

The GATT Uruguay Round agenda was largely shaped by US economic interests that had evolved in the early 1980s.[3] For the first three decades after World War II, the integration of the global economy through greater interdependence of trade, investment

and finance was increasingly important, both for the US domestic economy and the increasing number of American firms with overseas operations. Trade dependence of the US economy since World War II had more than doubled.[4] However, by the early 1980s the international coalition favouring trade liberalization was fragmenting for a number of reasons. The easiest part of trade liberalization, tariff cutting on trade in manufactured goods, had been for the most part completed by prior multilateral rounds, leaving a more difficult and contentious agenda of agricultural goods and services trade liberalization, non-tariff barriers and trade-related issues in investment and intellectual property. For US policy makers, the period since the late 1960s was a time in which US interests appeared to diverge progressively from those of the international economy at large, as relative gains in output, trade and global market share were won by other states at the expense of the United States.[5] Numerous American and US-based firms and industrial associations, some of which from the 1960s onwards had sought and received legislated relief against increasing competition from imports, increased their demands for protection as competition from Europe, Japan and newly industrializing countries grew. The demands of affected firms and industries were exacerbated after 1980 by what they perceived as the effects of the first Reagan administration's peculiar combination of laissez-faire economics where trade policy was concerned and loose fiscal policy. The latter resulted in the sharp rise in the dollar's value, which damaged the price competitiveness of US exports. The non-interventionist orientation in trade relations meant that, until pressed hard by industry and Congress, the administration showed a lack of interest in utilizing existing statutory remedies against imports.[6]

But in the 1980s, American firms dependent upon exporting found that their interests in lowering foreign market barriers to imports of American products closely converged with the interests of firms in other states that were seeking to limit US use of unilateral, domestically legislated, barriers to imports. Hence a transnational coalition in support of a new GATT round emerged, one of whose principal goals would be to strengthen and streamline the GATT's existing dispute resolution mechanism.[7] The principal complaint shared by American firms seeking access to markets traditionally closed by non-tariff barriers and non-American firms seeking access to the US market was that the GATT dispute resolution mechanism was too slow and, by requiring decision to be taken by consensus, too easy to block. US officials in the Reagan, Bush and Clinton administrations regarded dispute resolution reform as a major means to advance US economic interests consistent with GATT-based multilateralism.[8] For GATT system supporters, a new dispute resolution mechanism also formed the heart of a broader project of completing the long-delayed formal architecture of the GATT as an international organization.

The enhanced dispute resolution mechanism to which negotiators eventually agreed differed from its predecessor in several important respects. Under the new mechanism, timetables for hearing and panel ruling on disputes are accelerated. Panel findings are considered for adoption by a new Dispute Settlement Body (DSB), consisting of all WTO members, which will adopt panel recommendations. The DSB is empowered to authorize retaliation in the event of non-compliance by states with panel recommendations.[9] The key difference from the old dispute resolution system

is that, once a decision is adopted by the WTO, it is considered binding upon the country affected. It is important to note, however, that a WTO decision binds a member state under the terms of the state's signature of the treaty establishing the WTO, in the way that any other international treaty commitment is considered binding under international law.[10] But an affected state must act to implement a WTO decision under its own domestic law. WTO decisions have no superseding authority over domestic laws or courts of member states and no force of domestic law themselves.[11]

The public debate

Despite the relatively straightforward globalization-driven shift in the interests of American and US-based firms towards support for a strengthened GATT trade dispute resolution mechanism, competing notions of sovereignty made the debate complex and acrimonious. The locus of action in the US debate over the WTO was Congress. Debate in Congress, whether floor debate, committee meetings, hearings or other meetings, formal and informal, is at the core of US foreign policy discourse, in which what constitutes policy, what is counted as 'foreign' and what is 'American' are continually reconstituted and redefined.[12] Under US trade and treaty law the US Senate was required to ratify the GATT Uruguay Round final agreement, and both houses of Congress had to pass legislation that would implement the commitments undertaken by the United States in signing the final agreement. Hence the public campaigns for and against the WTO focused on members of Congress who would be casting votes on the relevant legislation. The sovereignty discourse formed a part, but by no means the whole, of both the public debate and the debate within Congress over joining the WTO.

The way in which the argument was conducted and the alignment of the coalitions indicated that the WTO debate was not simply a contest of strength between well-staked-out coalitions of economic interests, but rather involved questions of principle and ideology as well, and one in which issues broadly defined as ones of 'culture' figured. The debate over joining the WTO formed only a part of the overall debate over ratification of the Uruguay Round, a debate in which many of the other issues at stake could be linked much more directly to particular economic interests. Yet the debate over membership in the WTO took place in public and between highly unorthodox coalitions backing each position. From the beginning there was a peculiar coalition of supporters of ratification in Congress cutting across party lines and embracing both left and right as well as free traders and former protectionists.[13] The same diversity held for the Congressional opposition. Prominent backers of ratification outside Congress included all five then living former presidents, both Democratic and Republican, from Nixon to Bush. Leading opponents included former presidential candidates Patrick Buchanan and Ross Perot on the right and consumer and workers' rights advocate Ralph Nader and Sierra Club president Michael McCloskey on the left.

At the outset of the debate, groups of committed persons formed to lobby members of Congress both for and against passage of the Uruguay Round, groups bearing such names as 'GATT Now' and 'Save Our Sovereignty'. These groups

employed not only traditional direct lobbying of members of Congress, but also the more recently popular technique of direct 'grassroots' lobbying of the public (through large newspaper advertisements, media events, etc.) to shape and influence public opinion and generate public pressure on members of Congress and Senators. Public figures outside Congress took highly visible stances on the issue of ratification, either independently or in association with (or through leadership of) interest groups. The public character of this debate indicated that it was not necessarily clear to many voters (or even to many members of Congress) where their interest on the issue lay or how salient the issue was to their interests.

One of the reasons that supporters of US membership in the WTO were successful was that they were able to reconstruct the discourse of sovereignty in such a way as to make dominant an understanding of sovereignty consistent with their preferred discourse of space, which in turn reflected the redistribution of structural power in the global economy. The opposition to US membership was weakened by the fact that the two very disparate elements of the anti-WTO coalition were relying upon very different conceptions of sovereignty, which had the effect of weakening and rendering somewhat internally incoherent the arguments that they were making. The core of the case made by the opposition to WTO ratification essentially depended upon the realist, state-based conception of sovereignty and employed the discourse of place. The opposition argued that the United States, by joining the WTO, would cede a key part of its sovereignty by surrendering the right that it held under the 1947 GATT to veto GATT dispute resolution panel decisions. The WTO charter accepts a UN General Assembly style of one-country—one-vote principle rather than a system of weighted voting akin to that practised by the International Monetary Fund or the UN Security Council. Through its veto power in these latter institutions, WTO opponents argued, the United States retained the power to safeguard its vital and sovereign interests.[14]

This place-based, realist conception of sovereignty was primarily the preserve of the populist right, as public comments reported in daily newspapers by prominent anti-WTO campaigners on the right indicate. Conservative ultranationalist commentator and erstwhile presidential candidate Patrick Buchanan described WTO accession as a 'glittering bribe.... Enhanced access to global markets —in exchange for your sovereignty' and 'an insult to everything for which the Founding Fathers launched the American Revolution'.[15] Pat Choate, a trade expert and frequent critic of free trade, argued that the WTO was a foreign organization: 'For the first time in our history, a foreign body will have the right to hear challenges to any US law and rule against it as an obstacle to trade'.[16] The theme of independence being compromised was echoed in an anti-WTO television commercial run by the US Business and Industrial Council, which depicted the American Declaration of Independence being torn up.[17] Using this type of rhetoric and imagery anti-WTO campaigners sought to present the WTO to the American public as an assault upon American culture, history and nationality. The right-wing anti-WTO faction presented to the public a fundamental distinction between the American and the foreign.

The left-wing opposition to the WTO relied upon a different conception of sovereignty. For Ralph Nader and the populist left, transparency of judicial proceedings was a critical element enabling the public to be the democratic holders of national sovereignty. WTO panels, they argued, would be closed to the public and the media, and legal arguments and panel session transcripts would remain private. Moreover, no conflict of interest regulations would govern dispute panellists, and no independent appeals of WTO decisions would be possible. The system was perceived to be essentially undemocratic and inconsistent with the character of the US form of government.[18] Similarly, the left viewed the WTO's market-oriented liberal trade regime as a threat to existing US environmental and consumer protection laws. States having less stringent environmental regulation than the United States could complain to the WTO that existing US environmental laws were barriers to liberal trade, they argued. Likewise with respect to labour standards, Nader saw a substantial risk that other states could use the WTO to force the United States to reduce its stringent labour standards.[19] Nader also foresaw the danger that transnational firms seeking larger American market shares would 'hire' small-country governments to press WTO complaints against the United States designed to weaken US consumer protection, environmental and labour laws.[20]

The complexity of the discourse is evident in that although the right and left had different foci in their opposition to the WTO, revealing different conceptions of sovereignty, there were also clear areas of agreement that enabled the two disparate groups to co-operate. Perhaps the most significant area of agreement lay in their distaste for the possibility that US laws, legitimized through the domestic legislative process, could be overturned by WTO decisions. Ironically, supporters of US membership in the WTO did not contest their opponents' insistence upon the primacy of US law. Rather, supporters of accession relied on a different interpretation of the relationship of US law to the WTO. They argued that in no sense would the United States compromise its sovereignty by joining the WTO because WTO decisions had no binding effect under US domestic law. The President and Congress would always remain free to choose whether to implement a WTO directive, accept the imposition of retaliatory sanctions instead of implementing the directive or withdraw from the WTO altogether. Regarding the one-country-one-vote principle, supporters of the WTO argued that it would not function in any way like the UN General Assembly because most issues would still be decided, as under the 1947 GATT, by consensus. Issues involving the WTO Articles of Agreement—such as those concerning Most Favoured Nation status—would have to be decided by super-majorities of either two-thirds or three-fourths of voting members. Whilst this would require the United States to organize a minority coalition of states to block a measure it opposed, the dependence of other members of the WTO upon US participation to sustain the organization's viability would make this an easy task.[21]

The issue, WTO supporters argued, was not about sovereignty but about US power in the new organization.[22] Viewing the US power position without the mask of sovereignty, WTO supporters could see that despite having different institutional mechanisms from the 1947 GATT, the WTO would likely enhance US power to act

in the interests of American firms engaged in trade and US-based transnational capital. The WTO supporters' position was articulated within a discourse of space rather than one of place and thus did not presuppose the same oppositional conception of US foreign relations. Instead they advocated American construction of venues and institutions in which US interests in the global economy could best be advanced.

Supporters of the WTO in fact saw the new WTO rules as facilitating the exercise of US power over other states in trade disputes and thereby conferring direct advantages upon American and US-based firms. Julius Katz, Deputy US Trade Representative between 1989 and 1993 and chief US negotiator in the negotiation of the North American Free Trade Agreement, argued that the United States would be the principal beneficiary of the more rigorous dispute resolution provisions codified in the WTO because the United States was already the most frequent plaintiff in GATT disputes.[23] Under the 1947 GATT system, the United States frequently lost out in trade disputes because no GATT action could be taken at all except by unanimous consent, which included the consent of the offending country.[24] Steve Charnovitz, policy director of the Washington-based Competitiveness Policy Council, argued that the stricter rules and enforcement provisions under the WTO should make it unnecessary for the United States to impose trade sanctions upon other states unilaterally in trade disputes, something that brought perennial criticism upon Washington from other GATT members.[25]

The debate in Congress

The privileging of the discourse of space over that of place, with the resultant implications for the adoption of a preferred conception of sovereignty as power to shape the global economy rather than as a domestically oriented popular understanding, can be observed in greater detail in the Congressional hearing held on the WTO. The terms of the debate in Congress over the WTO were framed in a hearing held before the House Ways and Means Committee on 10 June 1994. As it was reasonably certain at the time of the hearing that ratification of the Uruguay Round by Congress would not stand or fall on the basis of the rules of the WTO, one of the hearing's primary functions was to consecrate the administration's and House leadership's conception of US sovereignty as it related to the WTO.

Acting Committee Chairman Rep. Sam Gibbons (D.—Florida) framed the parameters of the debate by indicating that the House leadership accepted the main arguments of the WTO supporters treating sovereignty as US power in the global economy. US Trade Representative Mickey Kantor argued that sovereignty extends beyond constitutional and congressional prerogatives to the state's ability to create economic security for itself in the global economy.

> The ability to build a global trading system, to increase our exports, to create jobs and to raise wages and to raise our standard of living and to create capital for our

> companies to compete in this globalized economy, not only protects our sovereignty, it enhances it.
>
> I think there is general agreement on this committee and in this Congress as to that principle.[26]

Rep. Newt Gingrich, attending the hearing although not a member of the Committee, acknowledged that the discourse of sovereignty masks a discourse of power by drawing a distinction between *de jure* and *de facto* sovereignty. Yet Gingrich's still very realist view of sovereignty as unhindered state power showed reliance upon the place discourse. Gingrich asked Kantor whether, even if the WTO would not impinge upon US *de jure* sovereignty, it would nonetheless not impinge upon *de facto* sovereignty by limiting US policy choices. Gingrich argued that an example of this *de facto* loss of sovereignty could be seen in US policy towards Serbia during the Bosnian War. In that situation the United States, in spite of wishing to end the arms embargo to Bosnia, acquiesced to UN demands to maintain it. US action in response to UN pressure, he argued, 'is not legally a surrender of sovereignty, but the functional effect is to have dropped your rights as a sovereign nation'.[27] Gingrich's interpretation of *de facto* sovereignty here is that it consists in complete freedom of policy action with no external constraints or influences. Kantor's response was that participation in international agreements on trade safeguard not only US sovereignty but also US interests.[28] The interests to which Kantor was referring clearly were American and US-based firms and financial institutions. Rep. Sander Levin (D.—Michigan), like Kantor and Gingrich, understood sovereignty as power and concurred with Gingrich's observation that *de jure* sovereignty was not threatened by the WTO, but that US interests could sometimes be open to challenge in ways that they had not been under the 1947 GATT. Levin took a view of US material interests close to that of Kantor, relying upon a space-based view of US interests in the global economic environment of the 1990s as on balance being best served by participation in the WTO.

The US Chamber of Commerce, which represented the interests of many US-based firms before Congress, made this point even more explicitly. Its position concurred with those of Kantor, Gingrich and Levin that the important determinant of US interests regarding WTO membership was its effect upon US power in the sense of leverage in negotiating situations, not US sovereignty in an abstract or juridical sense. Willard A.Workman, Vice-President, International, of the US Chamber, stated that

> [T]he Chamber strongly supports the GATT Uruguay Round Agreement and has concluded that the WTO does not infringe upon US sovereignty. Furthermore, we have concluded that the WTO offers the United States additional leverage with which to achieve greater fairness and timeliness in world trade dispute resolution and thereby would make a major contribu- tion to our economic interests.[29]

Importantly, some but not all of the opposition arguments to joining the WTO also explicitly understood sovereignty as power. They tended to focus upon US bargaining power in trade negotiations as being the real issue at stake, as well as referring to that leverage as the relevant aspect of sovereignty to be considered. However, unlike the proponents'

arguments, they relied upon a discourse of place that presupposed an oppositional view of the United States with respect to other actors, and that privileged the maximization of state power over the interests of transnational capital. Dr William Lovett, a professor of law and economics at Tulane University School of Law, testified that he did not regard technical loss of sovereignty as the issue at all, but rather the question of whether the United States is weakening its *de facto* bargaining leverage. Lovett's fear was that this weakening had occurred in the Uruguay Round, as the United States has accepted weakening of remedies on subsidies, dumping and intellectual property. Lovett regarded the 1947 GATT as better protecting US sovereignty than the Uruguay Round because it allowed wider latitude for the use of domestic US trade law remedies. According to Lovett, US domestic law gives the United States greater bargaining leverage in trade negotiations than the WTO would. The use of safeguards and Voluntary Restraint Agreements, for example, are allowed under the 1947 GATT but not nearly to the same extent under the Uruguay Round.[30] Responding to a specific question from Rep. Robert Matsui (D.—California) about his position on whether the WTO would compromise US sovereignty, Lovett later said: 'I would not use the word sovereignty. I think the discussion at great length has clarified that that really isn't the right verbal term of art here'.[31]

Bruce Fein, another trade attorney, concurred with Lovett (and with Gingrich) that the relevant aspect of US sovereignty is freedom of the legislature to act without external compulsion or pressure. Unlike the others, however, Fein retained the mask, valuing the notion of sovereignty itself. Fein argued that the WTO impinges on US sovereignty because its decisions would oblige Congress either to change US law or else pay a penalty. This, according to Fein, counts as compulsion, thus making the WTO more than only an advisory body:

> sovereignty is emphatically not maintained simply because a nation retains a choice between specific compliance with an international directive or economic detriment. It is, thus, no answer to the sovereignty issue raised by the WTO that the United States would retain the power to choose between economic retaliation and a change in its laws or practices or even the use of section 301 of the Trade Act.[32]

In Fein's view, imposition of international economic sanctions against a state impairs its sovereignty. Fein's interpretation of sovereignty as equivalent to power to act unhindered is clearly much more extreme than the expressed views of any of the other witnesses. He cites Supreme Court Justice Joseph Storey's ultimate realist, place-based definition of sovereignty as 'the power to do everything in a State without accountability'. Any lesser definition of sovereignty Fein considers lacking in meaning. Hence for Fein sovereignty appears to mean unconditional power, in the sense that only the most powerful state in the world could be argued to be truly sovereign, and even then not in every circumstance. Such unconditional power should not entail the obligation to submit to restrictions set by international bodies, whether voluntarily or not. The power to violate such agreements always exists in *realpolitik* terms if a state is willing to fight or else accept

the external consequences of violation. Fein was seeking explicitly and publicly to identify sovereignty with power, and with power conceived of in a particular traditional, state-centric, *realpolitik,* zero-sum fashion. But his attempt to gain public acknowledgement of the unity of the discourses of sovereignty and of power clearly failed, even amongst his fellow WTO opponents testifying, who shared his basic conception of state power.

Of the witnesses opposing WTO membership, only Pat Choate, Director of the Manufacturing Policy Project, acknowledged to a degree the discourse of space and the structural change in the global economy reflected in it. Choate's main—and rather more place-based—argument was that the United States should not voluntarily surrender power to a supranational organization. Like Lovett and unlike Fein, Choate consciously eschewed the use and definition of the term 'sovereignty', choosing instead to make his arguments directly within a discourse of power. Choate's argument was that by ratifying the WTO, the United States would be agreeing explicitly to abide by its rules and conform its laws to WTO rules. Choate's major problem was that the option to withdraw from the WTO would not be a realistic political option for the United States, given US dependence upon a liberal international economy. Choate assessed US dependence upon the system to be as great as the dependence of the other states upon it, therein recognizing the changed nature of US economic interests but not drawing the same conclusions from that understanding as Kantor or the other WTO proponents.

Conclusion

The public and Congressional debate over sovereignty did not play a deciding role in the decision of the collected members of Congress on voting for the Uruguay Round implementing legislation as a whole. The decision to back the Uruguay Round final agreement had already been made as part of a complex bargaining process between the Clinton administration (in consultation with the Congressional leadership) and domestic interest groups on the one hand and foreign negotiating partners on the other. But the sovereignty issue still had some potential to derail ratification. It attracted public attention and focused opposition to the Uruguay Round. Hence the employment of the sovereignty discourse was important for that pragmatic reason. The irony of the use of the sovereignty discourse in this instance lies in that, although it played the more general role of masking the exercise of power by the state, the state backed a space-based understanding of sovereignty as state power that opposed the traditional state-centric, place-based understanding of sovereignty embraced by WTO opponents.

The employment of the sovereignty discourse in bringing about WTO accession is important in that both proponents and opponents of US membership in the WTO were willing participants in the discourse, albeit for different purposes. Opponents of WTO membership used the sovereignty discourse in the realist, place-based, state-centric way that their predecessors always had done to articulate a view that the United States could maximize its power in the international economy by not surrendering any authority in a juridical sense to an external body. The key was that in the past, use of the state's own juridical language of sovereignty as power was

successful for those seeking to avoid US participation in international organizations (as business leaders did in opposing the Havana Charter). They were successful because their conception of sovereignty was shared by a sufficient number of legislators to enable them to prevail politically. The Clinton administration was quite prepared to use the juridical language of sovereignty both to justify and consecrate its official, changed position regarding US maximization of power in the international economy in light of its overall objective of locking in US gains from the Uruguay Round. The Congressional leadership too, having changed its conception of sovereignty as power in line with that of the Clinton administration, was also prepared to employ the sovereignty discourse in this role. Virtually the entire debate in the hearing was conducted amongst lawyers employing legislative-juridical language to discuss an issue that was fundamentally not juridical in nature, but rather concerned the changing balance of power between states and transnational economic interests in the global economy.

At a broad level the US debate on joining the WTO illustrates several important features of contemporary trade politics. Structural change in the global economy after World War II has redistributed the balance of economic power both within and between nation states in the direction of transnational interests that benefit from cross-border flows of goods, services, capital, knowledge and labour. This shift of material interests has undercut the traditional role of nation state governments in regulating cross-border flows. Among other things, it has given support to codification of multilateral rules for liberal trade backed by supranational enforcement authority. Responding to the interests of transnational capital, leaders of nation state governments have appealed to different understandings of state sovereignty in legitimizing their authority to use state power to participate in multilateral trade regimes such as the WTO. Hence it is too simplistic to argue that nation states are losing power to supranational bodies in contemporary global trade politics. The US debate on joining the WTO rather supports a view that shifting economic interests are prompting nation state governments to use their power to promote their interests on the global stage in changing ways.

Notes

1 The characterization of the debate over sovereignty as a discourse is taken from Joseph A.Camilleri and Jim Falk, *The End of Sovereignty? The Politics of a Shrinking World* (Aldershot: Edward Elgar, 1992), p. 2, wherein they describe the discourse of sovereignty as part of an essentially realist way of thinking about the world in which nation states are the principal actors and centres of power.

2 For a discussion of 'place-based' sovereignty, see David Novey, *The Condition of Postmodernity* (Oxford: Basil Blackwell, 1990).

3 Jeffrey Schott and Johanna W.Buurman, *The Uruguay Round: An Assessment* (Washington, DC: Institute for International Economics, 1994).

4 Michael C.Webb and Stephen D.Krasner, 'Hegemonic stability theory: an empirical assessment', *Review of International Studies* 15, 1989, p. 192.

5 I.M.Destler, *American Trade Politics,* 2nd edition (Washington, DC: Institute for International Economics, 1992), pp. 44–53.
6 Destler, *American Trade Politics,* pp. 57–8, 118–22, 153–61; Henry Nau, *The Myth of America's Decline* (Oxford: Oxford University Press, 1991), pp. 196–205.
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12 David Campbell, *Writing Security: United States Foreign Policy and the Politics of Identity* (Manchester: Manchester University Press, 1992).
13 James Gerstenzang, 'Trade accord confident of Senate approval', *Los Angeles Times* 1 December 1994, p. A6.
14 James Risen, 'New trade body's power called overrated', *Los Angeles Times* 2 December 1994, p. A18.
15 Buchanan quoted in Helene Cooper, 'World Trade Organization created by GATT isn't the lion of its foes or the lamb of its backers', *Wall Street Journal* 14 July 1994, p. A12.
16 Risen, 'New trade body's power'.
17 Cooper, 'World Trade Organization'.
18 Julius L.Katz, 'GATT is threatened by the squeamish…', *Wall Street Journal* 30 August 1994, p. A10; Ralph Nader, 'Drop the GATT', *The Nation* 10 October 1994, pp. 368–9.
19 Katz, 'GATT is threatened'.
20 Ralph Nader, 'WTO means rule by unaccountable tribunals', *Wall Street Journal* 17 August 1994, p. A12.
21 Katz, 'GATT is threatened'. Their argument followed exactly the 1949 argument put by Wilcox in favour of the United States joining the ITO, which contained similar voting mechanisms to that of the WTO. See Claire Wilcox, *A Charter for World Trade* (New York: Macmillan, 1949), pp. 196–7.
22 This comports more closely with an understanding of sovereignty articulated by Foucault, who regarded the discourse of sovereignty as inevitably masking a discourse of power. Foucault interpreted discourse as an intelligible text that reveals a conflict between powers, a conflict not reducible to an academic dialogue or debate. Foucault saw sovereignty explicitly as a juridical term for power employed by the political right, which he counterposed against a leftist formulation of power in terms of the state apparatus. Rulers of states have used the conception of sovereignty to conceal their exercise of power over their subjects through legal structures, something Foucault regarded as unhelpful to the understanding of the exercise of power as an historical phenomenon.
23 Katz, 'GATT is threatened'.
24 Risen, 'New trade body's power'.
25 Charnovitz, 'We can abide by global rules', *Los Angeles Times* 18 July 1994, p. B7.
26 House of Representatives, 'The World Trade Organization', Hearings before the Committee on Ways and Means, 103rd Congress, 2nd Session (Washington, DC: USGPO, 10 June 1994), p. 21.
27 House, 'The World Trade Organization', p. 26.
28 House, 'The World Trade Organization', p. 32.
29 House, 'The World Trade Organization', p. 47.

30 House, 'The World Trade Organization', pp. 69–74.
31 House, 'The World Trade Organization', p. 113.
32 House, 'The World Trade Organization', pp. 101–3.

Further reading

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Chapter 13
The World Trade Organization

Robert Wolfe

The global trading system is a considerable political achievement as well as an amazing economic phenomenon. Changes in the technology of transportation and communication have been a powerful force for global integration or 'globalization', but only the increasing sophistication of global governance ensures systemic stability. Markets in some sectors may approach global size, but communities are still resolutely local. The World Trade Organization (WTO), part of the governance of the world economy, is a forum for the management of the global trading system.

The modern trading system depends on insights about comparative advantage first advanced nearly two centuries ago, and it depends on a long process of institutional innovation beginning in the free trade era of the mid-nineteenth century. The closed international economy of the 1930s was widely seen to have contributed both to making the Depression worse and to hastening the onset of another war. States learned that the benefits of open exchanges cannot be obtained, nor the perils avoided, without co-operation, for both unrestricted exchanges and closed markets can be detrimental to peace and prosperity. The postwar system was designed to avoid both poverty and instability, to reconcile international openness and domestic autonomy. In short, the General Agreement on Tariffs and Trade (GATT), which entered into force on 1 January 1948, was a compromise between the need to end the managed trade of the 1930s and the equal imperative of preserving the social innovation of the New Deal.

The WTO came into existence on 1 January 1995 as the successor to the GATT. The GATT, formally an agreement not an organization, made an enormous contribution to the development of an open, liberal and multilateral system of trade and payments, but globalization gradually exposed the weaknesses of its fragmented institutional structure. With more countries becoming active participants in global exchanges, therefore wishing to be active in the elaboration of the system, and with the scope of the system expanding to include new issues such as services and intellectual property, a new organization was essential. The WTO became the capstone achievement of the Uruguay Round of multilateral trade negotiations (1986–94), the eighth and last held under the auspices of the GATT.

Scholarly work in international relations is often concerned with the behavioral problem of co-operation among states, but this chapter centers on the substantive problem of governance. I discuss the political basis for governance of the trading

system, describe how it is carried out in the WTO, provide an example of how the system worked in the domain of telecommunications, and consider the organization's coming challenges.

The WTO and the trade regime

The multilateral trading system, the 'trade regime', is a social institution created by governments to manage their interdependence with each other. The concept of multilateralism refers to the constitutive rules that order relations in given domains of international life. Within this architectural form there are 'regimes', which are more concrete than an order, and formal international organizations, which are palpable entities with headquarters and letterheads.[1] The WTO as an international organization is the concrete embodiment of the trade regime. In this section I describe its norms and principles; in the next section, I describe regime rules and decision-making procedures, its instrumental form.

The normative framework of the regime is best captured by the concept of 'embedded liberalism', which describes the GATT as a continuing compromise between open international markets and the development of the domestic welfare state, a compromise that reflected differing visions of how to organize a capitalist economy.[2] This framework allowed the incorporation in the trade regime of such otherwise contradictory norms as non-discrimination, multilateral liberalization, and special and differential treatment for developing countries. It allowed states to accept the paradoxical coexistence in the GATT of the non-discrimination norms of Articles I (Most Favoured Nation, or MFN) and III (national treatment), with Article XXIV which allowed for the inherently discriminatory creation of regional agreements. Under Articles **XX** and XXI states are allowed to dispense with their obligations in certain circumstances, and Article **XXV** allowed for other states to grant a waiver of obligations, including the obligation to end quantitative restrictions in favor of price-based measures such as tariffs. The framework stressed reciprocity; respect for the major interests at stake along with multilateralism in making and implementing rules; and a series of safeguards that allowed states to limit their multilateral obligations with the consent of their partners in defense of certain domestic imperatives.[3] Claims that states at any point in time do or do not comply with all of these norms miss the point that they are contradictory by design: it is impossible to comply with all of them all the time. What matters is whether states are able to maintain the embedded liberalism compromise between allowing ever greater integration through liberalization, and the maintenance of social cohesion through measures to sustain political community. Only other members of the WTO can determine whether the compromise is holding, which underlines the importance of respect for the international settlement of disputes.

This contradictory normative framework is embedded in the broad structure and the fine detail of the WTO Agreement. The WTO is a structure of rules, and it is a container for a set of commitments that reflect the specific application of those rules. Trade liberalization, therefore, is a political process. It does not *cause* economic

change, but it ensures that government policy *accommodates* change. The WTO seeks to manage conflict between states while respecting national differences. As members, states both discuss specific trade problems, theirs and others, in the context of existing rules, and hold periodic negotiations about the rules. How states understand themselves in relation to the world trading system—their *identity* as traders—has been shaped by the trade regime just as states shaped the regime.

The trade regime is a process embodying the shared knowledge and expectations of states. The GATT and now the WTO is not and was never meant to be a 'free trade agreement' aimed at the elimination of all barriers to commercial exchange. The WTO does not act in opposition to the supposedly 'interventionist' policies of states; it is rather the instrument by which national policies are reconciled. It is a forum for the legitimation of norms and principles—a source of information; a place to negotiate rules, make decisions, and settle disputes. When states come to see themselves as being sufficiently interdependent within a given domain that they need to express their reciprocal obligations in formal agreements with explicit mechanisms for surveillance and settling disputes, then the WTO becomes the preferred locus of collaboration, aiding states to do things they could not do on their own. When the domain of the market expands, as it has with globalization, the trade regime also expands, as it did with the creation of the WTO.

One way of expressing the political logic of the WTO is to argue that a country can do whatever it likes at home, so long as firms from other countries are treated equally to each other and to domestic firms. 'Don't shoot other countries in the foot' could be said to be the basic political imperative. The claim is normative not instrumental, and the norm relates as much to stable international relations as to sound economic policy. Economists find this logic bizarre. Nothing a small country does can influence world prices, yet the whole trade negotiation process seems to economists to be built on the fiction that trade actions by small countries mainly hurt other countries, instead of themselves. Tariff reductions are called 'concessions' since they are seen as something being given up, in order to wring comparable 'concessions' from some other country, rather than as the self-interested actions that they are. From this perspective, the role of the WTO is limited to advising countries to 'Stop shooting yourself in the foot'. This advice might be useful, economists argue, if it helps governments constrain the power of domestic lobbies.[4]

Economists accept that the WTO has a role in two other circumstances. First, large and small countries alike have learned that the most effective way to be concerned about the policy of other countries is to act in concert, multilaterally. Second, economists may know that 'free trade' is best, but they do not agree on the details of what that means in every circumstance, and their views evolve. The inclusion of the then 'new' issues of services, investment and intellectual property on the agenda of the Uruguay Round, responded as much to changes in the ideas of economists as it did to changes in flows of transactions in the real economy. Even if economists did agree, consistently, expertise in itself never makes a policy politically legitimate. Part of what is essential in making trade policy—as in any other domain—is the means available to governments to learn about and agree on appropriate policy.

The world economy does not exist in some state of nature: it is a social institution. States created the trading system, the set of practices, understandings, and rules that permit exchanges across borders. That system in turn has a powerful effect on how states regulate trade. The function of the WTO is to find ways to *reconcile* difference, rather than attempt to *remove* difference. This fundamental normative basis for the regime's role is reflected in its instrumental form, the functions and structures assigned to the WTO.

The functions and structure of the WTO

The trade regime is made concrete in the WTO. The norms of the regime have proved remarkably robust, but the instrumental form of the GATT has been in constant evolution, as we might expect given the considerable shifts in the structure of the world economy. The instrumental elements of the WTO include the agreements, a set of committees, a secretariat, the members and their practices, surveillance procedures, and a dispute settlement system. These elements are described in this section, beginning with its objectives.[5]

In the Preamble to the *Agreement Establishing The World Trade Organization,* members endorse the objectives of growth, employment, sustainable development, and progress for developing countries. In signing the *Final Act* of the Uruguay Round, referred to as 'the WTO Agreement', representatives agreed 'that the WTO Agreement shall be open for acceptance as a whole'. All of the agreements, including all of the revised agreements from the Tokyo Round, were included in the WTO Agreement, and countries could accept or reject it only in its entirety. The trading system had become a Single Undertaking, ending the gradual fragmentation that had been so evident at the end of the Tokyo Round. With the aim of developing an integrated, more viable and durable multilateral trading system, the WTO provides the forum for negotiations among its members concerning their multilateral trade relations, and the institutional framework for the implementation of the results of such negotiations.

Trade policy is now the domain of other organizations, and of citizens. With a view to achieving greater coherence in global economic policy making, the WTO is required to co-operate with the IMF and the World Bank, and with other intergovernmental organizations that have related responsibilities. The WTO must also work with non-governmental organizations concerned with related matters—to this end, members have agreed to make more information about WTO activities available publicly, especially on the WTO Website, and to ensure even greater transparency in the coming years.

The WTO agreements

The WTO agreements (see Table 13.1) cover goods, services, and intellectual property. They start with broad principles for trade in goods in the GATT, for services in the GATS, and ideas in the agreement on TRIPs. The agreements typically set out the

Table 13.1 **Annexes to the agreement establishing the World Trade Organization**

ANNEX 1

ANNEX 1A: Multilateral Agreements on Trade in Goods

General Agreement on Tariffs and Trade (GATT) 1994
- Agreement on Agriculture
- Agreement on the Application of Sanitary and Phytosanitary Measures
- Agreement on Textiles and Clothing
- Agreement on Technical Barriers to Trade
- Agreement on Trade-Related Investment Measures
- Agreement on Implementation of Article VI of GATT 1994
- Agreement on Implementation of Article VII of GATT 1994
- Agreement on Preshipment Inspection
- Agreement on Rules of Origin
- Agreement on Import Licensing Procedures
- Agreement on Subsidies and Countervailing Measures
- Agreement on Safeguards

ANNEX 1B: General Agreement on Trade in Services (GATS) and Annexes

ANNEX 1C: Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs)

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

ANNEX 3
Trade Policy Review Mechanism

ANNEX 4
Plurilateral Trade Agreements
- Agreement on Trade in Civil Aircraft
- Agreement on Government Procurement
- International Dairy Agreement
- International Bovine Meat Agreement

objectives to be attained; a structure of rules; the methods of liberalization; procedures for notification; methods of implementation; a commitment to monitoring and review, often in a separate committee, along with procedures for settling disputes using the common dispute settlement system; and they often prescribe special treatment for developing countries.[6] Finally, there are the detailed Schedules (or lists) of commitments made by

members allowing specific foreign products or service providers access to their markets. For GATT, these take the form of binding commitments on tariffs for goods in general, and combinations of tariffs and quotas for some agricultural goods. For GATS, the commitments state how much access foreign service providers are allowed for specific sectors, and they include lists of types of services not subject to MFN.

WTO committee structure

The trading system is a living entity. It is valuable only if members are engaged in it, day by day. That engagement is structured by participation in the bodies created by the WTO Agreement, as shown in Figure 13.1. The WTO governing body, holder of all decision-making authority, is the *Ministerial Conference,* composed of representatives of all members, which meets at least once every two years giving the WTO the kind of regular political guidance that the GATT lacked. In the early years of the GATT, most Ministerial Conferences were held to launch a round of negotiations, but efforts were made to engage ministers throughout the Uruguay Round, both in informal meetings and in the two Ministerial Conferences at Montreal (1988) and Brussels (1990). Members hope, therefore, that the biennial meetings of the Ministerial Conference will be useful for educating peripheral countries, and that they can be used to create deadlines and packages without wasting energy on discussions about whether to have a meeting. The first WTO Ministerial Conference was held in Singapore in December 1996.[7]

In the intervals between meetings of the Ministerial Conference, its functions are carried out by the General Council, made up of ambassadors resident in Geneva, and a variety of subsidiary bodies as shown in Figure 13.1. Committees responsible for agreements tend to report to one of the subsidiary Councils; committees and working groups responsible for administration (Budget), for new members (Accession), and for agreements that do not involve all members ('Plurilateral'), report to the General Council, as do committees for new issues that allow members to consider whether to expand the scope of the WTO (Environment), and committees to consider whether members are achieving consistency and coherence in the implementation of existing commitments (Regionalism). Officials attending meetings of these bodies come from permanent delegations in Geneva, supplemented by the participation of experts from capitals. The demands of attendance at all of these meetings obviously place great strains on governments, especially less developed members who may lack sufficient numbers of qualified staff. Technical assistance for least developed members has become increasingly important in helping states to exercise their responsibilities and obligations under the complex WTO agreements.

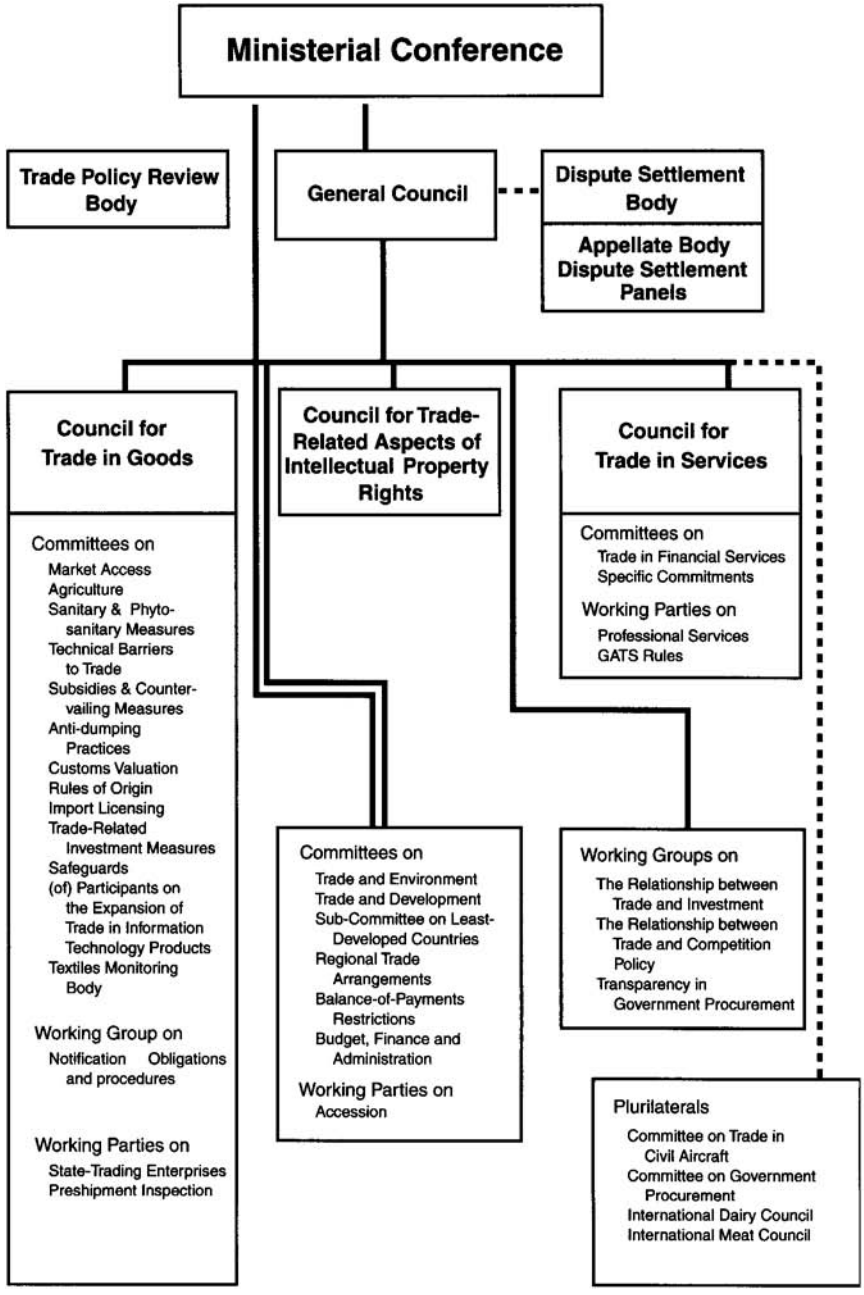


Figure 13.1 WTO structure

Source: WTO Secretariat

The Secretariat

The WTO Secretariat, located in Geneva, has around 500 staff headed by its Director-General, and four Deputy Director-Generals. The WTO budget is around US$93 million, with individual contributions calculated on the basis of shares in the total trade conducted by WTO members. The Secretariat has responsibility for administrative and technical support for WTO bodies, for negotiations, for technical assistance to the least developed members, and for monitoring implementation of agreements. It is responsible for economic and statistical analysis of trade performance and trade policy. Legal staff assist in the resolution of trade disputes involving the interpretation of WTO rules and precedents. The Secretariat is probably too small, however, to do all these things well.[8]

The WTO is still weak institutionally since the Director-General's role is ambiguous. He does not control any agenda, and he has no table that he can convene, yet he is supposed to provide leadership to his organization and to the trading system. The WTO has inherited a double-edged characteristic of the GATT: it remains essentially a member-driven contractually based organization. The WTO, like the GATT, has no autonomous power, and the Secretariat is kept on a tight leash—in contrast to the OECD, for example, which has a much larger secretariat able to take some policy initiative on its own. Member-driven organizations are responsive, but they are also prone to drift. For now, members are deeply suspicious of the organization having any autonomous capacity to move the system.

WTO practices

With the exception of the plurilateral agreements, all 132 members (as of May 1998) of the WTO can attend meetings of all the bodies listed in Figure 13.1, as can the thirty observer countries, and eight observers to the General Council. Unlike the IMF and the World Bank, no power is delegated to a smaller execu-tive group, and the Secretariat has no influence over individual countries' policies (although some analytical comments are made in the regular trade policy reviews). The WTO continues GATT's tradition of making decisions not by voting but by consensus. With so many members, none of these bodies could function if all discussions involved all members all of the time. Informal meetings of Heads of Delegation play an important consultative role, but major decisions usually emerge from a series of smaller meetings. Occasionally deadlocked negotiations can only be broken in a much smaller group, sometimes at meetings held away from Geneva in such groupings as the 'Quad' or the Invisibles Group.[9] In a market-access negotiation, a multilateral package of individual countries' commitments is the result of numerous bilateral, informal bargaining sessions.

Membership

The WTO is marked by wider as well as deeper integration: more countries are members than were Contracting Parties of the GATT, and the consequences of that membership are more significant. More than two dozen countries are engaged in the lengthy application process, including the two largest countries who had been outside the trade regime, China and Russia. Applications, which describe all aspects of a country's trade and economic policies that relate to WTO agreements, are examined by a working party. When agreement on principles for bringing a country's trade regime into conformity with the WTO is in sight, bilateral talks on market access begin between the prospective new member and individual countries based on the differing interests of the countries involved; the results are extended ('multilateralized') to all members under the MFN rule.

Surveillance of the trading system

The WTO is not merely an episodic disconnected set of negotiations, or the home of a legal text, but a set of continuous practices for implementing those agreements, including settling disputes about them, and for ensuring the harmonious evolution of the trading system. Members are associated because of their shared purposes in creating a dynamic trading system. Their common ends include developing a consensus on improving allocative efficiency in their trade policies, while their reciprocal commitments often require them to resolve distributive conflict. The need for surveillance in this context will move from informal mechanisms aimed at transparency to more formal dispute settlement mechanisms aimed at compliance. States need some means of understanding other states. It is one thing to argue in the abstract about 'optimal' policies, or new obligations; it is another to interpret ambiguous and complex reality. Part of what the WTO does, therefore, is provide a forum for this kind of intersubjective communication among states about such things as which GATT norm takes precedence in a given situation, and whether a given action is trade related and/or legitimate.

The first form of surveillance comes in the ongoing work of many of the WTO bodies shown in Figure 13.1. Many WTO agreements require member governments to notify the WTO Secretariat promptly of new or modified trade measures, often the only way to monitor implementation. The Secretariat can raise matters relevant to the covered agreement, but what matters is how 'noncompliance' is understood by the participants. In the committees, members discuss whether they got what they wanted in the complex agreements, and what the words actually mean.

The second form of transparency comes in the Trade Policy Review Mechanism (TPRM), the surveillance mechanism introduced into the GATT on a provisional basis in 1989. The TPRM reflects the assumption that greater transparency in the trade policies and practices of members will contribute both to better understanding of those policies and to the smoother functioning of the trading system. The TPRM is able to go beyond issues already subject to WTO rules to look at all policies arguably part of a country's trade-related policies. The extent of a member's impact on the trading system determines the frequency of reviews. The four biggest traders—the

EU, the United States, Japan and Canada—are examined approximately once every two years. The next sixteen countries (in terms of their share of world trade) are reviewed every four years, and the remaining countries are reviewed every six years. The policy statement of the government under review, and the detailed Secretariat report, are later published with the proceedings of the review body. The process of peer review and of publicizing the results, effectively a third form of surveillance, is based on a perception of the practical and democratic benefits of open government. The WTO now publishes a great deal of analytic information, in addition to the trade policy reviews, and it publishes the reports from the dispute settlement process.

Most of the trillions of dollars of world trade does not occasion disputes between governments, but some does. The fourth form of WTO surveillance is the *dispute settlement system.* Members use it to clarify the meaning of negotiated rules, they agree on breaches of the rules, and they monitor compliance. The system is the way in which states develop a common understanding of the sources of a conflict and the elements of a resolution. The *Understanding on Rules and Procedures Governing the Settlement of Disputes* (DSU) both codified accumulated GATT practice and created a new integrated dispute settlement system that is sometimes seen as the crowning glory of the WTO.

In the DSU, members state that the dispute settlement system is a central element in providing security and predictability to the multilateral trading system. It helps to preserve the rights and obligations of members under the covered agreements, and to clarify the existing provisions of those agreements in accordance with customary rules of interpretation of public international law. Recommendations or rulings made by the Dispute Settlement Body (DSB) must be aimed at achieving a prompt and satisfactory settlement of situations in which a member considers that any benefits accruing to it are being impaired by measures taken by another member. The preferred outcome is always a solution mutually acceptable to the parties to a dispute. In the absence of a negotiated solution, the first objective is usually to secure the withdrawal of the measures found to be inconsistent. Compensation to the complaining member is considered only if the immediate withdrawal of the measure is impracticable and only as a temporary measure pending the withdrawal of the offending measure. The last resort is the possibility of suspending the application of concessions or other obligations under the covered agreements on a discriminatory basis—that is, imposing sanctions, if authorized by the DSB.

The WTO dispute settlement system has been exceptionally active, with over 100 cases initiated during its first three years, a rate far in excess of complaints handled under the GATT. The system is being used by all members, big and small, developed and developing. The first dispute saw Singapore challenging Malaysia, and Costa Rica has taken the United States to a panel, but the Quad members are the most frequent litigants. Most officials argue that the greater level of activity is a sign of health: large and small countries rather than act unilaterally are using the system because it is perceived to be fair.

The system, administered by the DSB (the General Council in another form), is comprised of carefully selected panels of experts and a standing Appellate Body.

Disputes under *all* WTO agreements go through the same set of procedures. The system is designed to be quick, and the defending country has few opportunities to block the process. The DSB has the sole authority to establish 'panels' of experts to consider the case, and to accept or reject the panels' find-ings or the results of an appeal. The defending country can block the creation of a panel only once; panels can also be blocked by consensus. Panels normally consist of three independent experts from different countries chosen from a permanent list of well-qualified candidates in consultation with the countries in dispute. A panel's report to the DSB can only be *rejected* there by consensus. (Under the previous GATT procedure, rulings could only be *adopted* by consensus, meaning that a single objection, often coming, not surprisingly, from the defending country, could block the ruling.) Either side can appeal a panel's ruling, but only on points of law. Appeals are heard by three members of the permanent seven-member Appellate Body. The system is designed to be structured, predictable, and quick, with no case taking more than fifteen months.

Using the system does not necessarily mean adjudication: the rules encourage states to resolve their differences at any stage through consultations or conciliation. By mid-1997, about a quarter of all cases had been settled without going through the full panel process. Early resolution of disputes is a double success for the system, whose goal is always a mutually acceptable outcome. The improvements to the system might both encourage states to use it, and to settle expeditiously. It is important that the United States, whose Congress was so worried about the risks for US sovereignty, has been a big user of the system, and has tended to respect outcomes—when it lost the first case that went to the Appellate Body, the United States announced that it would bring its practices into conformity with its WTO obligations. That does not mean, however, that WTO decisions are more 'enforceable' than GATT decisions.

The WTO has an *economic* logic and a *legal* basis, but it is fundamentally a *political* entity. The trade regime is a living political creation that is in constant evolution as states agree to ignore some breaches of its rules or to reinterpret others through their practices or through the resolution of disputes. Some lawyers would prefer to see a move to a greater emphasis on adjudication of rules by legally trained people and less recourse to diplomatic fudges, but the underlying model is still one of civil, not criminal, justice. The preferred choice is that the offending state ceases the objectionable practice; the second choice is that the offending state pay compensation or suffer withdrawal of benefits previously acquired. Punishment for unlawful conduct is not contemplated or permitted. If sanctions were to be authorized by the DSB, something rarely even contemplated, they would be imposed by member countries, not by the organization—unlike the IMF, for example, which can withhold credit from an offending country dependent on its support.

The dispute settlement system is still 'diplomatic', therefore, because rulings can only be decided, implemented, or enforced by members, not by the WTO. The Appellate Body is far from being a Supreme Court, since its rulings must be accepted by governments in the DSB. The new system can help clarify a huge, complex agreement, but it does not attempt to resolve ambiguities at the expense of the governments involved, nor can its interpretations be used in place of new

negotiations. The value of the Appellate Body, therefore, is only to ensure that an *integrated* dispute settlement system remains coherent and consistent with itself, maintaining the Single Undertaking. The trading system remains a political achievement, and a work in progress.

Trade in phone calls

One of the successes of this work in progress has been its ability to provide a forum for the continuing elaboration of the rules. In February 1997, members of the WTO concluded a major negotiation on trade in basic telecommunications services that included commitments from sixty-nine governments (contained in fifty-five schedules to the GATS, the EU-15 counting as one).[10] The markets of the participants accounted for more than 91% of global telecommunications revenues in 1995.

The telecommunications sector has a dual role: it is a distinct sector of economic activity; and it is an underlying means of supplying other economic activities. Telecommunications firms are enormous in their own right, and they provide the infrastructure on which other industries depend, from airline reservation systems to electronic money transfers. Basic telecommunications are just one part of a complex regulatory domain in which technological change blurs the distinction between 'international' and 'domestic' because interconnection between the networks of different firms takes place everywhere rather than being confined to gateways.[11] The telecommunications regime based on the International Telecommunication Union (ITU), created in 1865, has proved so robust that these issues only moved into the ambit of the trade regime in the 1990s. Structural change created a need to adapt the rules, but the move required two conceptual changes. One was the international consensus that 'services' are tradeable. The other was the idea that telecommunications were one of the services that could be traded.[12]

Trade in telecommunications services is covered by GATS in principle since the four modes of supply are applicable. Accordingly MFN and national treatment also apply, in principle, Governments did not offer commitments on basic telecommunications during the Uruguay Round, however, essentially because the privatization of government monopolies was a complex issue in many countries. The GATS *Annex on Telecommunications* addressed services necessary to the provision of other services by *users* (e.g. airline reservation systems) rather than the ability to enter markets by *suppliers* (e.g. phone companies) to sell such services; the latter is addressed in each member's Schedules. Members did make commitments on access to sophisticated value-added telecommunications services, but few commitments had been made on basic voice and data transmission, the largest part of the market, and some large members were proposing to take MFN exemptions on these basic services. When the Final Act was signed, ministers created a new Negotiating Group on Basic Telecommunications in an effort to avoid locking in these derogations from the new rules.

Market-access negotiations in the new group covered not only cross-border supply of telecommunications but also services provided through the establishment of foreign

firms, or commercial presence, including the ability to own and operate independent telecommunications network infrastructure. Negotiating *trade* in basic telecommunications services, therefore, was of necessity a negotiation about *regulation* of telecommunications. The deal required investment (foreign ownership) commitments in the Schedules, and competition policy provisions. The *Reference Paper* goes beyond GATS in elaborating a set of principles covering competition safeguards, interconnection guarantees, transparent licensing processes, and the independence of regulators. The telecommunications markets of OECD countries may be opening without the WTO, but the February 1997 Agreement on Basic Telecommunications was important both because of the size of the sector, and the innovative techniques found to make an important services sector negotiable.

Challenges on the WTO agenda

In its first fifty years, the GATT helped create the conditions for the ever increasing global flows of goods, services, and ideas that, by bringing people closer together, undoubtedly contributed to peace as well as prosperity. The creation of the WTO may have seemed the culmination of this process, but it is in fact only a beginning. Ministers attending the WTO's second biennial Ministerial Conference in May 1998 had much to celebrate, and much yet to do.[13]

The most important debate concerned whether a new round of comprehensive multilateral trade negotiations is needed, the ninth since the creation of the GATT. Many negotiators, recalling previous rounds that seemed interminable, hoped that the biennial Ministerial Conferences could serve to force the agenda on negotiations conducted by the subsidiary bodies without the need for a round, or that ways could be found to allow a round as a whole to move quickly without being held up by contentious issues. It is in the nature of multilateralism, however, that the trade-offs between issues and domains will be diffuse and in some respects non-commensurable. No mechanism other than a comprehensive round exists to ensure an appropriate aggregation of issues and participants, with a forcing mechanism to ensure that at some point countries large and small accept the best deal on offer. Given the divergent interests at play on investment and agriculture, for example, or maritime transport services and textiles, it seems particularly hard to envisage progress without a new round to allow countries to win in one area what they will *believe* themselves to have lost in another.

Trade ministers mapped the way ahead for the WTO in a general declaration.[14] The language seems completely inward and self-referential, but the declaration actually records agreement on a process for deciding whether a new round will be launched at the next Ministerial Conference to be held in 1999 in the United States, the first time the GATT or the WTO will have met on the territory of its most important member. Ambassadors resident in Geneva will be discussing the 'scope, structure and time-frames' of the next steps for the WTO: should there be a round, and what should it contain? The declaration gives some guidance or structure to the so-called 'built-in agenda'.[15] Ministers asked for recommendations in four areas:

1 Developing countries attach considerable importance to a review of the implementation of the Uruguay Round, especially whether it had delivered the expected results for them, notably on textiles. The next round will certainly include the further negotiations that have already been agreed on such things as agriculture, electronic commerce, and trade in services. Members had also agreed to have 'reviews' and other new work on: the environment; institutional issues; trade 'rules' (e.g. safeguards and rules of origin); TRIPs; TRIMs; and domestic health and safety regulations.
2 Some members would like to move work on an investment agreement to the WTO from the OECD. Members will also consider whether issues related to the interaction between trade and competition policy merit inclusion. Transparency in government procurement is the other new issue already under consideration.
3 Members will consider whether the next round should include measures to assist the integration of least developed countries into the trading system.
4 Members will also consider the potential inclusion in the round of issues not yet on the table at the WTO, notably so-called 'Core Labour Standards'.

States are now clearly in one of the most important phases of the next round: deciding what it should contain and how it should be negotiated. Since the WTO is a Single Undertaking, what gets put into the frame of the negotiation at the beginning will be hard to leave out at the end.

International regimes are essential because the nature of international order is not given by some force of nature: it is a political construction that responds to change in markets and societies. The relative balance between these two organizing principles determines the nature of collective organization for individual states and for sets of states. The paradox is that an increasing role for global markets will call for an increasing role for states and their global institutions, not least in the trading system. World markets are vastly larger, and more open, than when the GATT was created fifty years ago, but the WTO is a much larger and more sophisticated institution of governance than the GATT. States want to retain the ability to regulate in the national interest, to allow the process of domestic dialogue to have a determinative influence on policy. States will only have such scope in the domain of trade, however, if the WTO is able to keep pace with globalization. The multilateral system can only remain vibrant if it responds to changes in the world economy, and to the concerns of all participants in the trading system. What matters is whether states are able to maintain the embedded liberalism compromise between allowing ever greater integration through liberalization, and the maintenance of social cohesion through measures to sustain political community.

Notes

1 John Gerard Ruggie, 'Multilateralism at Century's End', in *Constructing the World Polity: Essays on International Institutionalization* (London and New York: Routledge, 1998).

2 The idea was introduced in John Gerard Ruggie, 'International regimes, transactions, and change: embedded liberalism in the postwar economic order', in Stephen D. Krasner (ed.), *International Regimes* (Ithaca, NY: Cornell University Press, 1983).
3 Jock A.Finlayson and Mark W.Zacher, The GATT and the regulation of trade barriers: regime dynamics and functions', in Krasner (ed.), *International Regimes,* p. 274. See also Gilbert R.Winham, *The Evolution of International Trade Agreements* (Toronto: University of Toronto Press, 1992), Chapter 3.
4 In the extreme version of this view, 'political failure' is endemic, but it can be 'corrected' by using the WTO as a constraint on wayward governments subject to the equilibrium outcome of interest group competition. Bernard Hoekman and Michael Kostecki, *The Political Economy of the World Trading System: From GATT to WTO* (Oxford: Oxford University Press, 1995), p. 24.
5 This section draws heavily and without specific attribution on the description of the structure of the WTO in *The World Trade Organization: Trading into the Future* (Geneva: World Trade Organization, 1997).
6 In these respects the Agreement on Agriculture is typical. See Robert Wolfe, *Farm Wars: The Political Economy of Agriculture and the International Trade Regime* (London and New York: Macmillan and St Martin's Press, 1998), Chapter 5 and appendix.
7 For the results, see WTO, *Annual Report 1997,* Vol. 1 (Geneva: World Trade Organization, 1997), pp. 4–6, 97–100.
8 Richard Blackhurst, 'The capacity of the WTO to fulfil its mandate', in Anne O. Krueger (ed.), *The WTO as an International Organization* (Chicago: University of Chicago Press, 1998).
9 'Quad' refers to the Quadrilateral Group of trade ministers—Canada, the EU, Japan and the United States. Participants in the Invisibles Group include the Quad, as well as Argentina, Australia, Brazil, India, Korea, Morocco, New Zealand, Norway, Poland, Singapore, and Switzerland. The WTO Director-General is also invited to attend.
10 For the details see Gary Clyde Hufbauer and Erika Wada (eds), *Unfinished Business: Telecommunications after the Uruguay Round* (Washington, DC: Institute for International Economics, 1998).
11 Mark W.Zacher, with Brent A.Sutton, *Governing Global Networks: International Regimes for Transportation and Communications* (Cambridge: Cambridge University Press, 1996).
12 This section draws on Robert Wolfe, 'Farms, phones and learning in the trade regime', in Meric S.Gertler and David A.Wolfe (eds), *Innovation and Social Learning: Institutional Adaptation in an Era of Change* (London: Macmillan, in press).
13 The meeting was timed to come six months earlier than required, and the next one will also be held after an interval of only eighteen months. The third biennial Ministerial Conference, normally due in 2000, will instead be held in 1999, ensuring that this vital decision-making body does not meet during American election years.
14 WT/MIN(98)/DEC/1 available at http://www.wto.org/wto/anniv/mindec.htm.
15 For a full discussion of this agenda see the appendix of Sylvia Ostry, *The Postwar International Trading System: Who's on First?* (Chicago: University of Chicago Press, 1997).

Further reading

John Croome, *Reshaping the World Trading System: A History of the Uruguay Round* 2nd edition (Geneva: World Trade Organization, 1998).

Bernard Hoekman and Michael Kostecki, *The Political Economy of the World Trading System: From GATT to WTO* (Oxford: Oxford University Press, 1995).

John H.Jackson, *The World Trading System: Law and Policy of International Economic Relations* 2nd edition (Cambridge, MA: MIT Press, 1997).

Miles Kahler, *International Institutions and the Political Economy of Integration* (Washington, DC: Brookings Institution, 1995).

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Part III

Regions in world trade

Introduction

Regionalism is a distinguishing feature of modern trade politics, but its relationship to other levels—national or multilateral—remains a point of debate. Indeed, even the definition of region has proved somewhat elusive. This book, like much IPE writing, considers regions to be collections of states which have extensive trading links with one another. By contrast, geographers use the term regionalism to refer to subnational areas, such as US states and German *Länder,* or localized economic clusters, such as Silicon Valley.

Regionalism's effect on international trade is unclear. For some observers, the development of regional economic relationships is both natural and inevitable. It is natural in the sense that even in this digitalized age, proximity still counts for a lot, Sellers who are close to their markets have lower transport and other logistical costs, and they are apt to be familiar with local market conditions and customs. Many businesses, when first contemplating a move outside the home market, initially locate in nearby states in an effort to 'test the waters' before embarking on a more global strategy. Thus, Canada and the United States are each other's largest trading partners; the UK now conducts over 60% of its trade with mainland Europe, in spite of that state's historical place as a global trader. Regions develop around an anchor country, which acts as the motor of growth for the other economies around it. Thus, the United States, Japan and Germany are seen as the core states for North America, Asia and Europe respectively. But what about Africa and South America? In the African case, it seems clear that South Africa is starting to play this role. As for South America, perhaps the anchor is Brazil, or is it the United States, with its important role as a key market for South American goods?

The formalization of regional arrangements has alarmed some observers, who view these agreements as a threat to multilateralism as manifest in the WTO. Multilateral arrangements are, almost by definition, aimed at removing to the greatest extent possible discriminatory trading practices by forging broad agreement among countries on the rules of the game. Regionalism, by contrast, creates two categories of states: those party to the arrangement and outsiders. This, naturally, creates not one but two rule books. Indeed, regional economic agreements do seem to violate the spirit, if not the letter, of the WTO.

Each of the regions examined in this part has its own dynamic and faces unique challenges. Much attention is rightly focused on the two most important economic regions: NAFTA and the EU. As Cooper shows, the evolution of the North American political economy continues to be driven by the trade policy of the United States. The EU remains a 'superpower in progress' as Michael Smith argues. While the EU continues to evolve as a lucrative market and productive centre, doubts remain about the political capacity of the Union to play a management role commensurate with its presence in the international economy. South America has emerged from a period of political instability to embrace both liberal democracy and market economics. Wrobel's chapter demonstrates that, like Canada and Mexico, many South American states see their economic destiny laying in greater integration with the United States. The economic troubles of the Asia-Pacific through 1997 and 1998 have deeply shaken faith in the 'Asian model' (such as it was) of economic development. As Ravenhill notes, the region remains host to key players in the international trading system. Shaw and van der Westhuizen present an analysis of African political economy that is sharply at odds with the typical portrayal of Africa as an economic disaster area and reinforce some of the themes concerning patterns of actor involvement in trade politics which emerge in Part II.

Chapter 14
NAFTA and the politics of regional trade

Andrew F. Cooper

The North American Free Trade Agreement (NAFTA) has been commonly portrayed as indicative of a pervasive shift in strategy found in the contemporary international political economy. Through this broad lens, the evolution of the trilateral arrangement between the United States, Canada and Mexico is viewed as part of a wider 'trade policy revolution'.[1] As in the other major 'triad' configurations, that is to say the European Union (EU) and the Asia-Pacific Economic Co-operation (APEC), a regional option has been embraced in North America.

Consistent with this general image of the ascendancy of regionalism as a component of the international politics of trade, some considerable attention has been paid to the representative quality of the NAFTA arrangement. At the same time, however, the unique functional and geographic character of the deal should not be lost. The speed with which the negotiation and implementation of the deal took place stands out as an impressive feature, with a rapid progression from the initial agreement to negotiate in mid-1990, to the actual process of negotiations begun in June 1991, to the announcement of an agreement in August 1993, the decisive votes in the US Congress in November 1993, and the formal implementation of NAFTA on 1 January 1994. The form of the deal was also innovative, not the least because its three partners featured very different histories, levels of economic development, and cultural/social traditions. As frequently pointed out, NAFTA constituted 'the first reciprocal trade pact between a developing country and two industrial countries'.[2] In terms of scope, the significance of NAFTA continues to be marked by its extension beyond the traditional trade agenda to encompass a wide variety of non-trade concerns including investment and social matters.

NAFTA as a contested arrangement

As NAFTA has become embedded economically, it has remained highly contested politically. The debate surrounding NAFTA has been marked not only by discussions and about points of detail but by intense controversy over larger questions pertaining to its overall costs and benefits. To supporters of the deal, the logic of a trilateral deal has remained unassailable. A comprehensive free trade pact, instituted between the North American countries, opened up the prospect of an integrated market of approximately 360 million people. By 'reducing the economic significance of national political

boundaries within a geographic area',[3] the prospect of greater commercial efficiencies (though reduction of transaction costs, and economies of scale) was laid out.

The diffusion of a neoliberal economic model provided the pro-NAFTA side with a relative degree of ideological/policy coherence. By way of contrast, the anti-NAFTA forces were made up a variety of voices ranging from specific interest groups (labour, and segments of the environmental constituency) to a diffuse set of individuals, political parties and movements situated right across the political spectrum. In the United States, the anti-NAFTA struggle became associated largely with the union movement; the protectionist wing of the Democratic Party; Ralph Nader and other consumer advocates; Republican isolationists or America firsters' such as Pat Buchanan; and especially Ross Perot's 1992 populist-oriented presidential campaign.[4] Indeed, the resistance became symbolized by Perot's message that NAFTA would mean the loss of jobs or as he put it more dramatically the prospect of a 'big sucking sound from the South'. Organized opposition to the deal in the other two countries became wrapped up closely with party politics, and the bid to replace the Progressive Conservative government in Canada (1984–93) and the ruling Institutional Revolutionary Party (PRI) government in Mexico. The Canadian struggle against NAFTA was led by the 'nationalist' segment of the federal Liberal Party and the more left-wing New Democratic Party. Tapping into the sense of historical grievance and cultural sensitivities derived from the loss of territory and sense of victimization, the Party of the Democratic Revolution (PRD) was in the forefront of the anti-NAFTA fight in Mexico.

While a good deal of these campaigns could be devalued by their often crude, simplistic and overly pessimistic message concerning the economic and social consequences of NAFTA, there was no question about the impressive ability of these forces of resistance to mobilize politically. Even firm advocates of the NAFTA project were willing to acknowledge that any sense of ultimate triumph derived from winning out on this issue should be mixed with a great sense of relief. As Charles Doran has succinctly put it: 'what stands out in all three countries is how hard-fought the free trade vote was, how entrenched the industrial and labor opposition was, and how great a political leadership was necessary'.[5]

It must also be brought out clearly that if the emotional arguments associated with 'special interest', nationalist and even xenophobic elements constituted the most prominent public faces of the anti-NAFTA fight, these elements should not be considered the exclusive dimensions of this campaign of resistance. There developed as well a more considered and credible form of criticism. While not completely absent in the declaratory statements of practitioners, this second type of criticism has been located for the most part in the contributions to the NAFTA debate by a range of academic/journalistic commentators.

One source of this more attractive type of criticism relates to whether or not NAFTA serves as a building block or an obstacle to the existing multilateral trade order. In principle, the NAFTA project appeared to be generally consistent with the tenets set out by the General Agreement on Tariffs and Trade (GATT) and the World Trade Organization (WTO). NAFTA was designed to lower not raise barriers to

trade. Non-discrimination was to be practised to new entrants. The only criteria for entry was sound macro-economic policy and a commitment to liberalization. From the perspective of its supporters, therefore, NAFTA was 'designed to foster the ultimate objectives of the multilateral system'.[6]

Scepticism about this view, in practice, emerged on two different questions. With the Uruguay MTN Round still in train from 1986 to 1993, the NAFTA project was criticized by a good number of observers for sending a negative signal about the ongoing credibility of the multilateral system. Some of these critics worried about the possible demonstration or knock-on effect brought on by the United States moving towards regional arrangements.[7] Other critics expressed concern about developing countries being trapped in a tightened asymmetrical relationship to their detriment. Gerald Helleiner elaborated upon this second problem in a warning salvo against the allure of 'special deals':

> Mexico and other small countries (including Canada) attempt to advance their interests exclusively or primarily in bilateral negotiations with larger countries only at their peril. They may win some concessions via special arrangements, but there is a high risk that they will, on balance, lose much more from their contribution to an overall disintegration of existing global rules and a failure to work sufficiently to build new ones. As a developing country, with fairly limited retaliatory capacity on its own, Mexico could expect, in the longer run, to benefit greatly from an effectively functioning, nondiscriminatory multilateral system.[8]

Subsequently, these concerns have been directed towards the trade diversion effects of NAFTA. At odds with the notion of open regionalism, the implementation of NAFTA has not meant a reduction of external barriers. In an apparent effort to distinguish more explicitly on an 'us' and 'them' basis,[9] the barriers to outsiders have been raised in many cases on sectoral lines. The most sensitive of these issues has centred on the application of standards about 'rules of origin'. Goods from non-NAFTA countries become eligible for preferential treatment only if they go through a process of 'substantial treatment' in the region. The strict nature of these rules is illustrated most clearly in the auto sector, where the requirement for preferential treatment has been set between 60 and 62.5%. Given these restrictions, foreign auto and auto parts companies face an obvious choice: either to stay on the outside and face protectionist measures or to move production facilities so as to take on the status of an insider. While most visible and contentious in the auto sector, it needs to be mentioned that this system has been extended quite widely. According to one recent study, the application of these rules of origin is a mainstay in telecommunications equipment, colour televisions, printers and copiers, machine tools, and textiles as well as automobiles.[10]

Through these sorts of critical assessment, NAFTA was viewed as being an expression not of free trade liberalism but of a type of neomercantilism. The motivating force for this new geopolitical framework was not a shared sense of idealism (or even pragmatic learning) about the benefits of co-operation. Rather the drive was based on an instrumental and narrowly defined calculation of state interest.

Only by an active engagement in regional projects could material benefits be preserved in an increasingly competitive environment. National economic competition and rivalry—not the dictates of market rationality—shaped the choice of strategy.

Another source of this more thoughtful type of criticism has hinged on the question of sovereignty. The advocates of NAFTA have for the most part remained sanguine about the impact of this regional trade arrangement on the ability of national governments to intervene in economic affairs. M.Delal Baer's views are typical of this sentiment, in the suggestion that: 'By definition, NAFTA embodies a set of tri-national rules governing economic behavior. Acceptance of these rules has required fundamental modifications of traditional notions of sovereignty'.[11] Underneath this sense of equanimity is a welcoming attitude to the loss of control by national governments generally and the habit of interventionism more specifically. The various 'exceptions' accepted in the NAFTA agreement were deemed to be unnecessary 'gaps' to the logic of rationalization and harmonization, not valuable safeguards integral to the national well-being of the individual countries. These special cases included *inter alia* the application of US trade law, the exemption of energy in the case of Mexico, and the cultural 'industries' in the case of Canada.

The potential loss of manoeuvre was, in contrast, a huge concern for the antiNAFTA forces. Notwithstanding the list of exceptions, enshrined into the arrangement, there were fears that this project would cut down on the ability and/or the willingness of individual governments to take distinctively national 'self-help' measures. As one Mexican commentator put the argument bluntly: 'For many average Mexicans, NAFTA aims to circumvent and undo the Mexican's state's legal authority to intervene in the economy on their behalf'.[12] From this standpoint, the defence of sovereignty remained an absolute goal—tied in with the integrity of territory and national distinctiveness. It was not a relative goal to be bargained away by governments. The dilution of national economic control, according to the line of thinking, led inexorably over time to a loss of national solidarity and identity. A prime illustration of this thinking came out in Canada, centred on the argument that there would be a negative spillover from the NAFTA arrangement into areas such as medicare and other social services (including welfare and child care). While the traditional supporters of NAFTA expressed the view that these areas were completely 'off-limits', the opponents to the deal remained convinced that the main danger in the future would come from a racheting down of standards.

A third variant of this more considered form of debate relates to how the NAFTA arrangement was implemented. The proponents of NAFTA cast the process towards integration as a voluntary-driven one, entirely consistent with an appreciation of the benign nature of the project. The co-operative effort was considered to have evolved out of a growing awareness about the advantages of regional configurations. In accordance with Ohmae's concept of emergent 'region-states',[13] geographic proximity was characterized as going hand in hand with added efficiencies in terms of production, finance and the operation of the market.

The sceptics put a much more involuntary spin on the dynamics of integration. The major push behind NAFTA was considered to be the same set of impersonal forces which was integrating the international economy on a global basis: the production and distribution of goods and/or services of a homogeneous type and quality. What the formation of regional arrangements did was to provide a convenient stepping stone on the path to a more advanced goal, that is to say a stage after 'capitalist competition transcends…the nation-state and requires a continental, or regional, base in the gradual evolution towards global-ization'.[14]

In a similar fashion, power rather than a shared sense of purpose was privileged in the dynamic of regionalism. Regionalism was viewed as contributing to a democratic deficit. Apart from the question of whether transnational corporations came to have a 'bill of rights' unavailable to ordinary citizens, as a result of NAFTA,[15] their commercial interests were seen as enjoying a procedural dominance in the negotiating process. Lacking public accountability, the deal was done over the heads of the mass population with little or any access to non-elite input in any of the three countries. In the United States, congressional consideration of NAFTA was limited to a simple up or down decision through the mechanism of the fast-track legislation. In Mexico, NAFTA was pushed through a compliant Chamber of Senators in which the ruling PRI held a massive majority. In Canada, the policy process surrounding NAFTA was marked by its relatively closed nature in which business groups but not the rest of civil society had access.

Exploring the paradoxes of NAFTA

Standing back from these sorts of big and intensely contested questions, it is useful to look more closely at some of the details concerning the evolution of NAFTA. In this unpacking exercise, a number of fundamental paradoxes surface which illuminate both the complexity concerning the nature of contemporary trade politics generally and this type of regional project more specifically. On the surface, NAFTA appears to be a fairly straightforward issue with clearly demarcated boundaries of dispute. Looked at in greater depth, though, the distance between commonplace notions and a fuller appreciation of the nuances relating to NAFTA becomes enormous.

The first puzzle which merits attention relates to the structural foundations of the NAFTA project. With the centrality of political contestation firmly in mind, Andrew Hurrell reminds us that there are 'no "natural" regions'. It is the way that 'actors perceive and interpret the idea of a region and notions of "regionness" that is crucial'.[16] From this starting point, there is little debate about the importance of the economic dimension in laying the base for the 'North American region' as a social construct. The catalytic component for a more intensive form of regionalism was the level of economic interdependence between the United States and its two smaller partners. If restricted in the form of its *de jure* forms of regional integration up to the 1990s, the main bilateral relations present a picture of extensive *de facto* cross-border trade, investment and movement of peoples.

Still, this parsimonious account leaves a number of questions hanging. The most obvious of these questions relates to the uneven pattern of interdependence found in North America. While the level of economic interdependence between the three countries at the time of the implementation of NAFTA was impressive by any quantitative standard (approximately $US270 billion annually), there existed a huge difference between the US-Mexico and the Canada-US economic dyads on the one side and the Mexico-Canada economic dyad on the other side. In 1993, 78% of Mexican exports were shipped to the United States, with 68% of Mexican imports coming from the United States.[17] Over 80% of Canadian two-way trade was with the United States. By way of contrast to these two concentrated sets of linkages, the Mexico-Canada economic relationship remained undeveloped. Despite the spillover effect in terms of the extension of interdependence (particularly through the sourcing of components), economic contacts on this third leg of the North American triangle could not be categorized as either broad or deep.

Another set of questions relate to the means used to manage this intricate form of economic interdependence. One way of trying to manage this structural relationship is through a gradual process of institutionalization. Yet, even some of the most enthusiastic proponents of NAFTA have cautioned against an overly ambitious scenario along these lines. Alan Rugman advised, for instance, that the institutional course should be taken in a selective fashion:

> For North America, it is probably not desirable to seek the degree of political integration that exists in the EC—a common parliament, a powerful central commission, a social charter, common currency, and so on. However, it would be desirable to seek proper economic union.[18]

Another way of trying to manage this dynamic is through the expanded growth of a sense of regional identity. Certainly, a number of writers have alluded to the prospect of an extended form of North American community.[19] In the context of North American regionalism, however, any attempt to exaggerate this community formation is misleading. Notwithstanding the presence of 'multiple channels', 'social networks' and 'cross-governmental alliances' on a US-Mexico and Canada-US bilateral basis,[20] this thick multilevel pattern of interaction has not been replicated at anywhere the same level on a tri-national basis.[21]

The essential unevenness in the pattern of North American interdependence is accentuated still further when the micro-regional dimension is factored in. This feature locates the process of transnational networking not at the level of the national economy but in the form of subnational integration. Looked at within this context, the Canada-US and the Mexico-US relationships are extremely well developed. These two dyads contain a wide number of formal and informal mechanisms designed to consolidate cross-border co-operation. While too exhaustive to list completely, an illustrative sample includes such items as an Office of California-Mexico Affairs in San Diego, joint delegations to promote investment, and institutionalized meetings between US governors and Canadian premiers in a number of border regions.[22]

Behind all of these activities have been the same set of galvanizing agents: a mix of geographic proximity, economic complementarity, and infrastructure/market access. By way of contrast, the Mexico-Canada dyad once again constitutes the weak leg of the North American triangle. The findings of a 1996 study by two Canadian academics, for example, are sobering in its assessment: 'There are…no signs that NAFTA has inaugurated a vibrant era of trilateral community-building, or that the initial regime has "deepened" or will "deepen" to embrace the state-provincial level'.[23]

A different puzzle relates to the motivations—and the primacy—of the individual countries joining NAFTA. A dominant assumption among its critics has been that NAFTA needs to be looked at as a hegemonic project, intended to maintain American influence in the face of European and East Asian economic challenges of the early 1990s. In the words of Anthony Payne, this conceptual design

> tells us a good deal about the emerging US view of its position vis-à-vis the rest of the Americas in the 1990s and beyond…they sought in effect to set out and enforce new economic and political 'rules of the game' in the hemisphere.[24]

Such a top-down analysis is very necessary. The United States has had a huge stake in the evolution of the NAFTA project. Policy makers in Washington DC initially put greater emphasis on bilateral and regional options, because they appeared to offer useful demonstration effects for others in the international trading system. In particular, it was believed that flirting with bilateral or regional free trade areas would show Europe and Japan that alternatives to the multilateralism under GATT was possible. As the Uruguay Round bogged down, however, the regional approach was increasingly regarded not as a fall-back option but as a preferred first option, becoming attractive on its own merit. The high-water mark of this sentiment came in June 1990, with George Bush's call for an 'Enterprise for the Americas' with its vision of a hemispheric community.

As some astute observers have pointed out, the US motivations in support of NAFTA went well beyond the economic incentives. Foreign policy, and in particular geo-security considerations, concerning the future stability of Mexico, played an important part as well. Above all else, NAFTA was intended to lock the Mexican domestic reform agenda. As Paul Krugman wisely put it:

> NAFTA is a sort of pledge—a pledge to foreign investors that Mexican reform will continue (and that the U.S. market will remain open to goods produced in Mexico). It is also a pledge to the Mexican population that better times are coming.[25]

With the prospect of greater prosperity, concomitantly, NAFTA worked to keep Mexicans as illegal migrants out of the United States. Enhanced stability would in turn help keep issues such as the drug trade down.

As revealed by these mixed motivations, the United States was not only a demander but a reactive agent in the push for a regional trade arrangement. Leadership came not just from the hegemony but from below. Consistent with the dramatic changes

witnessed in its economic strategy, Mexico served as the activist driving force behind the project. This change of mind came about mostly by default. Mexico was hit hard by the shocks of the 1980s—tumbling oil prices, rising debt, dramatic devaluations, and the failure of import substitution industrialization and statist intervention. Accordingly, the government of Carlos Salinas de Gortari (1988–94) was galvanized to embrace a vigorous and outward-looking programme of reform. But an element of design must be factored in as well. The ideological policy inclinations of the Salinas government meshed well with this change of mind. With a confident mind-set, nurtured in American elite graduate schools, this cohort of state officials demonstrated a marked commitment to economic liberalization, privatization and a new sense of partnership.

The NAFTA initiative posed a serious dilemma for Canada. Any extension of the Canada-US trade agreement jeopardized Canada's privileged status in terms of the institutionalization of its special relationship with the United States. On the contrary, NAFTA raised the spectre that Canada would join Mexico as a spoke to the US hub.[26] The advocates of NAFTA argued, however, that Canada had little choice but to be a player in NAFTA. If regionalism created more of an imbalance in bargaining strength than did the bilateral option, the protection of Canadian interests seemed to be better achieved by taking part in the expanded negotiations rather than by remaining on the sidelines. 'Being there' was deemed essential for Canadian interests, especially if the government in Ottawa was to make its influence felt. As one Canadian official put it: 'If Canada is not at the table, it cannot make its views known—the absent party is always wrong'.[27]

This type of argument proved difficult to resist. Canada did not want to be excluded in any talks concerning the prospect of an emerging regional grouping. Forced to make a choicc, the government in Ottawa decided in instrumental fashion that 'going along' with NAFTA was preferable to being excluded from a bilateral Mexican-US free trade deal.

The shading of opinion about NAFTA

As noted throughout this chapter, a dominant feature of the NAFTA debate has been the high degree of political/policy contestation concerning the pros and cons of the regional arrangement. The merits of the deal have been debated in stark tones as a fundamental choice between the logic of economic rationality and the costs of restructuring; regionalism versus multilateralism; and the putative loss of sovereignty and national control. Despite these core arguments about the value of NAFTA becoming ingrained, around the ends and along the sides of this ongoing set of debates has seen some shading of opinion. For the shape of the NAFTA arrangement has not turned out exactly as predicted by either the original proponents or the opponents of the deal. Instead of the clear and decisive result most observers expected and hoped to get, the outcome has been far more uneven and muddled.

Progress towards a deepened NAFTA arrangement has been made in a variety of ways. Beyond the specifics of trade policy, the main advance of NAFTA is usually

taken to be the establishment of a transparent, consistent and enforceable web of rules of the game. This is particularly true in the main areas of investment and intellectual property, in which the contractual obligations of the three countries are detailed. Hufbauer and Schott highlight this feature, as providing an 'insurance policy' that reduces the hazards of doing business (especially Mexico) in the NAFTA domain.[28] Winham adds that: 'Investors now have the right to request an arbitral tribunal if host governments (including subnational governments) violate obligations under the investment chapter. This provides important increased security for foreign investment, resulting in greater stability for international transactions'.[29]

In terms of national economic development, some supporters of NAFTA have argued that NAFTA has allowed maquiladora industries (foreign-owned plants located in Mexico near the US border) to progress beyond their traditional status as 'screwdriver' assembly line operations at the lower end of the scale to the fostering of greater technology transfer and the provision of more sophisticated employment. This contention, however, remains highly controversial. Whatever progress has been made on a plant-by-plant basis, the image (and reality) of maquiladora industries remains poor because of low wages and poor conditions associated with occupational safety problems.[30] The view that NAFTA retards rather than stimulates national development is accentuated by the different slant the critics place on the stabilized 'rules of the game' in terms of intellectual property. By more tightly regulating the use of copyrights and patents, these critics maintain that one of the main effects of NAFTA will be to restrict the development prospects of the Mexican pharmaceutical industry which rely on technology transfer.

Where the uneven impact of the trade arrangement comes out most clearly is on the issue of trade liberalization. Giant strides have been made on tariff reduction via NAFTA. Moving rapidly away from its traditional habits, Mexico did away with its duties on almost half of the list of industrial goods brought in from Canada and the United States. The ongoing problem area has been non-tariff barriers (NTBs). Notwithstanding the extension of the 1989 US-Canada FTA dispute settlement provisions, through the creation of a trade commission and a system of consultations and expert arbitration panels, NAFTA leaves the questions of anti-dumping and countervailing duties largely for each country to determine on the basis of its own national trade laws. All the NAFTA provisions allow for is a determination of whether or not these actions have been appropriately applied. This system has allowed the United States to continue to take unilateral actions deemed by Canada and Mexico to be unfair, and which procedurally have continued to be time consuming and costly to fight. It also encouraged copy-cat behaviour. To be sure, by more closely harmonizing the working of its anti-dumping legislation with US and Canadian standards, Mexico could legitimately start to impose these sort of protectionist measures on its NAFTA partners. The steel industry, to give the most common illustration, is routinely susceptible to the regular intrusion of anti-dumping actions.

The introduction of NAFTA has brought to the forefront as well a host of technical questions, relating to the administration of transnational movement of goods and the

mutual recognition of standards. The way these questions have been handled seriously shakes the assumption that NAFTA brings with it an inexorable movement toward open borders. Despite the impression that business travellers can more easily obtain temporary visas, or that the transport of cargo has become less regulated, some considerable counter-momentum has built up. As the three countries have come closer, new types of control have taken over. Customs inspections have in a variety of ways grown more onerous, especially in terms of sanitary certificates. Reinforced by the 'rules of origin' requirements, the paperwork on the cross-border flow of goods has increased appreciably.

On top of all these other problems, the deepening of NAFTA was held back owing to the 1994–5 economic/political crisis in Mexico. The advocates of the NAFTA arrangement tried to play down the direct negative connection between the trade arrangement and the build-up and impact of these shocks, that is the Chiapas revolt led by the Zapatista National Liberation Army which broke out at the beginning of 1994; the 'Christmas devaluation' at the end of the same year; the so-called 'tequila effect' through 1995, with the escalation of political violence punctuated by the assassination of the PRI presidential candidate. Indeed, the orthodox view which soon took hold centred on the assumption that these crises would have been much more severe if NAFTA had not been in place. In this line of reasoning, it was not so much the US/IMF-centred emergency bailout but the availability of the NAFTA markets which cushioned the shocks. As one of the most robust defenders of the arrangement made the case:

> NAFTA may have helped the economy recover more quickly. After Mexico's [1982] debt crisis, its economy experienced no net growth for six years and could not take advantage of private capital markets for some time. By contrast, Mexico recovered rapidly after the 1995 crash, pulling itself out of a 6.2 percent drop in GDP in 1995 with 5.1 percent growth by 1996 and a return to the capital markets by mid 1995. NAFTA also preserved U.S. exports to Mexico, which had dropped by 50 percent in 1983–84, but rose by 11 percent during the two years following the December 1994 devaluation.[31]

The opponents of NAFTA interpreted the results in a very different fashion. A touchstone of these critics' fears was that this regional trade arrangement would have a serious destabilizing effect on the three national economies. Worstcase scenarios were offered, most vividly, in the Mexican case. As one leading commentator bluntly put it, NAFTA 'entails great risks.... In the short term especially, the accord as it stands may only exacerbate the country's already stark disparities and dislocations'.[32]

The series of shocks which hit Mexico in 1994 and 1995 acted in many ways to confirm these pessimistic forecasts. The start of the Chiapas revolt on 1 January 1994, the day on which NAFTA came into effect, symbolized for many critics the nexus between economic change and the determination of the region's indigenous peasants to defend their traditional way of life. Rather than ensuring stability (an argument that a good number of proponents of NAFTA brought out as a scare tactic during the

process of negotiations), the trade arrangement became indelibly linked to the process of coping with the shocks reverberating from currency devaluation. Less concerned with the impact of this crisis on Mexico's external reputation, with respect to trade and investment figures, these critics concentrated their attention on the consequences for the ordinary person in terms of inflation, the fall in public consumption, and the further rise in inequalities and level of violence.

While the problems in the architecture of NAFTA remained central to this critique, the defects of omission were not ignored. Judged in comparison with the European integration project, NAFTA was found wanting. Notwithstanding the asymmetrical structure, no developmental or social market dimension was built into the project. Unlike the European Union, there was no mechanism for a systematic redistribution of resources from rich to poor countries through a Social Development Fund. Nor was there any provision for the mobility and/or retraining of unskilled labour.

Yet, in spite of all of these ingrained flaws, NAFTA gradually took on some more positive connotations even for the critics. One form of compensation came via the new opportunities and/or necessities offered by NAFTA for political mobilization. As noted, a significant strand of this activity contained a highly inward nationalistic tone. Another strand, however, took on a transnational flavour through the formation of cross-border coalitions. This push beyond the confines of the national border may be located throughout the spectrum of civil society. High-profile organizations, operating on a trinational basis, include the Action Canada Network, the Common Frontiers project, the US Citizen's Trade Campaign, and the Mexican Action Network on Free Trade (RMALC). The motivation for this outward-looking drive has been defined by one NGO representative in the following terms: 'It wasn't just that we needed to have solidarity and linkage programs…it was a strategic necessity that progressive organizations establish long-term relationships of trust, movement-to-movement and sector-by-sector'.[33]

Another form of compensation came through the extended social dimension of the regional trade agreement. These provisions were most evident in the two so-called 'side-accords' on the environment and labour standards put into NAFTA by the administration of President Bill Clinton. In the case of the environment, a Commission for Environmental Co-operation (CEC) was established in 1993 with the task of implementing the 'green' side-accord. Individual citizens and/or groups could make use of the CEC's formal machinery for investigation if they believed national environmental laws were not being enforced. In the case of the labour side-accord, three national administrative offices were established to hear complaints about some areas of working conditions.

These add-ons did not go nearly as far as the critics of NAFTA would have liked. On the environment, the most controversial issues dealing with cross-border pollution whether in the form of the dumping of industrial wastes or air and water pollution remained untouched. Even in the area of the CEC's domain, there were a number of quite obvious deficiencies in institutional design. As the rulings of the CEC were not binding, there was little possibility of enforcement. While fully aware of these structural weaknesses, a good number of critics were nonetheless prepared to view

the side-accords as a significant concession. As a vehicle for policy advancement, the CEC at least allowed environmental issues to be made more transparent. As the director-general of a Mexican environmental group noted, civil society was accorded 'a moral power to make things public and to get governments to do things according to the law'.[34]

The influence of the 'glare of publicity', ensuing from the labour side-accord,[35] proved another form of consolation prize. What the side-accord delivered was a limited degree of transparency. Complaints were permitted on a number of issues, most notably the utilization of child labour, health and safety, and on questions to do with minimum wage. But because these complaints were restricted to the formal sectors of the economy, the scope of the side-accords was extremely narrow. Moreover, the effectiveness of the national administrative offices remained in doubt in that there was no provision for enforcement. While the union movement and its supporters could take some satisfaction for getting the side-accord inserted into the trade arrangement, therefore, there was little or no guarantee that this instrument would actually have the effect of ratcheting up labour standards.

Exploring future possibilities

From this overview, a better appreciation concerning both the constraints and opportunities *vis-à-vis* NAFTA becomes available. What stands out is the innovative—or even the novel—quality. Linking three very different countries containing two concentrated but asymmetrical dyads and one ill-formed relationship, the push for a new arrangement was bound to raise intense debates about the mix of motivations and distribution of outcomes. The speed with which the deal was negotiated, the fact that it was a (then) extremely confident Mexico which did most of the early running to launch the initiative, and the extension of the parameters of the deal beyond simply the trade agenda, all added to the level of controversy. Notwithstanding the abundant weight of its technical details, debate revolved around concerns with the big picture. NAFTA confirms the salience of the political ingredient within the evolving pattern of regional economic refigurations.

Yet, notwithstanding the clash of visions over NAFTA, it is the unintended consequences of the arrangement's application which stand out. At odds with the logic of the economic rationalists, NAFTA cannot be seen simply as a giant leap towards the goal of market liberalization. Both through design and default this trajectory has been tempered in a variety of ways. The waves of shocks in Mexico have underscored the salience of well-entrenched national differences as well as the convergence of values, systems and preferences in North America. Trinational community building remains slow paced, fragmentary and often distracted in application. While allowing some considerable impetus towards market opening on a continental basis, the arrangement has also provided an excuse to erect alternative (and in some ways more sophisticated) forms of protection.

To say that the goal of market liberalization has been muted in NAFTA is not to suggest that the social dimension has achieved anything close to equality in the

NAFTA agenda. Despite the concessions in terms of the side-accords, the arrangement remains driven by the principles of efficiency and stability, not equity and justice. Attempting to lock in the reforms implemented at the national level, most dramatically in Mexico, the arrangement has locked in massive problems as well.

This lack of balance has helped freeze opinions about NAFTA. In the report card put out by the advocates of the arrangement, most of the attention is devoted to the fact that since the deal was signed the two-way trade between the NAFTA countries has grown at a faster rate than for the international trade generally.[36] For their part, the opponents of the arrangement point to the high costs of the deal in terms of the downward pressure in all three countries on wages and living standards. Instead of the win/win scenario, popularized by the advocates of NAFTA, these opponents have continued to cast the trilateral arrangement in a more unflattering win/lose light dominated by the fears of accelerated structural adjustment, uncertainty and a race to the bottom.

Turning from results to process, the dominant impression is that NAFTA has become embedded in at least a loose fashion. Despite the ideological/policy opposition expressed to NAFTA, there appears to be little chance that the deal will be abrogated. Indeed some political parties, most notably the Liberal Party in Canada, have reversed their opinion and learned to live with the arrangement. Accordingly, the primary questions about NAFTA have shifted away from its durability to how the arrangement can and should be developed further.

Proponents of NAFTA have begun exploring the manner in which the arrangement can be deepened. For it is taken as a given that without such consolidation, the difficulties linked to the institutional fragility and the democratic deficit make the future of the arrangement more difficult.[37] Few suggestions have been made, however, that this move forward should be of a 'big bang' nature involving something equivalent to the 1992 Single Market initiative in Europe. Faced with the enormous practical/resource problems of such an initiative, not to mention all the political sensitivities attached to any hint of supernationalism, there is a gradualistic tenor to these sort of proposals. The main focal points are on extending the regulatory regime and the greater harmonization of rules in an issue-specific manner.

Another approach is to circumvent the deepening conundrum by placing the emphasis on the widening of NAFTA. Albeit for divergent reasons, a move towards an expanded free trade agreement is an area where some degree of consensus has been formed. For the United States, a southern expansion of NAFTA not only fits with the notion behind 'Enterprise for the Americas' proposal (reinvigorated by the December 1994 Miami Summit of the Americas, with its promise of an all-encompassing free trade zone by 2005) but has the instrumental advantage of consolidating the movement towards democratization and economic reform in the hemisphere. For Canada and Mexico, alternatively, expansion has the attraction of diluting some of the influence of the United States within a regional arrangement. As it is, these two countries have worked out separate bilateral free trade deals with Chile (the country at the top of the list of potential accession partners). As with

deepening, however, scenarios about widening have raised as many questions as answers. Deprived of fast-track authority, the Clinton administration's capacity to deliver has been severely reduced. At the same time, the will of some of the potential candidates for a NAFTA-plus deal has been cut into by the rise of other viable arrangements in the macro-region. The biggest question mark here relates to the evolution of Mercosur, a project which has taken a different path to NAFTA by forming a customs union (with a common external tariff) as opposed to a free trade area.

For all of the dynamism associated with NAFTA, then, the arrangement remains a work in progress. If it may be accurately described as being a vital component of 'trade policy revolution', the ultimate direction of this process of revolutionary change is still in some ways up for grabs. Unquestionably, NAFTA has brought with it a new sense of order. This is true not only concerning some significant aspects of the trade regime *per se,* but also in terms of the rules on investment and even more tentatively in some areas of the social agenda. If NAFTA has brought with it a semblance of order, the arrangement has precipitated a sense also of disorder. What was expected on outcome has not transpired in a seamless fashion. While mainly business driven, the intrusion of other influences and interests of both an 'outside-in' (geopolitical) and 'inside-out' (including the extension of transnational networks in civil society) nature have added complexity and uncertainty to the arrangement. Nor is it likely that what is seen in NAFTA now is what will be seen in the future. Under the weight of protracted crises, such as already experienced through the Mexican shocks, there is always the possibility that the arrangement may bend (although not inevitably break). The scenario here would be on tactical management not strategic vision. Alternatively, the momentum built up through this arrangement may well be enough for NAFTA to move beyond the consolidation phase. After pausing for breath brought on by the launching of the project, this scenario would have NAFTA moving towards a different stage of development. In either case, the one certainty will be that NAFTA will remain the centre of political contestation and debate.

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Chapter 15
Towards a political economy of trade in Africa
States, companies and civil societies

Timothy M. Shaw and Janis van der Westhuizen

Trade remains crucial to Africa's political economies even if the continent as a whole is increasingly marginal in global trade. For, while over the last quarter-century Africa has come to constitute a declining share of global exchange, in both services and products, both intra- and intercontinental, many companies and communities depend on it for any prospects of development, sustainable or not. Moreover, its proportion of world trade is probably considerably under-recorded, in part because of regional exchange and in part because of related informal trade, both legal and otherwise.

The distinctive architecture of the continent's trade as we approach the next millennium is all too little known (cf. chapters in this collection on Asia-Pacific and the Western Hemisphere), yet it holds promise in terms of more sustainable development as well as comparative analytic relevance. Hence the feasibility of anticipating an 'African renaissance' as the continent approaches the twenty-first century: an antidote to both Afro-pessimism and increasingly fraying 'Asian values'?[1]

This chapter is based on the premise that the political economy of trade in Africa as elsewhere is a function of a trio of actors, not just states and companies but also civil societies (see the chapters by Cloutier and Scholte). The latter are crucial in terms of consumption and fashion as well as professions, standards and technologies: from consumer and environmental international and/or indigenous non-governmental organizations ((I)NGOs) to professional associations and trade unions, co-operatives and media.

Just as a wide variety of types of civil societies and (I)NGOs have begun to be identified, so states and companies are hardly homogeneous on the continent: not only larger versus smaller states but also collapsed, diminished or failed states; and more local versus more global, uni- versus multisector corporations. In turn, the relationships among such heterogeneous states, firms and civil societies are diverse and dynamic, with the former losing out to the latter pair over time. This has been especially so over the last fifteen years which have been characterized by the hegemony of neoliberalism. Structural adjustment conditionalities have led not only to the downsizing and redefining of the state but also to the increasing contracting out of services to either private sectors or (I)NGOs. Increasingly, then, the African state is defined by three residual functions: the office of the president, the central bank and the military. Hence the expansive role of private and not-for-profit sectors and so the imperative of identifying novel typologies amongst them to distinguish the 'foreign

policies' of not only states but also firms and NGOs, particularly their relations with and policies towards the global economy in terms of exports (and imports) of goods and services etc.: more/less integrated/isolated etc.

However, the era of the 'Washington Consensus' (an array of neoliberal measures typically involving deregulation, privatization, liberalization and so-called 'good governance') may finally be drawing to a close as a combination of Asian crises and currency fluctuations challenges the primacy of the markets. The call in the World Development Report 1997 for sustainable 'partnerships' among states, corporations and civil societies may mark the dawn of a post-neoliberal dispensation, with profound implications for Africa and other parts of the global South.[2]

This chapter overviews Africa's global and regional trade, in both goods and services, proceeding to focus on a trio of particular issues—the continent as an emerging market, its place in post-Fordist production[3] and its position on global negotiations—then to highlight a couple of distinctively African characteristics—namely, trade under conditions of civil conflict and illegal trade—and to conclude by contemplating the implications of this case for broader debates and disciplines, that is implications and projections.

Global trade

The scale and character of trade around Africa has changed as a consequence of the evolving global political economy along with interrelated changes inside the continent itself: from postwar welfare state, Fordist production to a 'New' International Division of Labour (NIDL) dominated by globalization, flexibility and microchip technologies. It has also lost out in the New International Division of Power (NIDP)—that is, post-bipolarity—as it attracted resources—economic assistance as well as destructive weapons, especially the continuing proliferation of small arms or light weapons—from the two competing Cold War blocs as it declared its official 'non-alignment'. Africa may have been further marginalized by the decline in demand for 'colonial' agricultural and mineral products in a world of biotechnologies/genetic engineering and recycling/ polymers, although until very recently, demand for such had remained firm in Japan and the NICs even if not in the old North. Nevertheless, Africa's place in the less formal, less legal world of more informal regional and global exchange is assured.

After the 'lost decade' of the 1970s and the 'adjustment decade' of the 1980s, the 1990s may have marked a turning point; hence the not entirely fanciful, idealistic notion of an African renaissance, especially in post-apartheid Southern Africa and among post-insurgent states, like Eritrea, Rwanda and Uganda, if not yet Angola, Congo or the Sudan.[4] During the first half of 1990, Sub-Saharan Africa attracted only US$3.7 billion in FDI, less than 3% of all FDI to developing countries. More than 90% of inflows come from official sources, mostly on concessionary terms. Of this FDI, most is directed to North and Southern Africa with Egypt, South Africa and Nigeria being major recipients (in 1993–5 oil-rich Nigeria accounted for 93% of annual Sub-Saharan inflows and Egypt attracted 48% of the subregions' inflows over the same period).[5] By the mid-1990s, Africa's economies had begun to enjoy a

remarkable period of seemingly sustainable growth, in part based on growing external trade along with FDI, not seen since the initial post-independence period of the mid-1960s. The degree to which such renewed growth is a function of globalization, and/or adjustments, and/or Asia's NICs, and/or improved weather conditions is debatable. The World Bank proceeded to suggest that renewed growth was sufficient both to trickle down and spread out, whilst admitting that the human development indicators for the continent remained lamentably low, in part because of so-called 'complex political emergencies', some of which themselves resulted from highly unsatisfactory levels of human development:

> Sub-Saharan Africa's economic recovery both accelerated and spread to more countries in 1996. In sharp contrast to the early 1990s, the region's GDP grew faster than the population for the second year in a row....
>
> Yet improvements are fragile, and the threat of reversal is real in some cases. Several countries are mired in strife or civil disorder. Social indicators remain below those of other regions.[6]

Much of the renewed growth was concentrated in North Africa around the Mediterranean, especially in the Maghreb, and in Southern Africa, particularly outside South Africa. However, not only has the Asian flu virus spread to Africa and other emerging markets, so soon after the latter had finally begun to 'look east' in terms of both markets and models, but patterns of growth on the continent were already quite uneven, in part a function of the incidence of protracted structural adjustments and/or social conflicts. Such unevenness has profound implications for intra- and interregional relations. Thus in the mid-1990s, growth was fastest in post-insurgent (e.g. Angola, Namibia and Uganda), post-adjust-ment (e.g. Côte d'Ivoire and Ghana), and micro-states (e.g. Botswana and Mauritius), but slowest in some of the larger and more industrialized as well as oil-exporting political economies (e.g. Gabon, Kenya, Nigeria, South Africa and Zimbabwe). Even before the spillover of the Asian crisis to Africa was so apparent in terms of both direct exchange and secondary markets, the Economist Intelligence Unit cautioned:

> Although South Africa still accounts for about half of Sub-Saharan Africa's overall GDP, the region as a whole will continue to grow faster than South Africa. Moreover, GDP growth in SSA will accelerate from 3.2 per cent in 1997 to 3.6 per cent in 1998 as economic reforms and the market's opening continue to bear fruit. Impressive growth performances will be achieved by Angola, Uganda and Botswana, all of which will be among the ten fastest-growing economies in the world.[7]

Not surprisingly, these states were prime destinations during Clinton's historic Africa tour during the first half of 1998. Pushing the case for an 'economic partnership with Africa', Clinton sought to drum up support for the Africa Growth and Opportunities Act aimed at shifting the focus away from aid and clearly in favour of trade. In terms of the Act, countries violating human rights, failing to remove trade and investment barriers or

failing to improve their fiscal policies would no longer be eligible for duty-free privileges for their export products, participation in debt reduction programmes or many other US economic incentives.[8] Critics draw parallels with NAFTA (or 'Naftrica') contending that despite the access African exports would enjoy to the North American market, American goods and services will quite simply overwhelm African national, regional and local markets much as they have in Mexico.[9]

However, as South Africa emerges as the continent's next 'middle power', the Africa Growth and Opportunity Act is aimed not only at expanding economic linkages with one of the US Department of Commerce's self-designated 'Big Emerging Markets', but also at gaining support for US security policies. Washington's African Crisis Response Initiative was mooted as an African solution to regional security problems. Ultimately, such a force—directed under the aegis of the UN or the OAU—would be on standby to intervene in trouble spots, like Somalia in the 1990s, into which the United States itself is increasingly reluctant to be drawn in both logistical military and political terms.[10]

While the continent's economies overall grew in the mid-1990s, its export performance was less impressive. Africa's (formal, legal and recorded) exports grew by 6% in the last half of the 1980s, but only by a further 1% in the first half of the 1990s. By contrast, while global exports stagnated in the 1990s, inter-African trade grew in the first half of the 1990s: up from 6% to 8.5% in both imports and exports. So, the macro data provide supportive evidence for both the continent's continued marginalization and the revival of regional exchange. However, as we shall see, when informal as well as illegal trade is taken into account, Africa is less marginal both globally and regionally than at first appears.

Regional trade

Africa has more small, poor and often landlocked states than any other region although, given the post-bipolar proliferation of states in the former Second World, ex-Yugoslavia and Central Asia may come to rival its unenviable status. This political and economic geography has created the potential for considerable cross-border, transnational regional exchange, although so many neighbours are in similar ecological or mineral zones and so produce common commodities. Thus, in post-independence Africa, official, recorded regional exchange has rarely exceeded 5% of total trade. However, such a remarkable record is misleading as multiple informal exchanges across the continent's myriad borders in times of conflict as well as peace are unrecorded. Most estimates of such informal trade in clothing, colonial commodities like coffee and tea, diamonds, energy, foods, etc., would at least double routine regional exchange. And the amount of trade is even higher when illegal exchanges—that is, drugs, guns, peoples—are included.

'New' forms of non-state regionalisms, which may or may not be compatible with established interstate structures, include a variety of Asian-style 'triangles' and 'corridors' as well as emerging transnational links among civil societies. The former have blossomed in Southern Africa as South Africa's large urban areas come to play their natural post-apartheid role of commercial and communication hubs. They are

most advanced in subregional groupings within the Southern African Customs Union (SACU)—Maputo and Trans-Kalahari Corridors through Gauteng plus the Lumbombo Spatial Development Initiative between Durban, Swaziland and Maputo—but they have potential in the broader SADC (Southern African Development Community)—Beira, Nacala and Tazara Corridors through Mozambique or Tanzania, and, even more speculatively, the Benguela Corridor from the copperbelts to the Atlantic. The degree to which such substate and/or private sector initiatives are compatible with established official groupings is debatable.

Similarly, although the continent's regional and continental organizations claim that they wish to incorporate the private and NGO sectors, in practice, corporate and civil society definitions of regionalisms are not always compatible with the scope or traditions of intergovernmental communities. The ECA/OAU (Economic Commission for Africa/Organization for African Unity) and the major subregional institutions like COMESA (Common Market of Eastern and Southern Africa) and ECOWAS (Economic Community of West African States) claim to seek a dialogue with chambers of commerce and NGOs, but corporations and civil societies have their own criteria for regional development, from market share to policy advocacy, respectively. Thus in contemporary Southern Africa, for example, alternative spatial and organizational definitions of regional development are being advanced and affected by private companies, NGOs like *Mwelekeo we* NGO (MWENGO) and the South African National NGO Coalition (SANGO), and media like M-Net and Mail and Guardian. Further, ecological and ethnic communities are beginning to emerge, facilitated by historical and contemporary migrations of both peoples and other species: Kagera or Zambezi River Basins, Great Lakes, Nile Valley, even Rift Valley communities, let alone Yoruba or Swahili or Zulu 'empires'.

In short, if informal as well as illegal along with alternative regional formulations are all taken into account, the continent boasts a rather diverse and dynamic set of intermediate structures. Yet the degree to which these meso-level arrangements are compatible and so cumulative is problematic, with profound implications for macro- (e.g. ECA/OAU) or micro-regional (SACU or revived East African Co-operation) trade practices and negotiations.

To be sure, the emerging architecture of the continent-wide African Economic Community (AEC) seeks to recognize and take advantage of the variety of such burgeoning subcontinental groupings in terms of its own intra-continental schedule as well as negotiations with extracontinental communities. Hence its continuing attempt to encourage compatible as opposed to competitive forms of regionalism in part through the UN Economic Commission for Africa's new Centre for Civil Society Organizations and in part through the ECA's redesignated Subregional Development Centres. The AEC also seeks to reconceptualize previous coalitions of landlocked and least developed states as forms of regionalization and differentiation so that heterogeneous sets of states are not treated in a homogeneous way, which may be negatively discriminatory in practice. Rather it seeks to revive NIEO-type notions of affirmative policies in favour of historically and geographically disadvantaged sets of states.

Africa as an emerging market

Africa has begun to be rediscovered by direct and indirect investors in the 1990s. First, FDI was very low throughout the 1980s, only rising from US$1.2 billion in the first half of the decade to US$3 billion in the second. Moreover, after a decade and a half of structural adjustment reforms, in the mid-1990s a few stock exchanges on the continent began to be recognized as emerging markets, an unprecedented, probably unanticipated, form of recognition of the continent's increasingly important financial flows in the NIDL. As Hong Kong's *Sunday Morning Post* indicated in September 1997, as the seriousness of Asia's own crisis began to be appreciated:

> Africa is the Cinderella of emerging markets, better known for war and famine than booming stock markets. But a growing band of investors is being attracted to the continent's nascent stock markets after some spectacular gains in the past two years.[11]

A minority of larger stock markets in the major, primarily ex-settler, cities are long established—Harare, Johannesburg, Lagos and Nairobi—although these, especially that in South Africa, have expanded their listings and turnovers in the 1990s. In part, this is because of foreign investor interest, some of it from foreign mutual and pension funds which had previously sanctioned settler states' economies. But these pioneers have now been joined, partially in response to donors' demands under SAPs as well as expanding private ownership because of privatizations and demutualizations, by new exchanges in Botswana, Côte d'Ivoire, Ghana, Malawi, Mauritius, Namibia, Swaziland and Zambia, with other cities like Dakar, Dar es Salaam and Kampala to follow. Fifteen of the continent's fifty-plus countries now have them, just over half of them in the more prosperous and industrialized SADC region.

The growing sophistication of the financial sector enables African private mutual and pension funds, as well as its mortgage and financial companies, to invest their holdings more readily, while established conglomerates can be more easily unbundled as required under current national and global anti-trust regimes. And in the case of hitherto white minority states, especially South Africa, black empowerment/redistribution can thereby be advanced. African markets led all other emerging markets in 1994, partially because of the 'discovery' of the continent by global mutual funds then fleeing Latin America and now Asia. By mid-1998, for example, the oldest and largest such market—that in Johannesburg—had reached record price levels and attracted a record number of listings.

Africa in a post-Fordist global economy

Africa at the end of the century has to begin to respond to the NIDL in terms of post-industrial market niches, including services like telecommunications, to which we turn after treating other new opportunities like diasporic markets and non-traditional exports. Under post-Fordism, flexible global production chains mean that only one part of any

product will be produced in one place, often in a deregulated Export Processing Zone (EPZ), with container links by air, rail, road and/or sea to similar enclaves around the world. To date, the continent has fewer such extraterritorial areas than other regions of the world, but under SAPs it is beginning to establish such new infrastructures on a regular basis as indicated above under regionalisms.

First, it also has to begin to participate in market opportunities created by novel forms of distribution and consumption, such as those constituted by 'big box' consumer warehouses in the North, namely Europe, North America and Japan, beginning to be found in South Africa as well. Large North Atlantic and North Pacific chain stores with their own brands, such as The Gap and WalMart, in the clothing, food and furniture sectors, have immense buying power in terms of, say, cotton goods, ethnic foods and tropical furniture. Traditional, established African commodities have been pushed upmarket by clever value-adding marketing, such as the boutiquing of coffee beans by increasingly global chains like Starbucks, to 'ethnic' coffees, teas, etc., with neat wine-style labels of origin about particular ecologies, ethnicities, flavours, etc.

Second, in a world of global products there are also niche markets for authentic, traditional goods, such as African crafts—a distinct 'non-traditional' market in part constituted by growing diasporas, themselves something of a consequence of the continent's disappointing developmental performance, as 'economic refugees'. For example, the World Bank calculates that there is an 'Afrocentric' market in the United States alone of some US$200 million annually. Africa can gain through trade with growing diasporas not only in the Caribbean and Brazil but increasingly in Europe and North America: the source of potential FDI (into new countries like Eritrea or devalued currencies like the cedi) and import demand for traditional goods like garri, palm oil and newer products such as 'black' cosmetics based on selected tropical products. Admittedly small, some of these niches even extend to a few select 'post-industrial' services. For example, two South African advertising agencies—TBWA Hunt Lascaris in 1993 and Ogilvy and Mather Rightford in 1996—were named International Agency of the Year by the American trade newspaper *Advertising Age*.[12]

A highly undervalued 'niche export' is the cultural and sports industries sector. That is, high-profile so-called 'hallmark' tourist events ranging from the (relatively) better-known Africa World Cup to the less familiar African film and music festivals. These are not the exclusive preserve of the more affluent African countries. Burkina Faso, indisputably one of the poorest nations on earth, hosted the 21st African Cup of Nations despite the fact that it is not an excelling football nation (unlike Nigeria, Cameroon, Ghana or Liberia). Even though the modest profit generated barely covered rental for television broadcasts and fees to the Confederation of African Football, the event generated enormous publicity for the country in advance of the June 1998 OAU Summit, Burkina Faso's crafts fair in October 1998 and the Fespaco film festival in 1999.[13]

Third, the continent is already generating considerable 'non-traditional' exports under adjustment conditionalities, such as cut flowers from the burgeoning horticultural industries of Kenya and Zimbabwe and now Uganda. Such niches are a

function of relatively inexpensive air freight, especially from landlocked countries. They also require specialized facilities, such as dedicated packaging, cool warehouses at airports and environmental monitors to ensure compliance with 'international' standards in terms of, say, pesticide use, chemical dyes and diseased products.

Fourth, some African companies have begun to turn the continent's underdeveloped telecommunications sector to their advantage by 'leapfrogging' straight to cellular, digital, satellite technologies as their high-tech infrastructure. For example, although Africa on a regional basis has the least developed infrastructure with only 2% of the world's telephones and 12% of the population, some of the most sophisticated networks are located there. In Botswana, for instance, 100% of the mainlines are digital, in contrast to the United States where it is 49.5%.[14] This is especially so for South Africa, which is by far the largest Internet server on the continent as well as host to M-Net/DStv etc., which now stretch throughout COMESA.[15] Of the estimated 1 million Internet users in Africa, 700,000 live in South Africa. Indeed, South Africa ranks as the sixteenth most-Internet-connected country in the world, shortly behind Denmark and ahead of Austria. As was recently admitted:

> [w]ithin the continent South Africa is comparable to most European countries in the level of connectivity.... The range and quality of information resources on the web in South Africa is fully comparable to, and quite possible better than that in most industrial countries.[16]

Though concentrated in South Africa, the Internet has spread rapidly throughout the continent. Only sixteen countries had full Internet access in May 1996. Today, forty-four African countries and territories are wired up—more than three-quarters of all capital cities. The largest Internet markets in Africa are Côte d'Ivoire, Egypt, Ghana, Kenya, Morocco, Mozambique, Senegal, Tanzania, Tunisia, Uganda and Zimbabwe.[17] Apart from Egypt and Morocco in North Africa, the other major hosts therefore are in Southern and Eastern Africa, not Central or West. Africa Online now serves seven cities, from Johannesburg to Nairobi and Mombasa as well as Accra and Abidjan. And even in very poor states, cordless, cellular, satellite technologies enable short- and long-distance trade to proceed. Indeed, it is hard to imagine the complexities of peacekeeping partnerships without such advanced technologies! At Africa Telecom 98 in Johannesburg, a continent-wide plan was agreed between states, international agencies and private sectors, both manufacturers and providers, to spend some US$750 billion over the next five years almost to double the number of phones from 14 to 23 million.

Finally, African political economy generally pays scant attention to the tourist trade. Yet, globally, international tourism has grown by 9.6% during 1980–90 surpassing both commercial services (7.5%) and merchandise exports (5.5%). While the United States and Europe continue to dominate the international tourist trade, their combined share has been declining since 1950 at 92% to just under 80% in 1983. This suggests that as these destinations gradually reach their 'ceilings' the developing world becomes an increasingly sought-after destination, given the advantage of

depreciating currencies. Accordingly, the World Tourist Organization, using economic groupings of countries, suggests that Africa has the highest growth prospects from regions with tiny base volumes (i.e. Latin America/Caribbean, East/Central Europe) to be followed by Australia/New Zealand/Japan, Asia/Pacific developing countries and other parts of the OECD.[18]

During the past two decades, Africans increased the volume of their overseas travel by nearly 90%, increasing from 4.6 million in 1980 to 8 million in 1990, an average annual rate of growth of 6.6%. In 1990, 65% of arrivals recorded were on the basis of intra-regional travel. In fact, intra-Africa tourist flows grew by more than 17 % in 1992 in comparison with the previous year, reaching 5 3 % of all tourist arrivals in 1992. Subregionally, Southern Africa, North Africa and Eastern Africa respectively witnessed the fastest tourist growth rates on the continent.[19]

The continent and global trade negotiations

Africa has been not only at the margins in terms of actual trade in goods and services, but always marginal in negotiations about such exchanges. While its postcolonial regimes advocated claims for a New International Economic Order in the heady days of the 1970s, its ability to advance its interests in subsequent negotiations arising from the NIDL has been very limited.

If it was so disadvantaged during the relatively benign postwar Keneysian era then, given the hegemony of neoliberalism in the post-independence period, it was further peripheralized. Such marginalization has been particularly apparent in the complex and protracted Uruguay Round negotiations over the WTO as well as in the regular talks about the series of Lomé Conventions with the EU. For the Third and Fourth Worlds, Trade-Related Aspects of Intellectual Property Rights (TRIPS) and Trade-Related Investment Measures (TRIMS) tend to be quite disadvantageous.

In advance of further WTO talks due to start in 2000, the revitalized OAU and redirected ECA are attempting to minimize the effects of Africa's historic marginalization by orchestrating a continent-wide response through the embryonic African Economic Community (AEC). Thus at the OAU/AEC Ministerial Conference of the WTO in May 1998, ministers highlighted several areas in which progress since the Uruguay Round has been disappointing. These included reducing the abuse of trade measures in areas like anti-dumping, sanitary and environmental standards as well as overcoming any costs of reforms in least developed and food-importing developing states. They therefore concluded by lamenting 'continued marginalization' and insufficient 'integration…in the multilateral trading system' calling for attention to the 'development dimension and the principle of special and differential treatment of developing countries'.[20]

And although after over two decades the Lomé arrangement has become less generous to Africa as the EU has expanded, it nevertheless remains more of a bilateral development agreement than the WTO's ideology of free trade multilateralism. And for some economies highly dependent on one agricultural or mineral commodity, it still offers tangible advantages. Moreover, Lomé constitutes a forum in which the

South and North negotiate as formal equals without all the diversions and divisions of the Asian NICs. ACP-EU talks seek to balance WTO-style free trade with ACP needs, such as regionalization, political dialogue, financial, industrial and technological co-operation, all within a recognition of the social dimension of development.[21]

The status and role of the new South Africa will have an important bearing on the cohesion and creativity of the OAU/AEC team not only within the APC coalition but also in the negotiations with the EU itself for a post-Lomé framework. The Union's ability to divide and rule is apparent in its success in dealing separately with the Mediterranean states, so confining the effective scope of the OAU/AEC mandate to the smaller and weaker subset of Sub-Saharan Africa only. Nevertheless, African states have supported the idea of ACP Free Trade Areas and the notion of an EU-ACP summit in 2000.

Trade and civil conflict

As already indicated, the ubiquity of 'internal' conflict on the continent has not been as negative for external trade as might have been anticipated. Rather, some of the post-bipolar violence has been a function of competition for scarce resources in a global context where there is no longer any prospect of superpower intervention. Thus, one element in the protracted conflict in Liberia was control over tropical timber exports. Likewise, the civil wars in Angola and Sierra Leone are in part about access to diamond reserves. The ghat (a herb valued for its intoxicating effects when chewed) arrives in Djibouti and the rest of the Horn's coast every day whether there is war or peace. And exports from Somaliland, officially unrecognized though it remains, have soared since its *de facto* separation from Somalia!

'Humanitarian intervention'[22] in so-called 'complex political emergencies' now constitutes one way for external interests—non-state as well as state—to have some impact on economic as well as environmental, infrastructural and social outcomes. And the economic content of the peace-building syndrome is not inconsequential, from supplies for blue berets and NGOs to informal sector exchanges around refugee camps etc.

Illegal trade

There has always been illegal as well as informal exchange on the continent as well as elsewhere. In the one-party state socialist era much of this was to avoid state regulation. But in the current neoliberal era of globalization, Africa has become a transit route for drugs and guns, as well as other so-called small arms like landmines, as well as a source of ivory, mandrax, and marijuana. This trade shapes the new security agenda confronting African states and communities. Likewise, uneven incidences of conflict and patterns of development have contributed to contemporary waves of migrants and refugees, for a range/mixture of economic, ecological, political and/or social reasons, which often serve to exacerbate the cross-border flow of such illegal products. Thus the international sex

industry (turnover unknown, but estimated to be at least US$20 billion) becomes more transnational as women and girls are enticed or kidnapped from poor countries and smuggled into rich ones to work as sex slaves. In case they complain, 'they are warned that it is not only they, but their families back home who will suffer'.[23]

The scale of such various types of illegal trade cannot be calculated, but conservative estimates would put it at least double the legal trade. Its corrosive impact on communities and police forces is considerable, leading to corruption, Mafias, gang killings, symbolized by the chilling new feature of African conflicts: child, usually boy, soldiers—another (very!) lost generation? In turn, it has encouraged the expansion of private security structures, to defend both companies and communities against such new security threats—from armed guards to sophisticated communication networks to latter-day mercenaries, such as Executive Outcomes and Sandline.

Futures of African trade: policies, projections and paradigms

Finally, the emerging architecture of African trade processes, policies and projections—whither the African renaissance?—has implications for comparative analysis and praxis in several interrelated fields of analysis and practice, both established and novel, as indicated below (cf. other contributions in this volume, especially Chapters 1, 2, 9, 10 and 11). But we turn first to three clusters of issues around African trade peculiar to the continent: non-state governance, civil conflicts and new sources of power.

First, the different combinations of states, companies and civil societies inside and outside Africa in 'triangular' structures hold profound implications for governance. 'Authoritative decisions' are no longer the monopoly of supposedly 'sovereign' states, but may also be made by corporations and/or NGOs, especially within their mixed-actor coalitions as over, say, biodiversity, child labour, landmines, ozone depletion, tropical forests, etc. Within EPZs and corridors/triangles, governance is almost entirely non-state. Conversely, such triangular relations may lead to novel forms of company or NGO-dominated corporatisms (cf. Part II).

Second, as already suggested above, trade and other forms of economic activities during civil conflicts constitute a possible new field which would augment or extend the burgeoning area of peace building or peace operations. This could be done by taking into account not only supplies for blue berets and refugee camps —often small 'instant' cities—but also the economic dimensions of sustainable reconstruction and continuing 'track two' diplomacy to advance confidence building etc.; that is, the roles of companies as well as think-tanks and other non-state actors in sustained multitrack conflict prevention or minimization strategies.

Third, globalization is changing the nature of power. As our example of Burkina Faso hosting the Africa Cup reveals, African states and firms are attuned to the potential of hallmark tourist events—specifically sports and cultural industries and festivals—to generate the kind of publicity through which trade can be expanded in the highly consumer-driven, post-Fordist era of the late 1990s. Although Joseph Nye has begun conceptualizing these trends in relation to US hegemony as 'soft power',

influence or power derived in this way is actually profoundly structural.[24] Rather, the need is to analyse how smaller states as well as non-state actors are employing strategies to develop a range of 'post-industrial' goods and services from tourism, design and advertising, music, film and other cultural industries, not to mention major sports events such as the Africa Cup, Commonwealth and Olympic Games.

Conclusion

African political economy reminds scholars in international relations and related disciplines to look beyond the state to understand emerging trends in political economy, particularly the imperative of going beyond the state to bring in non-state relations of companies and civil societies. Only by doing this can we capture the dynamism and uncertainty that characterizes Africa's development. Studying this evolution requires less emphasis on, for example, formal economic modelling in development economics, and a greater concentration on patterns of informal economic exchange, including illicit trade. As Anna Dickson has argued, the study of Third World development has been relatively neglected in modern IR.[25] The continent's apparent marginalization does not mean exclusion but rather uneven peripheralization which requires creative strategies to transcend. This explains the development of a complex set of actors from government, firms and society, interacting at a variety of levels.

Notes

1 Compare Peter Vale and Sipho Maseko, 'South African and the African Renaissance', *International Affairs* 74:2, April 1998, pp. 271–87; David F.Gordon and Howard Wolpe, 'The other Africa: an end to Afro-pessimism', *World Policy Journal* 15: 1, Spring 1998, pp. 49–59.

2 World Bank, *World Bank Development Report 1997* (Oxford: Oxford University Press, 1997).

3 Whereas Fordism involves 'mass production of complex consumer durables based on moving assembly line techniques operated with the semi-skilled labour of the mass worker' (Bob Jessop, 'Post-Fordism and the State', in Ash Amin (ed.), *Post-Fordism: A Reader* (Oxford: Blackwell, 1997), p. 253), post-Fordism relies on supply-side innovation and a greater degree of flexibility both in terms of machines and/or systems of production as well as labour. As Eric Hobsbawm, *Age of Extremes: The Short Twentieth Century, 1914–1991* (London: Abacus, 1995), p. 404, once put it, post-Fordism was 'not the age of Henry Ford, but Benetton'. For an extensive analysis, see Jessop, 'Post-Fordism and the State'.

4 Dan Connell and Frank Smyth, 'Africa's new bloc', *Foreign Affairs* 77:2, March/April 1998; Dave Peterson, 'Finding African solutions to African problems', *The Washington Quarterly* Summer 1998, pp. 149–58.

5 However, with an expected rise of Sub-Saharan exports (which fell from 3.1% in the mid-1950s to 1.2% in 1990) per capita incomes between now and 2005 are expected to rise at an annual rate of 0.9%. H.Holman, 'Africa urged to catch bandwagon', *Financial Times* 25 March 1997, p. 4; United Nations Conference on Trade and Development, *World Investment Report 1996* (New York and Geneva: United Nations), p. 58.

6 Ibid.

7 Economist Intelligence Unit, *World Outlook 1998: Forecasts of Political and Economic Trends in Over 180 Countries* (London: EIU, 1998), p. 9. In fact, according to a recent survey of African competitiveness, South Africa only ranks seventh, superseded by Mauritius, Tunisia, Botswana, Namibia, Morocco and Egypt respectively: Jeffey Sachs and Sarah Sievers, 'Africa enters the rankings', WorldLink January/February 1998.
8 South African Press Association, 'US Senator Lugar urges passing of Africa Growth Act', 22 April 1998. www.anc.org.za/ancdocs/briefing/nw19980423/54.html.
9 As one observer noted,

> With its call for rapid privatisation and liberalisation of markets, Naftrica would create a financial windfall for US corporate big game hunters in Africa. The repeal of trade protections for local industries and farmers, proposed tax breaks for foreign corporations and reduced import and corporate tax rates are great for multinationals —hardly so for African markets.
>
> Deborah Toler, 'Clinton goes big-game hunting in Africa', *Mail & Guardian* (Johannesburg) 20–26 March, 1998

10 See Connell and Smith, 'Africa's new bloc'; Peterson, 'Finding African solutions to African problems'.
11 *Sunday Morning Post* (Hong Kong) 14 September 1997.
12 *Financial Mail* (Johannesburg) 9 May 1997.
13 'Close to the haphazard soul of African football', *Mail & Guardian* (Johannesburg) 13–19 February 1998.
14 Mike Jensen, 'More lines needed', in *Internet in Africa: Special Mail & Guardian supplement on Internet connectivity in Africa,* 8–14 May 1998, p. 5.
15 In collaboration with Malaysia Telecom, South Africa's Telkom has embarked on the 'SAFE' project (South Africa/Far East) to develop a fibre cable linking the two countries, thus enabling Telkom to act as a hub for African traffic (Jensen, 'More lines needed').
16 Cited in Fred Ahwireng-Obeng and Patrick J.McGowan, 'Partner or Hegemon? South Africa in Africa—part one', *Journal of Contemporary African Studies* 16:1, 1998, P. 19.
17 Mike Jensen, 'The expansion of African webspace', in *Internet in Africa.*
18 World Tourism Organization, *Tourism to the Year 2000 and Beyond, Volume 2: Africa* (WTO Forecasting Series, Madrid, 1997), p. xiii.
19 World Tourism Organization, 'Tourism to the Year 2000', p. 34.
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21 Gordon Crawford, 'Whither Lomé? The mid-term review and the decline of partnership', *Journal of Modern African Studies* 34:3, September 1996, pp. 503–18; Kaye Whitman, 'Africa, the ACP and Europe: the lessons of 25 years', *Development Policy Review* 16:1, March 1998, pp. 29–37.
22 Nicholas Wheeler, 'Humanitarian intervention and world politics', in John Baylis and Steve Smith (eds), *The Globalization of World Politics* (Oxford: Oxford University Press, 1997), pp. 391–408.
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24 Joseph Nye, 'Soft power', *Foreign Policy* Fall, 1990.
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Chapter 16
The Asia-Pacific

John Ravenhill

The Asia-Pacific region poses a number of puzzles for students of regional trade. Although no region-wide preferential trade arrangements exist in the Asia-Pacific, the share of intra-regional trade in the total trade of Asia-Pacific economies is higher than within the most institutionalized of discriminatory regional schemes, the European Union.[1] In 1997, APEC economies conducted 72% of their total trade with one another; for the European Union, the comparable figure was only 56%.[2] Trade among Asia-Pacific economies has grown rapidly despite some economies retaining high-tariff and non-tariff barriers. This growth owes much more to the dynamism of the private sector in the region than to the actions of governments, acting either individually or in collaboration with one another. Rather than facilitating trade flows, in some instances governments did their best to obstruct them, for example during the longstanding ban on direct trade between Taiwan and the People's Republic of China. Moreover, the region has been the location of some of the most contentious trade disputes in the global economy in the last two decades.

Regions are social constructions. There is no such thing as a 'natural' region, whether defined in terms of economics, culture or geography. Two decades ago, few people perceived the group of economies that are now members of APEC as constituting a region. Similarly, in the enormous literature on integration one finds few references until recently to the idea that East Asia might constitute a region.[3] Such has been the rapidity of growth of the East Asian economies, however, that this has transformed not just patterns of trade but also how states conceive of their identities and interests. By the mid-1980s, the countries of predominantly European settlement on the Pacific Rim—Australia, Canada, New Zealand and the United States—increasingly saw their economic destinies as closely intertwined with those of the East Asian economies.[4] The culmination of these developments was the formation of the APEC grouping in November 1989.

Whether APEC should be termed a region in any conventional sense of the word is debatable. For APEC includes within its membership several groupings that themselves normally would be considered 'regional' intergovernmental arrangements. Most notable among these is the North American Free Trade Agreement (NAFTA), itself the subject of a separate chapter in this book. If APEC were the region, then NAFTA would have to be termed a 'subregional' grouping, a seemingly inappropriate designation for a collaborative scheme of its importance and centrality to the interests of its member states. APEC also embraces two other

regional economic collaborative arrangements, the ASEAN Free Trade Area (AFTA) and the Closer Economic Relations (CER) agreement between Australia and New Zealand.[5] APEC in many ways might be considered a transregional arrangement rather than a region.

APEC's trans-Pacific form has caused some East Asian states to question whether it is the most appropriate 'regional' organization for representing their interests and enhancing their bargaining power in international trade negotiations. The expansion of APEC in 1998 to include the Eurasian power, Russia, may intensify these doubts. In 1990, the Malaysian Prime Minister, Dr Mahathir bin Mohamad, proposed the establishment of an East Asian Economic Grouping, to include the ASEAN countries plus China, Japan and Korea, as an alternative regional grouping to APEC. The proposal was shelved at that time because of resistance from Japan and some ASEAN countries. Their concern was that an exclusively East Asian grouping would encourage fragmentation of the global economy into regional blocs, and deny them access to their single most important market, the United States. As a way of saving face for the Malaysian Prime Minister, the countries agreed to form an East Asian Economic Caucus *within* APEC. Despite the continued desire not to embark on an initiative that might jeopardize their access to North American markets, the idea of an East Asian grouping as a means of increasing their bargaining power *vis-à-vis* the United States, and as a counterweight to NAFTA within APEC, clearly has some appeal for East Asian countries. With the creation of the Asia-Europe Meeting (ASEM) in 1996, where Asia was represented by most of the economies that constitute the East Asian caucus within APEC, the grouping gained a new institutionalization.[6] In the longer term, a more institutionalized East Asian grouping may yet evolve into a significant player in trans-Pacific trade.[7]

APEC's origins

Although APEC was not formed until 1989, efforts to promote economic collaboration across the Pacific have a much longer history. Some trace this to the interwar Institute of Pacific Relations.[8] For others, APEC has its origins in the 1965 proposal by the Japanese economist, Kiyoshi Kojima, for the creation of a free trade area among the industrialized economies of the Pacific (Australia, Canada, Japan, New Zealand and the United States) to balance the growing influence of the European Community in the world economy.[9] The proposal attracted no support from other governments. It did lead, however, to the establishment in 1967 of a grouping of free-trade-oriented economists, the Pacific Trade and Development Conference (PAFTAD), whose regular meetings have called for trade liberalization and collaboration among the economies of the Pacific Rim. In the same year, the Pacific Basin Economic Council, a grouping of businesspeople, was founded. Gradually the participation in both organizations expanded from the industrialized economies of the region to embrace all the major economies of East Asia, and some in Central and South America. Government officials became involved in the push for regional economic collaboration in 1980, with the foundation of PECC, the Pacific Economic Cooperation Council.[10] At this time, however, governments were unwilling to

Table 16.1 **Share of manufactures in total exports (%)**

	Indonesia	*Malaysia*	*Philippines*	*Singapore*	*Thailand*
1970	1.2	6.5	7.5	41.5	4.7
1975	1.2	17.3	11.7	–	14.7
1980	2.3	18.8	21.1	43.1	25.2
1985	11.0	27.2	26.6	51.0	38.1
1990	35.5	54.2	39.0	71.7	63.1

Source: World Bank data accessed through the International Economic Data Bank, Australian National University

create any formal intergovernmental arrangement: officials participated in PECC in their private capacities.

Why did governments change their mind over the course of the 1980s on the establishment of a Pacific economic grouping? Several factors are relevant here. ASEAN economies had been particularly resistant towards a new economic grouping, perceiving it as posing a potential threat to their own organization, and to their links with other less developed economies. The economic crises experienced in the first half of the 1980s led to a partial dismantling of tariff and non-tariff barriers in Indonesia, Malaysia, the Philippines and Thailand, and to a new desire to attract foreign investment. Moreover, the decline in commodity prices that followed the second round of oil price increases at the start of the decade suggested that their economic interests coincided as much with those of industrialized economies than other less developed economies, including other ASEAN member states.

ASEAN's resistance to a new economic grouping also declined as rapid growth resumed in the second half of the 1980s, fuelled in part by investment in export-oriented manufacturing from Japan, Korea and Taiwan. Within a short period of time, the composition of the exports of the major ASEAN economies changed dramatically (Table 16.1). The increasing share of manufactures in their exports diminished ASEAN governments' fears that participation in a regional economic arrangement would perpetuate an unequal division of labour in which they would hold a subordinate role. Subsidiaries of transnational corporations produced the vast majority of the new manufactured exports, a reflection of the increasing integration of these economies into global production networks.[11]

The resumption of rapid economic growth in South-East Asia in the second half of the 1980s contributed to the growth of interdependence in the Asia-Pacific—particularly because part of its new success in manufacturing exports rested on its participation in a trade triangle in which components and capital goods were sourced primarily from North-East Asia and then re-exported, often to the North American market. In these years, Indonesia, Malaysia and Thailand achieved per capita growth rates of around 7% annually, a performance matching that achieved over the previous

Table 16.2 **Interdependence amongst APEC economies: intra-APEC trade as a percentage of total trade**

1970	58.7
1975	55.2
1980	56.9
1981	58.9
1982	60.1
1983	63.0
1984	65.3
1985	66.4
1986	66.6
1987	67.5
1988	68.0
1989	68.5
1990	67.6
1991	69.1
1992	69.8
1993	70.9
1994	72.3
1995	72.3
1996	72.0

Source: **IMF Directions of Trade data accessed through the International Economic Data Bank, Australian National University. For the purposes of this table, APEC membership is the eighteen members as of 1996**

two decades by Korea, Singapore and Taiwan, and in the 1950s and 1960s by Japan. The East Asian economy as a whole was growing much more rapidly than other parts of the world economy. Not surprisingly, therefore, the share of their trade that Asia-Pacific economies conducted with one another also grew rapidly in the 1980s (Table 16.2).[12]

The desire to manage the problems arising from the increased interdependence among the Pacific economies contributed to the push for an intergovernmental institution. Trans-Pacific trade tensions had escalated markedly in the 1980s. The North American economies and those of Australia and New Zealand had for several decades attempted to slow the pace of domestic adjustment in response to the rapid growth of exports of manufactures, first from Japan and then from the East Asian newly industrialized countries, especially Korea and Taiwan. They imposed restrictions on imports—first against textiles, then automobiles, steel, consumer electronic equipment and semiconductors. How significant a brake on East Asian exports these

'voluntary' export restraints constituted is a matter of debate.[13] Certainly, they generated substantial friction in trans-Pacific trade. In the 1980s, however, as the Reagan administration ran large budget deficits that inevitably translated into trade deficits, the debate over trans-Pacific trade became dominated by US concerns that the North-East Asian economies were engaging in predatory trading practices by keeping their domestic markets closed while exploiting relatively free access to the American market.

Prodded into action by an increasingly angry Congress, the Reagan administration took a number of steps designed to pressure North-East Asian economies to increase their consumption of American exports. One was to negotiate a currency realignment, the Plaza Agreement, through which the US dollar was depreciated against North-East Asian currencies.[14] Another was to engage North-East Asian governments in consultations over perceived barriers to American exports. Finally, by amending the Trade Act, Congress gave the administration new instruments to exert pressure on trading partners. In particular, the passage of the Super 301 Amendment to the Trade Act in 1988 enabled the administration to threaten retaliation against a trading partner judged to be illegitimately restricting American exports. In the second half of the 1980s, a marked geographical shift towards East Asia occurred in the cases the United States brought under Section 301. Japan replaced the European Community as the principal target—and unlike the majority of actions against the Europeans, those against Japan targeted trade in manufactures. Moreover, Korea and Taiwan also appeared prominently on the list of alleged offenders.[15]

The increasing resort by the United States to bilateralism in its trade relations with East Asia caused substantial alarm among its trading partners. These fears were not confined to the economies that were the direct targets of pressure. Other governments in the Pacific were concerned that the US tactics would cause their exporters to lose market share in the target economies. Increasingly, Pacific Rim governments looked to the formation of an economic grouping in the hope that it would help restrain US unilateralism.

The positive response of the United States to the 1985 Canadian proposal for negotiations over a free trade agreement also alarmed other governments. Together with the proposed creation of a single internal market by 1992, the Canada-US Free Trade Agreement seemed to portend a fragmentation of the global economy. For Western Pacific governments, the fear was that their exports would find it more difficult to enter their most important markets. For some economies, the trade war between the United States and the European Community over agricultural subsidies further compounded these fears. The decision by the United States to retaliate against the Europeans by increasing its support for agricultural exports through the Export Enhancement Program hurt smaller agricultural exporting economies in two ways. It drove down world agricultural prices and helped American exports displace those from other producers.

The other factor that gave substantial impetus to the formation of an inter-governmental economic grouping for the Asia-Pacific was the slow progress in the

second half of the 1980s in the Uruguay Round of GATT negotiations. In 1988 the negotiations stalled over the issue of agricultural subsidies. The promotion of progress in the multilateral negotiations figured prominently on the agenda of early APEC meetings; one means by which APEC pursued this goal was through exerting concerted pressure on the European Community.

APEC and 'open regionalism'

When ministers from twelve Asia-Pacific economies met in Canberra in November 1989 to create APEC, they agreed merely to engage in further discussions on a lengthy agenda of trade issues. These included the GATT Uruguay Round, exchange of information on indicators, policies and developments, and collaboration in specific sectors such as human resource development, energy and fisheries. In the decade since its foundation, APEC membership has increased by more than 75%, the grouping has adopted the goal of free trade for its industrialized economies by the year 2010 and for its less developed economies by 2020, and the scope of co-operation has grown dramatically.[16]

Unlike the European Union or NAFTA, there was no founding 'treaty' to launch APEC. Much remained open for negotiation among the member economies.[17] The negotiations in PECC over the previous decade, however, had established the general principles that would govern APEC's operations. The first was that APEC would not be a discriminatory regional grouping. East Asian governments had long insisted that their participation in an economic arrangement was conditional on its not being a closed economic bloc. This principle was subsequently encapsulated in the idea of 'open regionalism', the notion that any trade concessions that APEC economies made would be extended on a non-discriminatory basis to other members of the WTO. This approach to trade liberalization makes APEC unique among regional economic groupings. Consequently, unlike other regional arrangements, APEC has not had to seek an exemption from the WTO's Article I on non-discrimination.[18]

A second principle, also insisted upon by East Asian governments, was that APEC should adopt the ASEAN model of consensual decision making. The Canberra meeting agreed that 'cooperation should involve a commitment to open dialogue and consensus, with equal respect for the views of all participants'.[19] East Asian governments were particularly concerned to avoid the institutionalization of a decision-making process in which a majority would be able to impose its will against a minority.

The early emphasis in APEC's work programme was on trade facilitation and technical assistance. Such an emphasis was very much in accord with the idea that a regional economic organization for the Asia—Pacific should play roles similar to those of the Paris-based Organization for Economic Co-operation and Development.[20] In 1994, however, a significant shift in APEC's programme occurred. Pushed by the US government and by recommendations from a group of expert advisers,[21] APEC leaders, at their summit in Bogor, Indonesia, adopted an ambitious agenda for the liberalization of trade policies of the member economies. Again, in contrast to most regional economic groupings, the commitment to free trade did not

include a detailed schedule for the dismantling of tariff and non-tariff barriers. Rather, member economies were unilaterally to determine the pace of liberalization and to put forward 'individual action plans' that would document how they proposed to achieve the goal of free trade by 2010 for industrialized economies and 2020 for others.

Proponents of APEC argue that a process of 'concerted unilateral' liberalization is the only viable approach to trade negotiations, given the group's diversity and its commitment to consensual decision making. Moreover, the rapid economic growth that followed the adoption of more liberal trade policies in the mid-1980s, in South-East Asian economies in particular, is sufficient, they believe, to convince governments of the virtues of unilateral trade liberalization.[22] Other writers have been more sceptical of APEC's approach. They point out that trade liberalization is an intensely political process in which governments have to battle domestic groups that may be adversely affected by liberalization. Moreover, governments have to convince a sceptical public that trading partners will match the 'concessions' they make in trade negotiations. From this political economy perspective, APEC's 'concerted unilateralism' is deficient on two counts. First, it does not provide the certainty to domestic groups that trading partners will reciprocate trade liberalization. Second, APEC's lack of binding commitments fails to provide governments with an advantage they often enjoy when they enter international treaties; that is, their being able to point to the legal obligations that they have assumed strengthens their negotiating hand with domestic groups opposed to liberalization.[23]

In the absence of binding obligations, APEC's principal leverage over its member economies comes from peer pressure and fears of possible loss of reputation. The lack of specificity of obligations, however, reduces the effectiveness of these levers. Although a definitive judgement would be premature given that the free trade deadline for less developed economies in APEC is not until 2020, progress on liberalizing trade to date seems to justify a sceptical view. First, the member economies have not reached any clear understanding on what 'free trade' actually implies. Some governments have interpreted this phrase to mean tariffs of no more than 5%, the definition adopted by AFTA; others interpret it as zero tariffs and the removal of all official non-tariff barriers. Second, governments have disagreed over the scope of their obligations. Although attempts by North-East Asian governments to exempt agriculture from APEC were rejected at the Osaka Leaders' Meeting in 1995, the simultaneous adoption of the principle that liberalization should be 'flexible' undermined the principle of 'comprehensiveness'. Third, no consensus exists on the status of their obligations under APEC. Some member governments (especially Malaysia—but its views are shared by others in East Asia) have insisted that they regard the trade liberalization objective as 'indicative' rather than binding.

To date, the individual action plans have offered few concessions beyond the commitments that member economies had already undertaken as part of the Uruguay Round negotiations.[25] In an effort to accelerate the pace of trade liberalization, APEC leaders, at their Vancouver meeting in 1997, identified a number of areas for 'Early Voluntary Sectoral Liberalization'.[26] The hope was to build on their success in

negotiating an agreement on trade in information technology products at the 1996 Manila meeting, which paved the way for the WTO's Information Technology Agreement. Again, however, early indications are that progress in the sectoral negotiations will be difficult. Some governments have emphasized their voluntary nature, and asserted that they are not bound to negotiate in all nine sectors or on all issues within each sector.

APEC's prospects for promoting liberalization are also clouded by US concern that other traders, especially the European Union, will 'free-ride' on APEC's liberalization on a non-discriminatory basis. Economic theory suggests that the optimal policy for most economies is to remove their trade barriers unilaterally because, as relatively small players in the global economy, they do not enjoy sufficient leverage by themselves to affect their terms of trade.[27] For large economies, however, the picture is somewhat different. Their ability to deny others access to their large markets can not only affect the price at which their exports are exchanged for imports (their terms of trade) but also afford them significant leverage in international trade negotiations. By unilaterally lowering their tariffs, this source of leverage (which might be used not only for national advantage but also to promote global trade liberalization) may be lost. Washington has repeatedly signalled that it is unwilling to liberalize unilaterally unless it can be sure that its major trading partners will reciprocate.

Several possible solutions to the free-rider problem exist. One is for APEC to concentrate its liberalization on products for which intra-regional trade constitutes a very high percentage of the total trade of member economies. The 'leakage' of benefits to non-members would thereby be minimized. The problems with this approach are that it will prevent APEC from achieving its goal of total free trade and, indeed, greatly complicate movement towards this goal. Partial liberalization runs the risk of exacerbating existing distortions in member economies. A second solution would be for APEC to become a discriminatory regional agreement in which member economies made concessions only to other members. Such an approach is unlikely to be acceptable to the majority of the membership of the grouping. It would also greatly complicate the process of trade liberalization because a discriminatory arrangement would require the introduction of rules of origin to ensure that goods had been produced within the region. A final alternative, perhaps the most feasible, would be for APEC economies to make their introduction of some trade liberalization measures conditional on other traders adopting similar measures. APEC pursued this strategy in the information technology sector—where removal of member economies' tariffs was made dependent on countries accounting for 90% of world trade in these products taking similar action. APEC's eighteen member economies in 1997 accounted for approximately 55% of total world income and 46% of global trade; acting in unison, they could be a formidable bargaining force in trade negotiations.

APEC and trade tensions in the Asia-Pacific

How successful APEC will be in its push for trade liberalization remains to be seen. The expansion of APEC in 1998 to include Russia, an economy that conducts less than 20% of its trade with other APEC economies, is likely to exacerbate the difficulties of pursuing trade liberalization. APEC is more likely to make progress on a more modest agenda of trade facilitation measures and technical co-operation. For East Asian members, these are preferred areas for APEC action, and would bring APEC closer to its original goal of being an Asia-Pacific counterpart to the OECD.

Tariff levels have fallen significantly in East Asian economies in the last fifteen years. Nonetheless, for some economies they remain a significant barrier to imports (Table 16.3).

In many instances, however, non-tariff barriers rather than tariffs have been the major impediments to trans-Pacific trade, and the most significant source of trade disputes.[28]

To expect APEC to make significant progress in resolving trans-Pacific trade disputes is unrealistic. APEC, unlike the WTO, has no dispute settlement mechanisms and is unlikely to develop them. Washington has indicated clearly that it does not wish APEC to constrain its freedom of action in trade disagreements, preferring instead to use bilateral and multilateral (WTO) mechanisms. Trade tensions between Japan and the United States subsided somewhat in the mid-1990s,

Table *16.3* Average tariffs on all imports, 1990–3 (%)

Australia	10
Brunei	n.a.
Canada	11
China	36
Chile	11
Hong Kong	0
Indonesia	19
Japan	6
Korea	9
Malaysia	14
Mexico	13
New Zealand	9
Papua New Guinea	7
Philippines	20
Singapore	0.5
Taiwan	n.a.
Thailand	23
USA	6

Source: **AusAid, 'APEC and development cooperation', in Senate Foreign Affairs, Defence and Trade References Committee, APEC *Inquiry: Submissions Volume 8* (Canberra: Parliament of the Commonwealth of Australia, 1998), p. 82**

as the strong growth of the US economy in contrast to stagnation in Japan diminished earlier fears of a long-term loss of US competitiveness.[29] Nonetheless, considerable tensions remain. The idea that 'structural impediments' in the Japanese economy constrain US exports remains popular in Washington. The WTO Disputes Panel decision in the Eastman Kodak versus Fuji dispute, which found that the United States had failed to substantiate its case that the Japanese distribution system for photographic film disadvantaged the American exporter,[30] persuaded few Americans that Japan is a 'fair' trader.[31]

The rapid growth of the economy of the People's Republic of China has led it to replace Japan as the principal source of US trade deficits. These deficits are likely to be exacerbated by the financial crises that afflicted East Asia in 1997–8. In mid-1998, when this chapter was completed, it was still too early to tell how the problems that have most severely affected the economies of Indonesia, Korea, Malaysia, the Philippines and Thailand will evolve. The large devaluations of their currencies in 1997–8 normally would be expected to give a significant boost to their exports. To date, however, the severe shortage of foreign exchange experienced by these economies has stymied imports of raw materials and components that are essential for their export industries. With the European and Japanese markets growing only slowly, any recovery in East Asian exports is likely primarily to affect trade with the United States, thereby exacerbating trade imbalances and tensions.

The Asia-Pacific region, as represented by APEC, is so large and unwieldy that the prospects for the strengthening of APEC as a regional economic institution appear slim. Students of regional institutions sometimes argue that they are superior to the multilateral WTO forum for the pursuit of 'deeper' integration, for example the harmonization of regulations on capital movements and foreign direct investment. The diversity of APEC's membership, and its decision making through consensus, however, offer little advantage (and some would say several disadvantages) over multilateral trade liberalization through the WTO.

Notes

1 For the purposes of this chapter, I am taking the Asia-Pacific region to be synonymous with the membership of the Asia-Pacific Economic Co-operation (APEC) grouping. The founding members of APEC in 1989 were the (then) six member states of the Association of South-East Asian Nations (ASEAN)—Brunei, Indonesia, Malaysia, the Philippines, Singapore and Thailand—plus Australia, Canada, Japan, New Zealand, South Korea and the United States. The 'three Chinas'—Hong Kong, the People's Republic of China and Taiwan—were admitted to APEC in 1991. Mexico and Papua New Guinea joined in 1993, Chile the following year. Peru, Russia and Vietnam were admitted at the Vancouver leaders' meeting in 1997 with membership to take effect from 1998.

2 Calculated from IMF Direction of Trade data accessed through the International Economic Data Bank, Australian National University. Such comparative data must be interpreted cautiously. The larger the share of the region in world production and trade, the higher the intra-regional trade share is likely to be (the ultimate would be a world region where intra-

regional trade would be 100% of total trade). APEC includes three of the world's four largest economies: the United States, China and Japan.

3 By East Asia, I mean the economies of North-East Asia—Japan, the Republic of Korea, China, Hong Kong and Taiwan—and those of South-East Asia, the member states of ASEAN (the six listed in footnote 1 plus the later entrants of Vietnam, Burma and Laos).

4 The US Under Secretary for Economic Affairs, W.Allen Wallis, noted, for instance, that since the late 1970s US trade with East Asia and the Pacific had exceeded that with Western Europe, and by 1983 was $26 billion larger than trade with Europe. 'Traditionally', he asserted, 'we have thought of Asia as the "Far East". We looked far, and we looked east, across Europe to Asia. Now we look west, across the Pacific, to Asia. East Asia and the Pacific region have become the "Near West"' (W.Allen Wallis, 'The Near West: America and the Pacific', *Department of State Bulletin* August 1984, p. 50).

5 The scope of both AFTA and the CER was widened in the first half of the 1990s. The relationship between APEC and these 'subregional' arrangements remains problematic.

6 China has blocked participation by Hong Kong and Taiwan in ASEM.

7 On the East Asian Economic Caucus see Linda Low, 'The East Asian economic grouping', *The Pacific Review* 4:4, 1991, pp. 375–82; Richard Higgott and Richard Stubbs, 'Competing conceptions of economic regionalism: APEC versus EAEC in the Asia Pacific', *Review of International Political Economy* 2:3, Summer 1995, pp. 516–35.

8 See Lawrence T.Woods, *Asia-Pacific Diplomacy: Nongovernmental Organizations and International Relations* (Vancouver: University of British Columbia Press, 1993); and Tomako Akami, *The Liberal Dilemma: Internationalism and the Institute of Pacific Relations in the USA, Australia and Japan, 1919–1942,* PhD thesis, Division of History, Research School of Pacific and Asian Studies (Canberra: Australian National University, 1995).

9 Kiyoshi Kojima, 'A Pacific economic community and Asian developing countries', *Hitotsubashi Journal of Economics* 7:1 June 1966, pp. 17–37.

10 For details of the evolution of these organizations see Woods, *Asia-Pacific Diplomacy.*

11 See Mitchell Bernard and John Ravenhill, 'Beyond product cycles and flying geese: regionalization, hierarchy, and the industrialization of East Asia', *World Politics* 45:2, January 1995, pp. 179–210.

12 Economists have demonstrated that the rapid increase of intra-APEC trade resulted not from any new 'bias' towards other APEC economies but merely from the fact that East Asian economies were growing more rapidly than the rest of the world. Jeffrey A.Frankel, 'Is Japan creating a Yen bloc in East Asia and the Pacific?', in Jeffrey A. Frankel and Miles Kahler (eds), *Regionalism and Rivalry: Japan and the United States in Pacific Asia* (Chicago: University of Chicago Press, 1993), pp. 53–87; Peter A.Petri, 'The East Asian trading bloc: an analytical history', in ibid., pp. 21–48.

13 East Asian manufacturers proved remarkably adept at circumventing the restrictions, and at upgrading the quality of their exports in response to them. See David B. Yoffie, *Power and Protectionism: Strategies of the Newly Industrializing Countries* (New York: Columbia University Press, 1983).

14 Yoichi Funabashi, *Managing the Dollar: From the Plaza to the Louvre* (Washington, DC: Institute for International Economics, 1989).

15 See data in Thomas O.Bayard and Kimberly Ann Elliott, *Reciprocity and Retaliation in US Trade Policy* (Washington, DC: Institute for International Economics, 1994), Table 3.2, pp. 60–1.

16 The statements from meetings of APEC's leaders and ministers plus a wealth of other information are available on the APEC Secretariat's Website: http: / / www.apecsec.org.sg.

17 APEC's membership since 1991 has included two economies not regarded as sovereign states by most countries in the international system: Hong Kong and Taiwan. Accordingly, APEC's terminology refers to member economies rather than to member states.

18 Article XXIV allows for exemptions from the non-discrimination principle enshrined in Article I for regional groupings provided they comply with specified criteria. On APEC's unique approach see Vinod K.Aggarwal, 'Comparing regional cooperation efforts in the Asia-Pacific and North America', in Andrew Mack and John Ravenhill (eds), *Pacific Cooperation: Building Economic and Security Regimes in the Asia-Pacific Region* (Boulder, CO: Westview Press, 1995), pp. 40–65.

19 'Asia-Pacific Economic Cooperation, First Ministerial Meeting (Canberra, 6–7 November 1989) Chairman's Summary Statement' (http://www.apecsec.org.sg/ minismtg/ mtgmin89.html).

20 The idea for an Asia-Pacific equivalent of the OECD was first put forward by Kiyoshi Kojima and Peter Drysdale in 1968, and refined in a paper for the US Congressional Research Service by Hugh Patrick and Peter Drysdale in 1979. In his speech in Seoul in January 1989 in which the idea of APEC was first launched, Australian Prime Minister Bob Hawke made specific reference to the OECD as a possible model for the proposed grouping. Kiyoshi Kojima, 'Japan's interest in Pacific trade expansion', in Kiyoshi Kojima (ed.), *Pacific Trade and Development: Papers and Proceedings of a Conference held by the Japan Economic Research Center in January, 1968* (Tokyo: Nihon Keizai Kenkyu Senta, 1968); Peter Drysdale, 'Pacific economic integration: an Australian view', in Kiyoshi Kojima (ed.), *Pacific Trade and Development: Papers and Proceedings of a Conference held by the Japan Economic Research Center in January, 1968* (Tokyo: Nihon Keizai Kenkyu Senta, 1968); Hugh Patrick and Peter Drysdale, *An Asian-Pacific Regional Economic Organization: An Exploratory Concept Paper* (Washington, DC: US Government Printing Office, 1979); Bob Hawke, 'Challenges for Korea and Australia: speech by the Prime Minister, Mr.Bob Hawke, at a lunch of Korean business associations in Korea, on January 31', *Australian Foreign Affairs and Trade: The Monthly Record* 60:1 January 1989, pp. 5–7.

21 The APEC Eminent Persons Group, chaired by the American economist, C.Fred Bergsten.

22 Andrew Elek, 'Pacific economic co-operation policy choices for the 1990s', *Asia-Pacific Economic Literature* 6:1, 1992, pp. 1–15; Peter Drysdale and Ross Garnaut, 'The Pacific: an application of a general theory of economic integration', in C.Fred Bergsten and Marcus Noland (eds), *Pacific Dynamism and the International Economic System* (Washington, DC: Institute for International Economics, 1993), pp. 183–223.

23 On the political economy of trade negotiations see Helen V. Milner, *Interests, Institutions, and Information: Domestic Politics and International Relations* (Princeton, NJ: Princeton University Press, 1997). For a more detailed discussion of the incentive problem in APEC, see John Ravenhill, 'Bringing politics back in: the political economy of APEC', in Il Sakong, Ku-Hyun Jung and Jang-Hee Yoo (eds), *Asia-Pacific Economic Cooperation: Current Issues and Agenda for the Future* (Seoul: Institute of East and West Studies, Yonsei University, 1996), pp. 1–27.

24 See, for instance, *The Economist* 25 November 1995.

25 C.Fred Bergsten (ed.), *Whither APEC? The Progress to Date and Agenda for the Future* (Washington, DC: Institute for International Economics, 1997). One exception is a reform package offered by the People's Republic of China. This, however, appeared to be motivated

more by its government's desire to secure entry into the WTO than by a commitment to APEC.

26 The nine sectors listed for urgent action were: environmental goods and services; energy; fish and fish products; toys; forest products; gems and jewellery; medical equipment and instruments; chemicals; and a telecommunications mutual recognition arrangement (APEC—Ninth Ministerial Meeting) (http://apecsun.apecsec.org.sg-/minismtg/mtgmin97.html).

27 John Whalley, *Trade Liberalization among Major World Trading Areas* (Cambridge, MA: MIT Press, 1985).

28 Non-tariff barriers (NTBs) are notoriously difficult to measure. Moreover, attempts to identify NTBs seldom include 'structural impediments' to trade. For one estimate of some NTBs in APEC, see Pacific Economic Cooperation Council, *Survey of Impediments to Trade and Investment in the APEC Region: A Report by the Pacific Economic Cooperation Council for APEC* (Singapore: Pacific Economic Cooperation Council, 1995).

29 Such fears had been fanned in the 1980s by the development of strategic trade theory, a branch of economic theory that suggested that governments could intervene to promote the interests of domestic companies at the expense of their foreign competitors. For discussion see Richard G.Lipsey and Wendy Dobson (eds), *Shaping Comparative Advantage* (Toronto: C.D.Howe Institute, 1987); Paul R.Krugman (ed.), *Strategic Trade Policy and the New International Economics* (Cambridge, MA: MIT Press, 1986); Laura D'Andrea Tyson, *Who's Bashing Whom? Trade Conflict in High-Technology Industries* (Washington, DC: Institute for International Economics, 1993).

30 A summary of the WTO findings is available on the WTO Website at http://www.wto.org/wto/dispute/bulletin.htm.

31 An enormous literature exists on the question of whether Japan's trade structure is in accord with its geographical location and factor endowments. See, for instance, Robert Z.Lawrence, 'How open is Japan?', in Paul R.Krugman (ed.), *Trade with Japan: Has the Door Opened Wider?* (Chicago: University of Chicago Press, 1991), pp. 9–37; Robert Z. Lawrence, 'Imports in Japan: closed markets or minds?', *Brookings Papers on Economic Activity* 2, 1987, pp. 517–48; Edward J.Lincoln, *Japan's Unequal Trade* (Washington, DC: Brookings Institution, 1990); John Ravenhill, 'The "Japan problem" in Pacific trade', in Richard Higgott, Richard Leaver and John Ravenhill (eds), *Pacific Economic Relations in the 1990s: Cooperation or Conflict?* (Boulder, CO: Lynne Rienner, 1993), pp. 106–32; Gary R. Saxonhouse, 'Comparative advantage, structural adaptation, and Japanese performance', in Takashi Inoguchi and Daniel I. Okimoto (eds), *The Political Economy of Japan: Volume 2. The Changing International Context* (Stanford, CA: Stanford University Press, 1988), pp. 225–48; Gary R.Saxonhouse, 'What does Japanese trade structure tell us about Japanese trade policy?', *Journal of Economic Perspectives* 7:3, Summer 1993, pp. 21–43.

Further reading

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Jeffrey A.Frankel and Miles Kahler (eds), *Regionalism and Rivalry: Japan and the United States in Pacific Asia* (Chicago: University of Chicago Press, 1993).

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Chapter 17
The European Union

Michael Smith

The European Union (EU) is the world's largest single trading entity, accounting for something over 20% of total world trade. Although historically its strengths have been based on exchange of manufactures and industrial goods, increasingly the EU's international economic presence reflects its leading role in the international service economy, which by some estimates accounts for something like 60% of its international activity. In 1996, according to provisional figures issued by Eurostat, the EU's statistical agency, the EU ran a trade surplus of ECU46.3 billion with the rest of the world, reflecting exports of ECU620 billion and imports of ECU573.7 billion.[1] The EU is thus not only a major presence in the world trading system; it also trades at a profit.

This general picture, though, conceals significant differences between different trading relationships. Whilst the EU's relationship with the United States—its predominant external trading link—is approximately in balance year on year, it runs consistent deficits with Japan. The reverse of the EU's strength in industrial products and services is a weakness in commodities and in semi-manufactured products. And although there are areas of considerable strength in high-technology exports, there are also crucial weaknesses, for example in semiconductors and other areas of information technology equipment. Perhaps most importantly, a view of the EU based on trade between the Union and the rest of the world misses out what has historically been the most dynamic element of its trading activity: trade between the Union's member states themselves, or so-called 'intra-trade'; in many areas of trade the member states find each other at least as interesting as the outside world. This tension between the development of internal commerce and the demands of international trade is, of course, experienced by many countries in the global economy.

But the EU is not a 'country' in the normal sense of the word. It is an entity which in many respects mimics the actions and performance of states and national governments, but which in some crucial aspects is different. In the global arena, this raises questions about the capacity for action, influence and leadership of the Union; in the EU itself, it raises questions about the process of trade policy making and about the tensions between EU and other levels of economic action.[2]

This chapter centres on these questions about trade policy making and international role. It does so by focusing on three key areas: first, the characteristics of the EU as a 'region' in trade politics; second, the issues arising for trade policy

making; third, the implications for EU activities and roles in the wider world arena. It concludes with an evaluation of key trends and future prospects for trade politics in the EU.

The EU as a 'region'

Compared with other regions under examination in this part of the book, the EU is distinctive; indeed, it is often argued that the Union is *sui generis* in the world political economy. This argument is based on a number of features, perhaps the most important and distinctive of which is the EU's dense and far-reaching institutionalization. The Union represents the fruits of a process which began in the 1950s with the establishment of the European Coal and Steel Community (ECSC), the European Economic Community (the EEC) and the European Atomic Energy Community (Euratom); this will reach new levels of activity and influence when, during 1999, a majority of members of the EU established Economic and Monetary Union, centring on a common currency, the Euro.[3]

Even this brief sketch indicates the exceptional nature of the institutional framework established in the EU.[4] For our purposes, the key areas of the framework are those in the 'first pillar' of the EC. From the outset, European integration had an external dimension. Indeed, it could not help but do so, since the establishment of decision-making bodies in key economic areas entangled the Communities immediately in the development of the world political economy. In many ways, the earliest of the Communities' common policies was the Common Commercial Policy, based on Article 113 of the EEC treaty. Once this was in place, it was inevitable that there would be a call for trade negotiations and trade agreements—and also that there would be trade disputes as the Community's policies developed.

The responsibility for handling trade relations between the Community and the outside world was given to the European Commission, which still retains this leading role. This executive agency thus has some of the institutional attributes of a 'government' for trade policy purposes, but as we shall see later these attributes are not unchallenged. In fact, the EC in trade policy terms is a curious hybrid: the Commission has the responsibility for conducting negotiations and administering trade policy instruments, but the member states retain important areas of influence and representation. Thus, in the WTO, the Commission now formally represents the Community, but each of the fifteen member states is also a member. Such hybrid forms also exist in other trade-related bodies such as the Organization for Economic Co-operation and Development (OECD).

Although the EU, through the EC, is thus heavily involved in the trade policy arena, the influence of its institutions does not stop there. The EC has developed a complex and sophisticated economic policy system in a number of areas central to the world political economy—for example, in agriculture, industrial and technology policies and in the area of economic development assistance. Not only this, but through the programme to complete the Single European Market (SEM) during the early 1990s, it developed a major capacity in regulatory policy and standards setting. The advent of EMU will create a further dimension to EC institutional capacities in the

area of monetary and macro-economic policy, although it remains to be seen how far this will extend into fiscal policy, for example. This pattern of dense and firmly based institutional growth surrounds EU trade policies with important institutional assets, whose management and deployment is bound to influence the broader trade policy arena.[5]

From what has been said already, it can be seen that the institutional framework is not the only feature bearing on the EU's trade politics. Equally important in many ways, and linked to the working of the institutions, are the relations between the member states themselves, which can encompass deep differences in trade 'culture', between protectionism and free trade, for example. Also, as the Community grew, it was clear that its 'centre of gravity' shifted, essentially towards the south and the Mediterranean, whilst the 'triangle' of France, West Germany and the UK remained the core. The addition of Austria, Finland and Sweden in 1995 shifted the balance again, to the north, whilst further enlargement in the Mediterranean and particularly Eastern Europe during the early 2000s will represent an even more significant movement.

A key feature of the EU as a 'region' in trade politics is thus the relationship between its member states on two levels: first, the links between the core of major states; and second, the balance between this core and the shifting focus of the EU as a whole. When this is added to the balance between the EU's institutions—especially the Commission—and the member states in general, we can begin to see some of the layers of trade policy formation. A further layer is added by the fact that the EU, as well as being the largest single market in the world, is heavily penetrated by external influences. The process of globalization has found some of its most potent expressions during the 1990s in the EU, through a spate of mergers and acquisitions and through the influence of increasing investment by American and other multinational firms. In some areas, this penetration has extended to such a level that it is difficult to identify exactly what is a 'European' and what is a 'foreign' company, with consequences for trade politics which will be examined later in this chapter.[6] The Single Market programme, though, only accentuated a trend which had been evident from the foundation of the EEC in the 1950s, towards the intensification of foreign investment and the formation of corporate links between the Community/Union and the global political economy.[7]

One consequence of this penetration of the EU and the Single Market has been growing salience for the politics of regulation and market access, as opposed to traditional trade politics. Given the multilayered linkages between multilateral institutions, the Union's institutions, national governments within and outside the EU and a host of private corporate actors, it has become apparent that the 'inside' and 'outside' of the EU are intimately connected if not indistinguishable. The Single Market can thus be used as a weapon or a source of influence at the same time as it forms a powerful attraction for non-EU actors in the world political economy. There is a tension here between two images of the EU: on the one hand, the EU and its market as a 'magnet', attracting exchange and investment; on the other hand, the EU as a

(potential) 'fortress', dedicated to preserving the advantages of those inside the walls and committed to the framework.

The tension between 'magnet' and 'fortress' in the EU's trade politics is given greater weight by the fact that the Union is expanding. There has never been a time since its establishment when the EC/EU has not been negotiating with applicants for membership, admitting new members or coping with the consequences of their admission. As time has gone on the EU has 'internalized' a growing part of the world economy, not only through the growth of trade between its existing members but also through the incorporation of new members. Each such expansion has consequences not only for the EU itself but also for the pattern of trade in the global arena, for accompanying issues of investment or of regulation, and for the effectiveness of institutions at the regional or at the global level.

Finally, we must note another feature of the EU as a 'region', which arises directly out of its roots as a 'trading state' and its predominant concern with the stability and growth of the world political economy. To put it simply, the EC and the EU have a basic tendency to seek stability and predictability in the world arena, and have bent considerable efforts towards the encouragement of these qualities. As a result, there has emerged a complex system of 'environmental management' in which the Community/Union has developed a network of agreements with both its near neighbours and those further afield. This has been described as a 'pyramid of privilege', constructed around partnership and co-operation agreements, preferential trade agreements and association agreements (the last often with potential future members). A question that inevitably arises is whether this web of agreements can be effectively managed and adapted to changing circumstances.

What are we to make of this complex picture? Throughout the discussion, we have used the term 'region' to describe the features of the EU, but it is clear that it is more than simply an expression of the regionalization of processes of production or exchange. Compared with other regions examined in this book, the EU has a much harder 'shell' of institutions and practices, which give it a distinctive presence and impact. Some have gone so far as to describe the EU as a 'trade superpower', or as one of the key components in a world of competing blocs.[8] But these images are at odds with the complex and multilayered processes we have described here, which raise important problems of access, management and institutional capacity. In the next section, we explore some of the issues in trade politics to which these features give rise.

Issues in EU trade politics

Internal issues

The first internal issue to assess, and one which has been at the centre of EU trade politics since the beginning, is that of competence and legitimacy. As already noted, the EU—and particularly its 'first pillar', the EC—has a strong and well-rooted institutional existence.

For our purposes, the key issue is that of what might be described as the 'division of powers' in trade policy, which arises from the workings primarily of Article 113 (now Article 133 in the consolidated EU treaty of 1997 and after). This article is often said to give the EC exclusive competence in the conduct of trade negotiations and the making of trade agreements.[9] Two qualifications are in order, however. First, the 'Community method' of decision making means that although the EC may be given competence (and the Commission given the responsibility of negotiating or otherwise applying that competence), there is in fact a division of powers. For trade negotiations such as those carried out in the Uruguay Round, the Council of Ministers, representing the member states, acts on a proposal from the Commission to produce 'negotiating directives'; these guide the Commission in the negotiations, but can be revised especially during extended negotiations. In other areas, such as the use of anti-dumping legislation, the Commission may have the power to impose provisional measures, but this must then be validated by the Council. In addition, when it comes to trade agreements, the European Parliament (EP) has the power of assent over the final outcome. The result is a constant if muted tension between the institutions, particularly when the Commission seeks to expand its freedom of action in trade matters. This in turn is given new dimensions by the changing nature of world trade, which means that the issue of competence can be raised almost continuously, for example by the growth of trade in services.

The Uruguay Round, by dealing with such issues as services and intellectual property, gave new focus to the problem. In EU terms, the agreements themselves created a political problem: although the Commission acting for the Community had negotiated the agreements, was it competent to operate them? The net result of the argument was that on the 'new' issues, the Commission had in each case to act jointly with the member states.[10] Although the Commission asked again for an extension of competence in the negotiations for the Amsterdam Treaty of 1997, the final text contained only a provision that issues of competence in the 'new' areas should be agreed between the Council and the Commission on an *ad hoc* basis (requiring a unanimous vote in the Council).

Such a tension over matters of competence expresses in part a second key issue: the differing philosophies and preferences of EU member states when it comes to matters of international trade. We noted earlier the tension in the EU between 'free traders' and 'protectionists', which often (but not always) corresponds to a North-South tension. In the original Community of six members, the French and the Italians were in general more protectionist and interventionist than the Germans and the Dutch, for example; this in turn reflected national positions on key internal policies such as the Common Agricultural Policy, which fed through into external commercial policy. As the Community and then the Union have grown, the balance has shifted several times, leading to fluctuations in trade policies.

The effects of this fluctuating balance are to be seen both at the broad strategic level and in the operation of specific trade policies within the EU. Strategically, the EU's entry into broad global trade arrangements is almost invariably accompanied by hard bargaining within the Union, in which the more protectionist elements attempt to preserve the Union's 'trade defences'; thus in the final stages of the Uruguay Round

negotiations, the French and others were able to extract commitments to strengthen surveillance and unfair trade measures as part of the price for their agreement.[11] At the level of operational policy, some of the more striking examples are provided by the EU's anti-dumping measures. For example, in 1997, the Commission (responding to pressure from mainly French cotton producers) imposed provisional anti-dumping duties on imports of unbleached cotton. This move evoked the opposition both of cotton processors in the Union and of the more 'free-trade'-orientated member states. As a result, the provisional duties were not confirmed by the Council of Ministers. But during late 1997 and 1998, again under pressure from the French and Eurocoton (the producer body), the Commission not only reopened the anti-dumping investigation, but also reimposed provisional duties.[12]

As these examples indicate, there are a number of important audiences and influences present in the EU's trade policy community. From the outset, there have been organizations in Brussels and elsewhere designed to promote the interests of producers or consumers in relation to trade policies; for a long time, perhaps inevitably, these organizations represented predominantly producer interests, but during the 1990s they have experienced a number of important transformations. The cast of characters on the trade policy stage now includes trade union interests, consumer lobbies, a wide range of non-governmental organizations with interests in such areas as human rights, and a range of local and regional agencies from within member states. As a result, the management of trade policies has become less technocratic and more subject to pressures for accountability and short-term responsiveness. Arguably, this has increased the constraints on the trade policy makers, and thus the possibility of inconsistency and reactiveness on their part. It can be seen that this brings us back again to issues of legitimacy and authority in EU trade politics, and also that it links processes in the EU with those for example in the United States, where politicization of trade policy is a long-established fact of life.

External issues

Article 113 of the EC treaty, signed in 1957, committed the EEC as it was then not only to internal co-ordination of trade policies but also to an active role in the liberalization of world trade. Integral to the bargains that set up the Community (and indeed to the establishment of the ECSC before it) was recognition of the external forces to which it would become subject, and the global constraints imposed by institutions and other actors. Indeed, the EEC as a customs union could only be set up explicitly under the provisions of article **XXIV** of the GATT, and—less formally—with the acquiescence of the United States as the dominant economic power. The playing out of these external forces has been a constant theme in the trade politics of the EC and then the EU, and can be seen in terms of the major external relationships in which the EU is embroiled.

Predominant in the EU's external environment are the relationships with other industrial countries and groupings. In particular, the relationship with the United States embodies the largest flows of goods, services and capital in the global economy. At the same time, the links between the EU and its near neighbours in

Europe have been consistent and intimate, to the extent that a number of the former members of the European Free Trade Area (EFTA) are now members of the EU itself, and even the remaining members of that body and the European Economic Area constitute one of the EU's largest external relationships. Links with Japan are less intense than those with the United States, but generate a considerable number of trade disputes as well as efforts to collaborate. The links between the EU and other industrial groupings thus embody what has often been called the 'management of interdependence'; those involved in the relationships need each other and profit from each other, but the very intensity of the links between them creates a vital need for active management of the inevitable disputes and tensions.[13] We shall see in the next section how these needs are translated into mechanisms of co-operation.

Another key focus for EU trade politics is what some have termed the 'near abroad': those countries in Central and Eastern Europe, the former Soviet Union and the Mediterranean which have proliferated during the 1990s as the result of the end of the Cold War.[14] During the height of the Cold War, in a way the trade politics of many of these links were repressed, with the US—Soviet confrontation and the predominance of security or ideological concerns acting as a kind of insulation. The era following the Cold War has seen an eruption of trade politics, as those in the 'near abroad' seek new patterns of exchange and the EU seeks to stabilize or manage the consequences of this disruption. Here, we see the true power of the EU's 'magnet' role; many of the countries concerned not only want to develop new trade and investment links with the EU and its members, they also want to become members. As a result, the EU has spent much of the 1990s searching for ways of managing these demands—at one level, by reaching new trade and co-operation arrangements, and at another level by preparing for a new and far-reaching enlargement process.[15] The difficulty from the Union's perspective is that these two things are inextricably linked, and that what might be seen as technical economic provisions are heavy with political symbolism. In particular, the relationships with Central and East European countries (the CEEC) have moved through a number of hard-fought bargaining stages: first, the attempt to construct new trade and co-operation agreements, then the 'Europe Agreements' which embodied closer co-operation and eventually preparations for membership, and finally, the pre-accession and accession stage, in which anything up to ten new members might be admitted during the first decade of the new century. Not only does this pose an immense negotiating challenge for all of those involved, but also it implies a major redirection and rebalancing of the EU's external trade patterns and of many of its internal policies such as the CAP, with consequent effects on a number of 'great outsiders' such as the United States.

Whereas the relationships between the EU and its industrial rivals illustrate the 'management of interdependence', it is clear that relations with the 'near abroad' embody considerable asymmetries and patterns of dependency. The trade politics of these relationships is thus distinct, although in themselves they are differentiated between 'pre-members', possible members and those who will never be members. The last are in some ways more like the countries of the African, Caribbean and Pacific (ACP) grouping, who have relations with the EU largely through the Lomé

Conventions; here, the emphasis is on economic restructuring and technical assistance as well as on specific provisions for market access for sensitive commodities.[16] Although it is in many respects odd to link developing countries in the 'South' with countries in the 'near abroad' such as Russia or the Ukraine, the point here is that when we move into these areas we are dealing more with the trade politics of dependency than with those of interdependence and interpenetration, and thus that the issues for the EU are different. This is not to say that these problems are disconnected from each other, however: one of the first effects of the ending of the Cold War and the redirection of EU interest towards the East was a fear in ACP countries that they would lose out. It must also not be forgotten that a number of developing countries have important sponsors in the EU itself—not least those such as France, the UK, Spain and Portugal whose former colonies have an obvious claim for their attention.

Each of these sets of relations has to be seen not only as a discrete source of trade policy issues but also as embedded in a global system. As has been pointed out many times in this book, the processes of globalization and regionalization have posed challenges to all of those involved in trade politics; we have already noted that the EC and the EU are inseparable from the development of the broader world trading system. Whereas with industrial partners we are concerned with the politics of interdependence and interpenetration, and in the case of developing countries we confront the politics of dependency, in the case of the global system we are presented with what might be termed the politics of compatibility. The central question here is: to what extent are the EU's trade policies and practices compatible with the multilateral system or with the activities of other regional groupings?

This is not simply an abstract issue. The EEC originally was set up within the GATT system, but it has created a number of important frictions with multilateral trade rules as it has developed and grown.[17] Indeed, even before the Treaty of Rome in 1957, the ECSC had caused frictions with American steel producers who claimed that it set up an illegal cartel and thus traded unfairly. During the 1960s, the development of the CAP in particular created important tensions with the United States, whilst the successive enlargements of the EU have created a demand for compensation as more and more countries are surrounded by the customs union and the Common External Tariff. The programme to complete the Single Market during the late 1980s and early 1990s also raised important issues for the multilateral system, since many of the areas in which the Single Market had most effect (e.g. regulatory policy, trade in services) were precisely those most at issue in the Uruguay Round.[18] Quite apart from these broad issues, there have been many instances of complaints against specific EU trade measures (most of them from the United States), ranging from the treatment of banana imports to the apparent subsidization of large civil aircraft. The EU has an important interest in defending itself against these complaints, and specific EU producer groups have even more intense feelings; but at the same time, the EU profits immensely from the maintenance of the multilateral system, and is inexorably committed to its strengthening (see below). The result is another series of essentially political issues.

The EU also has important interests in developing relationships with other regional groupings, and has pursued a consistent policy of promoting and maintaining such relationships. Indeed, it could be argued that links with such groupings as Mercosur (the Southern Common Market) in Latin America and ASEAN (the Association of South-East Asian Nations) are important not only in terms of EU trade policy interests, but also and much more broadly in terms of competition among the leading trading entities within the global arena. During the mid-1990s, the Commission in particular developed a wide-ranging strategy of developing links with regions in which the EU's profile had historically been underdeveloped. This led for example to the establishment of the Asia-Europe Meeting (ASEM), between the EU and ten Asia-Pacific partners, which met for the first time in March 1996 and then again in London in April 1998. ASEM was explicitly linked by the EU not only with the promotion of interregional trade and investment, but also with some broader security issues and with the assertion of an EU presence in a region previously dominated by the United States and Japan.[19]

Issue-linkages

In this section, the focus is on three types of issue-linkage which have profound implications for trade politics in the EU: first, the internal/external linkage; second, linkages between policy sectors; finally, the question 'who are EU?'[20] in trade policy. In the first case, it is clear that many issues in EU trade politics cannot be neatly consigned to the 'internal' or 'external' box. As an example, consider the question of international air transport. This is a vast and rapidly growing area of international exchange and service provision, which by its very nature crosses national boundaries. During 1996 and 1997, the EU Transport Commissioner, Neil Kinnock, attempted to establish the competence of the Community and thus the Commission to enter into negotiations on air routes with the United States, but at the same time a number of EU member states were busily negotiating 'open skies' agreements with Washington, often linked to particular inter-airline alliances involving national airlines. The complexity and variety of the linkages thus generated was a major challenge for EU policy.

There are also important linkages between air routes and other dossiers in EU policy. In particular, there is a major connection with competition policy (an area central to 'new trade policy'). During 1997, for example, British Airways and American Airlines proposed to merge, creating what can be seen as a 'dominant position' in transatlantic air transport. This was of course of great interest to the Commission in its role as competition watchdog, and to the anti-trust authorities in the United States. But it was also linked to British-American negotiations on an 'open skies' agreement, and to issues as apparently technical as the allocation of landing slots at airports in the UK and the United States.

The case of air routes is only one of a number of challenging policy issues embodying both internal/external linkages and intersectoral linkages. In the area of more conventional trade politics, the EU has been confronted by the complexities of relationships between importers and exporters, producers and consumers, in areas as

diverse as the trade in handbags, mountain bikes, bananas and semiconductors.[21] Likewise, theCommission has had to deal with major cross-sectoral linkages in the context of negotiations as large scale as those of the Uruguay Round or the 'Europe Agreements' and as intimate as those on teddy-bears from China or the liquor tax in Japan. In all of these areas, the EU has been engaged in dealings not only with other governments but also with international institutions and with private corporations, trade associations and pressure groups.

The upshot of these complex interactions in EU trade politics is a European version of the question posed by Robert Reich, 'Who is US?', given the increasing evidence that territory and tangible assets matter less in international exchange and competition than knowledge and intangible resources.[22] For the EU, the question in a sense has always been there, given the in-built tensions between institutions, and between institutions and member states. But the 1980s and 1990s have exposed it even more sharply, as the implications of increasing interpenetration and the impact of globalization have made themselves felt. Susan Strange has rephrased Reich's question as 'Who are EU?' in exploring the ways in which firms have responded to the pressures and opportunities of the global marketplace.[23] In this marketplace, it is increasingly difficult to identify the 'European' as opposed (say) to the 'American' or 'Japanese' interest in specific policy areas.

We are left with an image of the major issues in EU trade politics which is complex and challenging. At one level, it clearly validates the focus of this book on multilevel and multilayered trade politics processes, but then the EEC and the EU have embodied those qualities since the 1950s. At another level, it validates the proposition that the growth of interdependence and interpenetration exacerbate the 'who is us?' issue; the EU has always experienced this challenge, in the context of a shifting internal balance as well as a changing membership, and, moreover, it has long experience of the intersection between the public and the private in the management of trade policy, both in its internal market and in the world arena. EU trade politics is characterized above all by an emphasis on process, rather than on results, a feature which can make it difficult for those with other presuppositions to accommodate the European style. It is also characterized by an underlying tension, sharper in the 1990s than before, between technocratic styles of trade policy making and broader questions of accountability. It remains for this chapter to explore some of the implications of these patterns.

Implications

In this section, we identify five areas of enquiry: first, strategic coherence and credibility; second, processes of bilateral management; third, interregional and intersystem co-operation; fourth, multilateral rule making; finally, private management of trade policy issues. All are central to an evaluation of EU trade policy in the late 1990s.

The argument in this chapter suggests that whilst there are areas in which the EU's strategic action capacity and its status are well established, there are others in which it reaches the limits of its resources. We have seen examples of this in 'new agenda'

items such as air transport, but we have also seen that the boundaries of EU effectiveness are constantly shifting, and it can be argued that there is an underlying trend towards the accumulation of greater legitimacy, coherence and credibility.[24] There is also a contrast in EU policy between the capacity to establish broad strategic directions and frameworks, and the capacity to achieve results in specific issue areas; the Commission is a fertile source of documents setting out frameworks for the development of relationships, but these cannot always be implemented in detail, because of the intervention of both internal and external forces. It could be argued that there is an inherent conservatism and defensiveness about EU strategy resulting from the complex internal constraints—more complex than in other major trading entities—but this may be a difference of degree rather than a difference of kind.

The structure and process of EU trade policy making have not prevented it from entering into a complex web of bilateral trading relationships, often with innovative institutional structures. The most elaborate of these can be found in the relationships with the United States—through the Transatlantic Declaration of 1990, and the New Transatlantic Agenda of 1995—and with the members of the European Economic Area; others have developed during the 1990s with the countries of the 'near abroad' (see above). In many of these cases, there has been a capacity on the part of the EU to export its internal model of mutual recognition and market organization, and to use its internal assets as the basis for model building in the global arena. This does not mean there are no problems and no consequent disputes, but we must remember that the EU is based on the world's largest integrated market, making it at least probable that it will become embroiled in a significant range of trade conflicts.

The picture is thus one of complexity and of intersecting, sometimes contradictory, pressures. The complexity extends into the third area, that of interregional and intersystem competition. It was pointed out earlier that the EU has long been active in building interregional links, and that increasingly these have been defined as part of a competitive 'game' with the United States and Japan (predominantly the former). Some would take the argument further and contend that the EU has an in-built dynamic towards the building of bloc structures, either through the incorporation of new members and new activities or through the construction of cross-regional alliances (or both). There is no doubt that the EU has acted to stabilize its near neighbourhood, and that it has acted to develop interregional links such as those with Latin America and the Asia-Pacific. Trade policy has been instrumental in such activities, as it has been for the United States, but unlike the United States, the EU cannot at present offer the non-commercial assets of security policy.[25] This may of course be seen as a strength rather than a weakness, and it raises a crucial question about the extent to which the EU as a predominantly 'civilian power' can muster a comprehensive trade policy.

Next, we should examine multilateral rule making. The EEC, the EC and the EU have been thoroughly embedded in the multilateral trade regime from the outset: the Community, and the Commission as its representative, have accumulated considerable legitimacy and experience in dealing with global trade problems. Despite the issues of competence and authority outlined earlier, it seems clear that in

all but the most taxing of cases the Community can act as the EU's agent in the global trading order.[26] This does not mean that the member states have been reduced to the status of Connecticut or Bavaria: they can and do still exercise a powerful influence on the Union's activities. But it does mean that the EU, with its central role, its weighty stake in the multilateral system and its capacity to adapt and innovate at the strategic level, can be a powerful actor in world trade politics. Such a conclusion is borne out by experience since the Uruguay Round, in which the EU has often functioned as a leading force in defining new sectoral agendas and forming coalitions (to such an extent that in some areas such as financial services the United States has appeared decidedly reactive and defensive, whilst the EU has the initiative).

Finally, it is apparent from the discussion here that the EU not only experiences the challenges arising from the interaction of public and private in the world trading system, but also has considerable resources with which to tackle the resulting problems. Increasingly, the EU has become the focus of the lobbying and of the pressures arising from the interests of firms and other private groupings. It has developed a strong set of working relationships with these parts of the European trade policy community, and actively promotes the networking and the communication which sustains trade politics in the late 1990s. There is of course a set of intersecting pressures here—between firms from different national contexts, member state governments, 'outsiders' who are also 'insiders', cross-national and intercontinental alliances. The claim made by Lester Thurow in the early 1990s, that the EU with its experience of handling complex multinational markets would predominate in a twenty-first century in which that experience would be a crucial power resource, is in part borne out by such evidence, but the story is not a simple one of ever increasing resources and influence.[27]

Conclusion

It is easy to imagine an EU in the year 2010 with perhaps twenty-five members and with a stable single currency, which could use these assets to play a predominant role in world trade and investment. After all, the advantages of scale and of financial management would be significant if not crucial. The discussion in this chapter does not rule out such an outcome. What it does do, though, is to indicate two things: first, that reaching the two goals of major enlargement and EMU is likely to be very hard work and to absorb a good deal of the energy of the EU and its member states; second, that the concomitant increases in the internal complexity of the EU and its trade politics will not allow a simple linear relationship on the lines of 'more means better'. For trade politics in particular, the chapter has indicated a number of features and issues which simultaneously bestow enormous influence and potential on the EU and limit the extent to which that influence and potential can easily be deployed. The EU may be a 'trade superpower', but it will continue from time to time and from issue to issue to display its feet of clay.

Notes

1 'EU trade surplus widens', *Financial Times* 24 April 1997, p. 2.
2 For other treatments dealing with these questions, see the list of further reading at the end of this chapter.
3 As of the writing of this chapter, four of the EU's fifteen member states were set to abstain from the 'first wave' of EMU: Denmark, Sweden and the United Kingdom (each of which chose not to proceed) and Greece (which did not meet the criteria for inclusion).
4 For fuller discussion, see Christopher Piening, *Global Europe: The European Union in World Affairs* (Boulder, CO: Lynne Rienner, 1997), chapter 1; Christopher M.Dent, *The European Economy: The Global Context* (London: Routledge, 1997), chapter 6.
5 See also Loukas Tsoukalis, *The New European Economy Revisited* (Oxford: Oxford University Press, 1997), chapter 10.
6 For treatments of these issues see, for example, B.Burgenmeier and J.L.Mucchielli (eds), *Multinationals and Europe 1992: Strategies for the Future* (London: Routledge, 1991); Mark Mason and Dennis Encarnation (eds), *Does Ownership Matter? Japanese Multinationals in Europe* (Oxford: Oxford University Press, 1994); Susan Strange, 'Who are EU? Ambiguities in the concept of competitiveness', *Journal of Common Market Studies* 36:1, March 1998, pp. 101–14.
7 See John Dunning and Peter Robson (eds), 'Multinational corporate integration and regional economic integration', in John Dunning and Peter Robson (eds), *Multinationals and the European Community,* special issue of the *Journal of Common Market Studies 26:*2, June 1987, pp. 103–25.
8 See, for example, Lester Thurow, *Head to Head: The Coming Economic Battle among Europe, Japan and the United States* (New York: Morrow, 1992); for a very recent view, see Mark Turner, 'Unified trade policy gives EU superpower status', *European Voice* 26 February-4 March 1998, p. 13.
9 For detailed analysis of the EU's trade policy powers see I. Macleod, I.D. Hendry and Stephen Hyatt, *The External Relations of the European Communities* (Oxford: Oxford University Press, 1996), esp. Part 1; see also Michael Smith, 'The Commission and external relations', in Geoffrey Edwards and David Spence (eds), *The European Commission* 2nd edition (London: Cartermill, 1997), pp. 264–302.
10 See Macleod, Hendry and Hyatt, *External Relations,* chapter 3.
11 See Hugo Paemen and Alexandra Bensch, *GATT to WTO: The European Union in the Uruguay Round* (Leuven: Leuven University Press, 1995).
12 David Allen and Michael Smith, 'External policy developments', in Geoffrey Edwards and Georg Wiessala (eds), *The European Union 1997: Annual Review of Activities* (Oxford: Blackwell, 1998), pp. 69–91.
13 Dent, *The European Economy,* chapter 5.
14 Piening, *Global Europe,* chapter 4.
15 See Christopher Preston, *Enlargement and Integration in the European Union* (London: Routledge, 1997).
16 See Marjorie Lister, *The European Union and the South* (London: Routledge, 1997).
17 Stephen Woolcock, 'The European *acquis* and multilateral trade rules: are they compatible?', *Journal of Common Market Studies* 31:4, December 1993, pp. 539–58.
18 See Stephen Woolcock and Michael Hodges, 'EU policy in the Uruguay Round', in Helen Wallace and William Wallace (eds), *Policy-Making in the European Union* (Oxford: Oxford University Press, 1996), pp. 301–24; for a detailed treatment of the implications for EU-US

relations, see Brian Hocking and Michael Smith, *Beyond Foreign Economic Polity: The United States, the Single European Market and the Changing World Economy* (London: Cassell/Pinter, 1997).

19 For a detailed treatment of the EU's relations with the Asia-Pacific, see Michael Smith, 'The European Union and the Asia-Pacific', in Anthony McGrew and Christopher Brook (eds), *Asia-Pacific in the New World Order* (London: Routledge/The Open University, 1998), pp. 289–315; see also Dent, *The European Economy,* chapter 5.

20 This question is posed by Susan Strange, 'Who are EU?'.

21 See David Allen and Michael Smith, 'External policy developments', in successive editions of *The European Union: Annual Review of Activities* (Oxford: Blackwell, 1995, 1996, 1997, 1998).

22 Robert Reich, The *Work of Nations: Preparing Ourselves for Twenty-first Century Capitalism* (New York: Knopf, 1991), chapter 25.

23 Strange, 'Who are EU?'.

24 Michael Smith, 'The European Union, foreign economic policy and a changing world economy', *Journal of European Public Policy* 1:2, Autumn 1994, pp. 283–302; Michael Smith, 'Competitive co-operation and EU-US relations: can the EU be a strategic partner for the US in the world political economy?', *Journal of European Public Policy* 5(4):561–77, 1998.

25 See Piening, *Global Europe,* chapter 9.

26 For a discussion of this 'actor/agent' relationship, see Michael Smith, 'Does the flag follow trade? "Politicisation" and EU foreign policy', in John Peterson and Helene Sjursen (eds), *A Common Foreign Policy for Europe? Competing Visions of the CFSP* (London: Routledge, 1998), pp. 77–94.

27 See Thurow, *Head to Head,* chapter 10.

Further reading

David Allen and Michael Smith, 'External policy developments', in Neill Nugent (ed.), *The European Union: Annual Review of Activities* (Oxford: Blackwell, 1995, 1996, 1997).

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Chapter 18
A free trade area of the Americas in 2005?

Paulo S. Wrobel

On 18–19 April 1998, a second summit of the Americas took place in Santiago, Chile. Attended by the heads of state of thirty-four American states,[1] it followed the first summit of the Americas, convened by the United States, in Miami in December 1994. The Santiago agenda included issues such as education, drugs, combating poverty and organized crime, but it was the announcement that the heads of state were ready to start negotiations for a Free Trade Area of the Americas (FTAA) that received most attention.

The proposal to negotiate an FTAA was first put forward by US Vice-President Al Gore during a speech in Mexico City in December 1993. More than four years later, in March 1998, after intense debate, high-level diplomacy and numerous technical meetings, a consensus document on the format of an FTAA was approved in a meeting of ministers of trade in San José in Costa Rica. This document formed the basis on which the heads of state of the Americas were able to announce in Santiago a detailed plan of action to conclude negotiations for an FTAA no later than 2005.

Ideas, proposals and plans to stimulate trade and investment, and foster economic links, among the countries of the Americas are certainly not new. There were several attempts in the past to encourage economic integration among the 'American family of nations', but by and large they failed to go beyond the intentions of political leaders and catch the imagination of their civil societies.[2] Initiatives to foster economic links in the Americas—from measures to facilitate trade and investment to ambitious schemes for regional economic integration—have been considered many times since the nineteenth century. Immediately after independence, unsuccessful attempts were made by Spanish American leaders to create economic and political unions of the recently created republics; by the end of the century a pan-American initiative led by the United States had failed to stimulate significant regional commerce; and more recently, several subregional groupings were formed, when a number of Latin American and Caribbean countries developed formulae to foster economic integration excluding the United States. Yet despite all these initiatives and a moderate success achieved in recent decades, it was only in the 1990s that subregional economic integration became a significant way of fostering trade and investment among the countries of the Americas[3]. Regional and subregional trade and trade-related agreements are a conspicuous trait of the current international economy, and one of the most heatedly debated economic issues of the decade.[4] However, given the past record of the Americas in this area, the sheer number of nations involved in

the proposal led observers to respond to Vice-President Gore's announcement with some scepticism. If it is successfully concluded, the free trade area will include all the nations of the Americas with the exception of Cuba, which was expelled from the Organization of American States (OAS) in 1962, and therefore does not belong to the 'American family of nations'. The geographical area will extend from Alaska to Tierra del Fuego, with a population of around 730 million people, a combined GDP approaching US$10 trillion, and total exports of more than U$ l trillion (1997 data). An FTAA would become a formidable regional grouping and arguably the largest regional economic grouping in the world.

One should not take for granted the notion that the Americas is anything other than a geographical definition. The thirty-four (or thirty-five with Cuba) nations of the Americas certainly share a continent (or the western hemisphere), but it is one that embraces a very heterogeneous 'family of nations'. From the largest economy in the world to a number of micro-states in the Caribbean, they have in common their colonial European past and a forging of nationhood by a combination of indigenous populations and descendants of European and Asian immigrants and African slaves. Inter-American relations in the twentieth century have been characterized by the disparity of economic power between the United States on the one hand and thirty-four nations of very different sizes, shapes, economic clout and cultural background on the other. The United States, with around 35% of the Americas' population, accounts for 76% of the total GDP, and 73% of total industrial output. Brazil, the second largest country in the Americas, with about 21% of the total population, is responsible for only 7.5% of GDP and 10% of industrial output.

These numbers show that the greatest economic attraction in the Americas is the sheer size of the US market. In theory, then, all the countries of the Americas should be equally interested in gaining free access to the US market. In fact, the ratio of interregional trade varies significantly among North, South and Central America and the Caribbean. In North America, that is Mexico and Canada, more than 80% of total trade is with the United States, while in Central America and the Caribbean the proportion is on average 60%. At the other end of the scale are the countries of South America: in the southern cone, trade with the United States makes up just over 20% of total trade.

The Americas as a whole are quite diverse in the geographical distribution of foreign trade and therefore should not be perceived as a single 'natural' region. Moreover, trade negotiations are very complex and time consuming, requiring skilful and technically well-prepared negotiators, a resource not possessed by most of the thirty-four nations. Trade negotiations also involve bargaining and concessions that will affect well-organized and entrenched interests within all the countries involved, and a free trade area, if and when implemented, will have an unknown impact on the economies and societies of the participating countries. Given these circumstances, it may seem surprising that most of the leaders were so eager to embrace the proposal for a free trade area, and this enthusiasm can only indicate the scale of changing global, regional and national circumstances.

Global factors

The end of the Cold War was bound to inspire the United States to take some sort of new political initiative towards Latin America and the Caribbean. During the period defined by the East—West confrontation, Latin America and the Caribbean did not figure prominently in Washington's interests. Relations with these countries were perceived in terms of gains and losses in Washington's overall competition with its main rival, the Soviet Union. US attention to the area was therefore based principally on security concerns, as reflected, for example, in its support for authoritarian regimes as well as its several interventions in the domestic affairs of Guatemala, Cuba, Chile, Nicaragua, El Salvador, Panama and Grenada, among others.

This pattern of inter-American relations, with security taking priority over development, pervaded the whole Cold War period. It certainly created resentment among Latin American and Caribbean leaders, who could see the contrast between the United States' economic engagement in Europe and Asia, and its apparent neglect of the economic plight of their region. When the United States initiated a project that had economic prosperity as its main goal—the Alliance for Progress during the Kennedy administration—it was short lived, lacking continuity and easily subverted by other priorities.

The dramatic change in the international scene after the demise of the Soviet Union, and the reaffirmation of the international leadership of the United States, created the conditions for the launching of a new economic policy towards Latin America and the Caribbean. This took the form of a proposed series of initiatives to stimulate trade and investment, and to deal with the foreign debt crisis, the most urgent economic problem in Latin America and the Caribbean in the late 1980s. The plan was announced by President Bush in 1990 under the name of the Enterprise for the Americas Initiative.

Regional factors

A more optimistic climate was created in the region once the Latin American countries were able to deal with the main factor responsible for their dreadful economic performance for most of the 1980s, the so-called 'lost decade'. Starting with the Mexican debt default of September 1982, the area suffered its worse economic downturn since the 1930s, and much needed resources were sent abroad to pay debts incurred during the boom years of the 1970s. Furthermore, the debt crisis forced economic authorities in most countries to close further their already inaccessible economies in an effort to save hard currency and repay the spiralling costs of servicing foreign debt. As a result, in most countries of the area, the 1980s was a decade of sluggish economic growth, deteriorating living standards, high rates of inflation (even hyperinflation in some countries), and a last attempt to protect their economies from foreign competition. Economic policies that had served the area reasonably well for some decades—import substitution, industrialization and extensive state intervention in economic affairs—finally collapsed under zero growth, fiscal crisis and hyperinflation.

Some countries realized sooner than others that the economic model which had prevailed for so long had collapsed, and started unilaterally implementing policies to open up their economies to foreign trade and investment and to stimulate export-led growth. From the mid-1980s Chile, followed by Mexico, pioneered new trade policies, drastically reducing tariff and non-tariff barriers to trade, and stimulating competition and foreign investment. These market-oriented measures would eventually be followed by every Latin American and Caribbean country.[5] The opening up of their economies, the end of policies favouring import substitution and of the bias against exports eventually forged a new climate for economic prosperity as the area followed the guidance of a series of market-orientated reforms which became known as the Washington Consensus. These reforms, which went beyond economic management to include other areas of public policy, contributed to a more market-friendly atmosphere in the area, closing the period of 'defensive nationalism' that had for so long characterized Latin American and Caribbean cultural, political and economic relations with the United States.[6]

Another important feature of the regional environment of the 1990s was the establishment (or relaunch) of schemes for subregional economic integration throughout North, Central and South America and the Caribbean. Latin America and the Caribbean had already gained quite substantial experience in subregional economic integration with the formation in the 1960s of the Central American Common Market, the Latin American Free Trade Association and the Andean Pact. However, in spite of their good intentions, these did not contribute to significantly expanded trade, investment and economic integration.

A new era of economic integration in the Americas started with the conclusion in 1988 and the entering into force in 1989 of the Canada—US Free Trade Agreement. This marked a turn away from the policy previously favoured in Washington of favouring multinational over regional or bilateral trade agreements as a result of changing perceptions among US trade policy authorities about the respective roles of multilateralism, bilateralism and unilateralism in US trade policy making. The United States had been the champion of multilateral negotiations to liberalize trade since 1945, but as the multilateral negotiations conducted at the Uruguay Round of talks under GATT seemed to be going nowhere, a bilateral agreement with Canada was perceived as a way to foster business links with Canada. In most areas Canada was already the United States' main trade partner, so a free trade agreement between the two countries would serve to stimulate still further existing trade and investment connections. From the Canadian point of view, it would boost exports to the United States and US investment in Canada.

The Canada-US Free Trade Agreement having been concluded, Mexico promptly entered the picture. Mexico was already revising its economic and trade policies, opening up a previously closed economy, a process which included becoming a member of GATT. In 1990, President Carlos Salinas proposed a free trade agreement with the United States—reflecting, among other factors, a historical shift in Mexico's relations with its powerful northern neighbour. President Bush accepted President Salinas's proposal, and, with Canada, the two states formed the North American Free

Trade Agreement (NAFTA) in 1992. After a fierce debate, NAFTA was finally approved by Congress in the following year and entered into force on 1 January 1994.

Meanwhile, in Latin America and the Caribbean, old schemes for subregional integration were being relaunched and new ones formed. The most significant new initiative was the establishment of the Common Market of the South (Mercado Comun del Sur, or Mercosur), which was set up in 1991 by the Treaty of Asuncion. Mercosur resulted from initiatives taken jointly since 1985 by Argentina and Brazil, aiming to improve their bilateral relations after decades of suspicion and rivalry. After the conclusion of a series of bilateral agreements, Argentina and Brazil invited Uruguay and Paraguay to join them and a new scheme for economic integration was created. Since 1 January 1995, Mercosur has been a very successful customs union. Trade between its partners has multiplied five times since 1990, and Brazil has become the most important trading partner of Argentina, while the latter is the second most important Brazilian trading partner.

Other examples of economic integration currently in force in Latin America and the Caribbean are the Group of Three (Mexico, Colombia and Venezuela); a relaunched Central American Common Market; the Andean Community (previously the Andean Pact); and a strengthened Caribbean Community and Common Market (CARICOM). In addition, a series of bilateral free trade agreements concluded in recent years has had quite a substantial effect in boosting trade and investment between many Latin American countries.

Domestic factors

The most important change in this period in almost all the nations of Central and South America and the Caribbean was the emergence of leaders more willing to embrace economic co-operation and in favour of expanding foreign trade and investment. In addition, the transition to and consolidation of civilian rule and democracy was a powerful drive in changing their attitude towards the United States. Furthermore, with few remaining exceptions, old territorial rivalries were, or are in the process of being, resolved, and leaders of different political persuasions seem convinced of the need to move forward in order to deepen political and economic co-operation.

A change of direction was also taking place in North America. Canada, for so long a reluctant player in inter-American affairs, joined the OAS in 1992, and began improving its economic and political links with Latin America and the Caribbean. The United States began to take a more pragmatic approach to its southern neighbours. The opening up of the economies in Latin America and the Caribbean contributed to a more benign perception of the opportunities for trade and investment within the Americas. Particularly after the election of President Clinton, with the importance given to trade policies by his administration, the United States was much more attuned to business opportunities in the Americas. Canada and Mexico are respectively the United States' largest and second largest trade partners, and the boom in US exports to South America over the past five years has put the area firmly in the

strategic, long-term vision of US trade and investment interests. In contrast to its trade deficit with Asia and its stagnant trade with Europe, interregional trade has boomed and the United States has a substantial trade surplus with Latin America. Furthermore, it exports to the area products of high-value-added content such as capital goods and machinery.

In sum, after decades of being perceived as a land of opportunity but besieged by intractable economic, political and social problems, Latin America and the Caribbean began to be seen as an area of enormous opportunities by US business. This more pragmatic approach, initiated by President Bush and continued by President Clinton, made trade and investment, instead of aid, the name of the game in a new era of inter-American relations.

These seem to be the main global, regional and domestic factors that contributed to turn the Americas into a region much more receptive than formerly to the idea of fostering economic links. Nevertheless, a history of unsuccessful attempts, and the difficulties of implementing agreements, made analysts sceptical about the real commitment of the American nations. It is therefore necessary to turn to the negotiating process itself, and look into the dynamic created and the mechanism devised in order to move the process forward. The way to conclude an FTAA was thought to be to lock the proposal in an irreversible dynamic of negotiations and achievements.

The beginning: the Miami Summit

President Bush announced his Enterprise for the Americas Initiative (EAI) in June 1990, prior to a visit to Latin America. The initiative consisted of a plan for foreign debt relief and the promotion of foreign investment, along with the Inter-American Development Bank (IDB) and a free trade component. The free trade aspect of the EAI languished and, despite the rhetoric about a partnership for a new era of prosperity, the only moderate tangible result was the debt relief plan, which succeeded in developing imaginative ways to address the debt crisis.[7] On matters of trade and investment, NAFTA absorbed all the energies of the Bush administration.

Congressional approval and the entering into force of NAFTA, which required the personal involvement of President Clinton and Vice-President Gore, raised great expectations throughout the area, and it was in this atmosphere that Gore announced the administration's intention to hold a summit of all the republics of the Americas, the intervention of the United States being to seek to broaden the scope of the EAI and NAFTA.

The first summit of the Americas took place in December 1994 in Miami. Prior to the summit, the US government circulated a draft document to its Latin American and Caribbean partners containing its main proposals. After contentious rounds of talks, a consensus document was approved, known as the Airlie House Agreement, which reflected the views of all the main players.[8] The centrepiece of the document was a commitment to conclude negotiations on a free trade area of the Americas no later than 2005. It was a declaration of intent that was warmly received by most, but

not all, leaders of the Americas. Those concerned with gaining better access to the US market were pleased by what was then perceived as an extension of NAFTA, but others were nervous of the possibility that an FTAA would become a reality.

Perhaps the most important aspect of the Miami Summit was that, for the first time after a declaration of such ambition, a mechanism to follow up and implement the agreement was established. In contrast to what had happened so often in the past, momentum was not lost after the end of a heads of state meeting. In this case, a concrete goal, with a timeframe and commonly agreed procedures, was created to ensure forward movement.

The negotiating process after Miami

The main document signed by the presidents in Miami contained a declaration of principles and a plan of action. A few months later, in June 1995, a first meeting of trade ministers took place in Denver. There, twelve working groups at vice-ministerial level were set up, each one chaired by a different country, to discuss each topic of the agreement in great detail and to prepare background technical information. From Colorado to San Jose, the working groups met nine times, and succeeded in generating inventories from every nation involved and amassing a great amount of information about various aspects of trade and trade-related issues.

It is interesting to note that the main objective of the negotiating process is to achieve a free trade area, but under US pressure it intends to go beyond the traditional issues of removing tariff and non-tariff barriers. According to the US vision, it should include such issues as services, investment, competition, intellectual property and government procurement. Hence, from the standpoint of the United States, the negotiations being conducted in the Americas are more far reaching than those conducted at multilateral level—that is, the FTAA agenda is GATT-plus; some observers take the view that this was a clever strategy devised by US trade policy makers to move the agenda of the multilateral trade negotiations forward.[9]

Another novelty of Miami was the creation of a tripartite commission, consisting of the OAS, the IDB and the United Nations Economic Commission for Latin America and the Caribbean (ECLAC). Here it appears that the main objectives were to use the resources and technical expertise developed by the IDB and ECLAC as well as revitalizing the role played by the OAS in inter-American affairs. A trade unit of the OAS was set up in 1995 and, despite the bad image of the OAS as a Washington-led organization, its participation in this initiative was sought as a way of giving it a new lease of life.[10]

Four meetings of trade ministers have taken place since Miami (in Denver, Cartagena, Belo Horizonte and San José), preceded by several meetings of vice-ministers, where the agenda was set and the main differences discussed. In Belo Horizonte, in May 1997, a first draft document was produced and the decision taken to convey a second summit of the Americas.

As expected, disputes occurred constantly during these negotiations, only the most relevant of which are mentioned here. First, there were different perceptions of how

a free trade area should come about. The initial US view, which persisted until very recently, was that an FTAA would be a gradual extension of NAFTA to the other Latin American and Caribbean countries.[11] At the Miami Summit, Chile was formally invited to be the next country to join NAFTA, while other nations such as Argentina were mentioned as next in line. Opponents of this approach, led by Brazil, argued that an FTAA should not be an extension of trade preferences granted unilaterally by the United States to well-behaved countries, but a truly new initiative, negotiated by equal partners. Eventually, this dispute was resolved with acceptance of the approach advocated by Brazil.

A second and related issue concerned disagreement on the role of the existing subregional groupings in the negotiating process. The United States argued that countries should negotiate individually, while other members, Brazil in particular, argued in favour of a 'building block' approach: that is, that subregional groupings such as the Andean Community, Mercosur or the Central American Common Market could, if they wished, speak as one voice during the negotiations. In the end, the view prevailed that each country would be allowed to choose how it wish to be represented. Some, such as the United States, Canada and Mexico, opted to do so individually, while others, such as the members of Mercosur, opted to negotiate as a group.

A third cause of friction related to the way the free trade area should enter into force. Some countries favoured the idea that agreements should be progressively implemented as soon as they were concluded. Other countries favoured the idea, by and large agreed in Miami, of a 'single undertaking': that is, that all the agreements would enter into force at the same time, when all the negotiations had been concluded. The latter vision prevailed.

An additional source of friction came from the fact that some countries wished to aim to end the negotiations by the year 2000 rather than 2005. The original timetable prevailed, although with an addendum stating that efforts will be made to achieve concrete results by the end of the century.

The final step: San José, Costa Rica

The meeting of trade ministers held in San José on 19 March 1998 was the last chance to achieve a compromise and bring a consensus document to Santiago. Perhaps unexpectedly, a consensus document was approved. All the remaining disagreements about dates, venues and methods of bringing the agreements into force were resolved, allowing the document to receive political sanction from the heads of state in Santiago. What follows is a brief description of the main points agreed upon in San José regarding the format of the negotiations to take place from May 1998 until 2005.

The main body that will direct negotiations is a trade negotiating committee, composed of the vice-ministers of trade of the thirty-four nations. The committee will be responsible for the work of nine negotiating groups, chaired by different countries, on the following areas: market access; investment; services; government procurement; dispute settlement; agriculture; intellectual property rights, subsidies;

anti-dumping and countervailing duties; and competition policy. The negotiations will take place in Miami, Panama City and Mexico City and will be chaired by Canada, Argentina and Ecuador, and in the last stage co-chaired by Brazil and the United States. In addition, a consultative group on smaller economies will be attached to the trade negotiating committee.[12] The Tripartite Committee—IDB, OAS, ECLAC—will continue giving technical support to the FTAA process as well as technical assistance to subregional groupings and individual countries.

Two main aspects of the negotiation to date stand out. First, in spite of the unequal partnership between the United States and the other members it was a negotiation if not between equals at least between less unequal partners, with the United States unable to impose its view on most of the competing issues. Second, Brazil stood out as the main interlocutor of the United States. Owing to its sheer size and economic might, as well as diplomatic skills, Brazil was able to galvanize support from its Mercosur partners and from other South American countries to confront US views.

Since Miami, it seems accurate to describe Brazil, perhaps alongside Mexico, as the least enthusiastic among the Latin American and Caribbean countries to press ahead with the proposal for an FTAA. After all, as the second largest economy in the Americas it has more than most others to lose when a free trade area is completed.[13] Nevertheless, when the process moved ahead, Brasilia did not want to be seen as a block against progress in the negotiations. However, its cautious approach and status as main challenger to the United States enabled it to impose its view on many contentious points, resulting in a view which represented at least a common position from Mercosur. Perhaps the most important gain for Brazil's foreign policy was that it achieved the status of a truly important player in inter-American affairs.

Remaining obstacles for a successful FTAA after 2005

Lack of 'fast-track' authority in the United States

Since the 1970s, the President of the United States has been granted a special authority by Congress to negotiate trade agreements. Under this authority, Congress can either approve or reject a trade agreement but cannot amend it. This legislation is known as 'fast-track' authority. The legislation granting this authority has expired, and to enable new trade agreements to be negotiated, President Clinton submitted a renewal bill to Congress in September 1997.[14] However, concluding that the bill would not be approved, he decided to withdraw the legislation on the eve of voting.

Several possible motives for Congressional reluctance to renew the authority of the President have been identified. Among them are the rise of protectionism among US legislators, in particular among members of Clinton's own Democratic Party; the mood in Congress after the last legislative election, which elected a substantial number of fresh Congressmen and women not committed to new trade agreements; the role played by organized labour and environmental groups in lobbying and persuading members of Congress against renewing the authority; and the belated and

weak strategy pursued by the executive to persuade enough members, in particular from the Democratic Party, to support the bill.

In addition to these, another factor is the bad image of NAFTA among the US Congress and US public opinion. In spite of data showing that NAFTA has produced good results, both increasing exports to Canada and Mexico and creating new jobs, the mood has turned definitively against NAFTA.[15] This fact seems to me the single most important reason for the lack of support for granting the President 'fast-track' authority, despite the argument that this is an essential piece of legislation to enable the United States to undertake new trade agreements and maintain the exceptional record of economic growth and job creation recently achieved.

Congress also defeated a fourth attempt by the executive to pass legislation granting members of the Caribbean Basin Initiative similar trade preferences, in some products, to those granted to Mexico under NAFTA. The NAFTA parity bill was defeated by a substantial majority, suggesting that President Clinton is unlikely to be able to renew the authority during his remaining period in office. As a consequence, his successor will inherit the task. Without the renewal of 'fast-track' authority, a free trade area may not come into force, because the Latin American and Caribbean partners are well aware of the power of the US Congress to block or amend international trade agreements.

Free trade areas versus multilateral negotiations

There is no consensus among economists on the role played by regional trade agreements in economic growth,[16] or on whether these initiatives work towards the ultimate goal of a free trade world.[17] Meanwhile, after the successful conclu-sion of the Uruguay Round of GATT, and the setting up in 1995 of the World Trade Organization (WTO), proposals have been put forward to proceed with another multilateral round of talks to liberalize trade further.

It has been suggested that this proposed new round—a Millennium Round—of talks should address topics including the rules governing contentious issues such as agriculture, investment, services and government procurement, among other themes. Moreover, many developing countries have liberalized their trade policies and become committed to free and fair trade,[18] a trend which could itself advance the process towards further liberalization. At present, it remains to be seen if, when and how such new talks will take place. Nevertheless, if a new round of talks does begin, it might absorb all the energy of participants in the short term and make regional negotiations for free trade redundant.

A reversal in economic and political fortunes in Latin America

A third factor which could disrupt the process of creating an FTAA relates to the possible reversal of current trends of political and economic openness in Latin America and the Caribbean. The alleged reason for the exclusion of Cuba from the process is the undemocratic nature of its regime. Therefore, it is plausible to argue that a return to

authoritarian rule in any other country could eventually lead to its exclusion from the negotiations.

It is not my intention here to speculate about the prospect of political reversal in Latin America, but it is important to remember that despite the progress made in consolidating democratic rule, and the lack of alternative competing ideologies, some countries still lack the vitality of a robust civil society, as well as the solidity of institutions, that would make a return to authoritarian rule impossible.

Another challenge would be a return to protectionism as a result of economic or financial turmoil. Two recent events—the Mexican peso crisis of December 1994-January 1995 and the financial turmoil in some East Asian countries since July 1997—have shown that emerging markets are not immune from the excessive deregulation of the international financial markets. An important component of the reformed economies of Latin America and the Caribbean has been deregulation of domestic financial markets as well as a return to the international capital market. A series of macro-economic measures was implemented in order to boost the confidence of foreign investors, but the two financial crises in the last four years have shaken investor confidence in emerging markets. Despite the fact that some Latin American countries reacted very rapidly to these events, taking measures to buttress investors' confidence, there is a risk that the strategy of opening up the area to a more market-orientated approach could suffer in any new financial turmoil. Even with the constraints imposed by the WTO in force, a third serious financial or balance of payments crisis could in theory re-establish policies favouring more restricted access to domestic markets, which would derail, or at least complicate, negotiations to achieve an FTAA on time.

Conclusion

The proposal for an FTAA was born out of a quite unique set of circumstances: the end of an era of confrontation in international affairs and the transition towards another where trade and economic links seemed the right way towards peace and prosperity; a move towards regional economic integration; a regional climate conducive to economic openness, trade and foreign investment as legitimate tools to development, after the exhaustion of decades of closed economies; and a new political climate among democratically elected leaders of the Americas. These factors have persuaded reluctant leaders that a new vision of development, relying much more than in the recent past on robust civil societies and a market-orientated economy, is a vital precondition for prosperity. Indeed, for the first time ever in negotiations for a common inter-American project, business and labour associations participated intensively in the debates, and it appears that their participation reflected the mobilization of organized sectors of the civil society. In sum, what could have been empty rhetoric became serious negotiations, in turn requiring that many countries of the area develop the necessary expertise to deal with matters of such complexity.

The United States initiated the proposal for an FTAA and conducted the negotiations, even though not every country in the Americas—Brazil in particular

having reservations—perceived a free trade area as serving its best interests. After the first summit of the Americas in Miami, and the evolving negotiations that followed, it seemed that a free trade area had became *a fait accompli,* but public opinion in the United States has since grown much more doubtful about engaging in further trade agreements, as reflected in President Clinton's unsuccessful attempt to renew 'fast-track' legislation. Moreover, despite all the evidence to the contrary, NAFTA has been criticized for supposedly granting excessive benefits to the United States' trade partners.

Meanwhile, several countries in Latin America did not sit still while the negotiations were taking place. Several initiatives have been taken by Latin American countries to develop stronger economic links with extraregional partners. Mercosur, Chile and Mexico have in recent years concluded agreements with the European Union with the aim of strengthening their trade and investment relations, including the goal of establishing free trade agreements. Caribbean countries, Central America and the Andean Community are also seeking to reinforce their economic and political links with the European Union. If it is successfully completed by 2005, an FTAA will most probably require a transitional period of ten or fifteen years to become fully operational, that is with zero tariffs and no non-tariff barriers imposed on trade among its members. Every trade agreement needs a period of adjustment to new rules. This seems a reasonable period of time to prepare all the countries involved to reap the benefits of free trade.

Notes

1 The thirty-four countries are: Antigua and Barbuda, Argentina, Bahamas, Barbados, Belize, Bolivia, Brazil, Canada, Chile, Colombia, Costa Rica, Dominica, Dominican Republic, Ecuador, El Salvador, Grenada, Guatemala, Guyana, Haiti, Honduras, Jamaica, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay, St Kitts and Nevis, St Lucia, St Vincent and the Grenadines, Suriname, Trinidad and Tobago, United States and Venezuela.

2 Sidney Weintraub (ed..), *The Annals of the American Academy of Political and Social Science. Free Trade in the Western Hemisphere* (Special number), 526, March 1993.

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