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**Research Report**

## The world trading system after Cancún, or: How the rhetoric of the development round rebounded on the industrialized countries...

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## The World Trading System after Cancún, or: How the rhetoric of the development round rebounded on the industrialized countries...

- *International trade increases worldwide growth and improves the chances of successful poverty reduction. A development round could reinforce this potential.*
- *Development scholars largely agree on what would constitute a development round: improved market access for developing countries, no negotiations on investment and competition rules in the current round, additional support for developing countries in the field of trade-related capacity-building. In contrast to their own rhetoric, however, trade policy makers in industrialized countries do not feel obliged by this consensus. It is therefore they who bear the main responsibility for the failure of Cancún.*
- *In Cancún the developing countries successfully presented themselves as an articulate group with the potential to block multilateral trade negotiations. It remains to be seen whether they will use their new-won scopes of action to take a hand in constructively shaping the world trading system. This will depend largely on newly industrializing countries (NICs) and anchor countries like India, China, or Brazil.*
- *The conference's failure does not mean a success for developing countries since they failed to achieve their trade-policy goals. What remains is the hope that the shock of Cancún will lead to a greater willingness to compromise, above all on the part of the industrialized countries, but also on the part of NICs and anchor countries, with a view to giving the WTO a more development-friendly shape. If this fails, the multilateral trading system would be in serious trouble.*

The new world trade round was to be a development round – and now, thanks to the resistance put up by many developing countries in Cancún, the round has reached a deadlock. Those most loudly bewailing this fact are the trade policy makers from the North, who had previously dubbed the Doha Round a "development round". In the statements made by many governments of industrialized countries as well as in large parts of the media, it was claimed that the developing countries had missed a major chance. It is, though, often overlooked that what the developing countries rejected was less the development round per se than a new trade round based in essence on the notions of the industrialized countries. True, it is still uncertain whether the developing countries, buoyed by their newly kindled spirit of contradiction, will manage to gain additional concessions from the industrialized countries or whether, in the final outcome, they will end up empty-handed. But there were good reasons for the stance they took in Cancún.

### What would constitute a development round?

A "true development round" would provide a positive impulse for worldwide growth, poverty reduction in developing countries, and the continued existence of a rule-based world trading regime. Among many scholars, development-policy institutions, and moderate nongovernmental organizations (NGOs), there is a surprising measure of consensus on some of the central elements of a development round:

- The industrialized countries would have to cut their agricultural subsidies, which currently add up to some US\$ 300 billion per year. What these subsidies and a lack of open markets mean for developing countries is a loss of potential export revenues amounting to an estimated US\$ 40 billion (to compare: taken together, official development assistance comes to roughly US\$ 50 billion per year).

- It would be essential to improve market access for nonagricultural, labor-intensive products from developing countries, among other things by lowering tariff peaks and tariff escalation (tariffs that rise in accordance with processing stage). For many developing countries, liberalization of temporary labor migration could also mean higher export earnings in their trade in services.
- The so-called Singapore Issues should not be on the agenda of the development round. Singapore Issues is a term used to refer to negotiations on foreign direct investment, competition, transparency in government procurement, and trade facilitation. The only one of these issues not under dispute is trade facilitation, which is about reducing transaction costs and red tape in customs administrations. The main argument against placing the other issues on the agenda is that they would serve to expand the WTO agenda before the "old" market-access problems have been solved. The Singapore Issues should for this reason be adjourned until the current round has been concluded.
- It would be important to agree to provide developing countries additional support in trade-related capacity-building as a means of fostering their integration in the world economy and their ability to assert their rights in the WTO.

A development round of this kind is part of the Monterrey consensus on international development policy: while, according to the consensus, all countries are themselves primarily responsible for their own economic development, international trade policy has to provide a development-friendly framework geared to supporting the effects of the national policies pursued by developing countries. The heads of state and government attending the UN conference in Monterrey committed themselves to this objective. In Cancún the trade policies of the EU and the US were far removed from the Monterrey consensus.

## The road from Doha to Cancún

At the WTO ministerial conference in Doha, in November 2001, member countries launched a new round of trade negotiations. Still smarting from the shock of September 11, the US wanted to make a symbolic gesture in favor of multilateralism. The EU sought to win the developing countries for the new trade round by dubbing it a “development round”. Since then, however, the deadlines set have come and gone in all fields under negotiation, without any agreement having been reached on disputed points. The EU, the US, and the developing countries blocked one another on central issues. The Cancún ministerial, at first planned as a stock-taking exercise, was now expected to send out a political signal demonstrating the member countries’ determination to reach a successful conclusion of the development round. In the run-up to Cancún it was not even possible to work out a mutually agreed-upon draft for a ministerial declaration. The chairman of the WTO’s General Council subsequently presented, “in personal responsibility”, a draft which could in his opinion have served as a basis for negotiations. In the preparatory phase for Cancún this draft was harshly criticized by the developing countries for largely reflecting the interests of the industrialized countries.

### Substantive points of contention in Cancún

The Cancún conference was dominated by two issues: agricultural liberalization and the start of negotiations on the Singapore Issues. There were also two other issues of major import on the agenda: subsidies for cotton and nonagricultural market access, while all other points played a subordinate role on the wide-ranging conference agenda.

**Agricultural trade:** Industrialized and developing countries clashed head-on over agricultural issues. Weeks before Cancún the US and the EU had agreed on a compromise linking an offer of moderate cuts in domestic support measures with demands that advanced developing countries further open their markets. In its agriculture section, the chairman’s draft ministerial declaration closely followed this “compromise proposal”, a fact which drew harsh criticism from a group of developing countries. Subsequently, the so-called G-21 was formed, an informal association of developing countries under Brazil’s leadership.\*

The G-21 managed to acquire a certain profile in Cancún as the “voice of the developing nations”. Its clout was underestimated by the industrialized countries. In a sense, the G-21 replaced the Cairns Group, which, including some industrialized countries, had in the past pushed for across-the-board liberalization of agricultural trade. The G-21 now turned into a “South Cairns” which includes protection-minded countries like India. This led to a reshuffle of positions in the sense that it was now primarily the industrialized countries that were expected to liberalize their agricultural markets, with the developing countries asserting their rights to retain certain protectionist measures. With China on board – which here for the first time joined a coalition with the developing countries in the WTO – the group gained additional political weight, a fact underlined by a statement noting that the G-21 represented “more than half of the world’s population”.

As the conference got underway, the G-21 flatly declined to accept the draft ministerial text as a basis for negotiations. Following a sounding-out phase, negotiations did get underway between G-21 and industrialized countries, but without making much headway. The second ministe-

rial draft was still based in essence on the US-EU compromise paper. The standstill on agriculture blocked all of the other areas under negotiation. Once again, liberalization of agricultural trade was to become the stumbling block to international trade negotiations.

**The Singapore Issues:** In parallel to agriculture, another North-South conflict revolved around the start of talks on the Singapore Issues. In Doha it had looked as though the developing countries had abandoned their resistance to their inclusion. Only India had, at the last minute, pushed through a formulation stating that a start of negotiations should be made conditional on an “explicit consensus” at the next ministerial conference. What had at first looked like a diplomatic rearguard action turned out in Cancún, to the surprise of many observers, to be the means needed to rekindle resistance among numerous developing countries. Both a group of 70 developing countries under the leadership of Malaysia and India and the group of African countries came out against the Singapore Issues. The opposing side was made up of the EU (together with Japan and Korea), which worked furiously for talks on all four Singapore Issues, rejecting all requests for an unbundling of the issues. It quickly became clear that the issues of investment and competition were running up against stiff resistance on the part of the developing countries. The US continued to back the EU on the Singapore Issues, but without actively pushing for their inclusion. The US’ focus was on opening markets in advanced developing countries, not on development of new multilateral rules.

The second draft ministerial text excluded competition from the negotiations. However, the even more contentious issue of investment remained, albeit in somewhat hedged language, on the conference agenda. Only during the last night of negotiations did the EU offer to drop investment. This compromise proposal came too late. The fronts had already hardened, and the African countries continued to speak out against the inclusion of any of the Singapore Issues, while Japan and Korea insisted that all four issues be included (presumably with an eye to blocking once and for all any possible progress in the agricultural talks).

**Cotton:** Somewhat surprisingly, just a few months prior to Cancún the cotton initiative launched by four West African countries was placed on the agenda of the ministerial conference. Benin, Mali, Burkina Faso, and Chad called for a decision in Cancún to discontinue all subsidies in the cotton sector by the year 2006. The US provides some US\$ 3 billion per year in subsidies for its 25000 cotton producers – a sum roughly equivalent to the gross national product of Burkina Faso, where two million people are dependent on cotton production. Subsidies in the EU amount to US\$ 0.6 billion. While the EU continued to signal its willingness to negotiate, though without offering any concrete concessions, the US was willing to address the proposal only in the context of the overall negotiations – which meant, in effect, adjourning it indefinitely. Cotton turned out to be Cancún’s symbolic issue, and it is in the cotton sector that the false development-round rhetoric of the industrialized countries was easiest to expose. In fact, the passage on cotton contained in the second draft ministerial text was little more than a diplomatically worded slap in the face: it offered the developing countries prospects of funding, from existing development-cooperation measures, to help diversify their export structures – a cynical proposal in view of the fact that the only reason why the West African cotton producers are not competitive is the cotton subsidies provided in the industrialized countries.

\* Egypt, Argentina, Bolivia, Brazil, Chile, China, Costa Rica, Ecuador, Guatemala, India, Colombia, Cuba, Mexico, Nigeria, Pakistan, Paraguay, Peru, Philippines, South Africa, Thailand, Venezuela.

**Nonagricultural market access:** The actual core of the world trading system was pushed into the shadow of the three first issues named above: negotiations on offers to open markets in all other goods sectors apart from agriculture. Both the US and the EU had a major interest in gaining substantial concessions from the advanced developing countries, which have import barriers far higher than those of the industrialized countries. Due to the standstill on agriculture, these negotiations remained more or less stuck. But here an old polarization began to re-emerge: while the developing countries were long more than reluctant to commit themselves to opening their own markets, they at the same time demanded tariff reductions in the industrialized countries. It is, though, uncertain whether it was mainly for tactical reasons that the developing countries so adamantly refused to make significant concessions here, preferring instead to await developments in the agricultural sector.

### **The role played by nongovernmental organizations (NGOs)**

There is much evidence to support the thesis that the influence of NGOs was stronger in Cancún than at the ministerial conference in Seattle, which also ended in a failure. One reason is that the NGOs have continued to professionalize in substantive and organizational terms over the past few years. Another reason must be sought in the successful formation of tactical alliances between NGOs and governments of developing countries. The shifting emphasis experienced since Seattle from environmental and social standards to negotiations on agricultural trade and investment paved the way for this solidarity process. In Cancún observers noted that together with many developing countries, a large share of NGOs argued on the basis of the development consensus outlined above, sometimes even coming out in favor of further liberalization of world trade. Like other institutions such as the World Bank, NGOs made use of an array of different instruments to influence the outcome of the ministerial: funding of studies, consultations with governments in the South, tapping of media connections in the North. In this way NGOs were instrumental both in ensuring that the industrialized countries would not forget their development-round rhetoric and in backing the developing countries in their resistance to the agenda of the industrialized countries. But this they achieved by means that are a legitimate element of pluralist democracy, and are practiced by other interest groups as well. To this extent, the occasional voices criticizing NGOs for their lack of democratic legitimacy are mistaken.

### **The responsibility for the failure**

There are numerous factors that contributed to the failure of the Cancún conference. On the one hand, there are procedural deficits (inefficient conduct of the negotiations, a premature decision to break off the talks). On the other hand, the – differently grounded – resistance put up by the developing countries to the last draft of the ministerial text prevented the conference from ending with a substantive political statement. However, the main responsibility for the conference's failure lies squarely on the shoulders of the industrialized countries, and here in particular on those of the EU, which, in the first place, and despite its rhetoric, was unwilling to carry its share of the burden of a "genuine" development round and, in the second place, seriously underestimated the resistance of the developing countries.

The problem behind all this was a clash between different action logics and interests: the development-round rhetoric implies that reforms will be launched that are in line with the specific interests of the developing nations. This is a position that abstracts from political and economic

self-interests, assuming in their place a global public interest. It is therefore not by chance that scholars, development-policy institutions (World Bank), and NGOs have little trouble reaching consensus on some issues: they all argue within the (normative) framework of just such a logic.

Negotiations in the WTO, however, do not proceed on this pattern; they instead follow a highly pragmatic political rationale defined by the nations involved, one that takes account of economic special interest groups. In contrast to their development rhetoric, the industrialized countries have adhered to this rationale. This is the only plausible explanation for statements like the one found in an internal EU paper insinuating that a reform of agricultural trade along the lines of the G-21 proposal would "impose the whole burden of adjustment exclusively on developed countries". This would in fact have been one consequence of a development round (although, argued from a normative welfare economist's standpoint, the adjustment would have proven highly beneficial to the industrialized countries themselves, because the agricultural policy to which they subscribe is in fact detrimental to their own interests). But it is the resistance of a home-grown agricultural lobby that continues to prevent any development-oriented reform – an argument that is difficult to swallow for those who are working for the global public good.

In this sense, the development round rhetoric indulged in particular by the EU has rebounded on the Union itself. Another factor working to the detriment of Cancún was that the EU underestimated the resistance of the developing countries to the EU's hard-nosed 'business-as-usual' policy, the outcome being that the compromise proposal on the Singapore Issues simply came too late. Evidently, the European Commission failed to coordinate its foreign, development, and trade policies in such a way as to enable it to adequately perceive the resistance of the developing countries in the run-up to Cancún. In Cancún the EU doggedly nurtured the impression that the developing countries would, in the end, and as they always had in the past, bow to the agenda of the industrialized countries. This proved to be a fallacy.

### **The role played by the developing countries**

Cancún experienced the successful resurgence of an active developing-country block in international trade policy. Many of the demands it pressed for stood squarely on the ground of the Monterrey consensus, and its rejection of the ministerial draft was therefore understandable. But if block formation is not to end up in a Pyrrhic victory, the newly industrializing countries (NICs) and anchor countries (i.e. the countries important for their own region of the world, including e.g. India, China, or Brazil) are going to have to assume greater responsibility for the continued existence of the multilateral trading system. This means, among other things, that they are going to have to be prepared, in their own interest as well as in the interest of the less developed countries, to accept further market-opening commitments. Only under this condition will it be possible to shepherd the development round to a successful conclusion, since otherwise the industrialized countries will lack an important incentive to reach an agreement.

The African countries and the LDCs should be careful not to fall into the trap of presenting themselves as defensive naysayers and making too frequent use of their veto power. In Cancún, for instance, the LDCs addressed the problem of preference erosion. The relative advantage of a market access more preferential than that accorded to advanced developing countries will shrink if agreement is reached on a general reduction of tariffs. This made the LDCs less disposed to engage in constructive negotia-

tions. As understandable as this position may be for the short term, the LDCs are here running the risk of becoming even more dependent on preferential agreements of doubtful effectiveness. Furthermore, the LDCs are also in danger of further isolating themselves from the other developing countries and thus finding themselves even more marginalized in political and economic terms than they already are. For the future, it would make more sense to address the real supply-side problems of LDCs with additional development cooperation than to allow them to fall into the role of the unloved heel-draggers of the world trading system.

### The future of the multilateral trading system

The failure of the WTO ministerial conference in Cancún cannot be regarded as a success. It would have been a success if the attending heads of government and state had committed themselves to a genuine development round geared to boosting worldwide growth and promoting poverty reduction. And the consequences of Cancún? The conference could influence the multilateral trading system in at least three directions: (1) a more marked inclination of the industrialized countries to seek bilateral and regional trade agreements; (2) development of a “two-tiered” multilateral trading system; (3) promotion of a new spirit of compromise on the part of industrialized countries and NICs, linked with procedural reforms of the WTO.

Most observers fear that international trade policy may now be headed more in the direction of **bilateral and regional agreements**, as announced immediately after the conference by the US trade representative. Just a few days after Cancún, for instance, Colombia and Peru left the G-21 to enter into bilateral trade talks with the US. A large number of trade blocks would raise the transaction costs of world trade, for one thing because of the complicated rules of origin involved, and would tend to erode the multilateral trading system. Since developing countries are in most cases accorded even fewer concessions in bilateral talks with the powerful industrialized countries than they can expect from multilateral negotiations conducted in the framework of the WTO, they could, in the end, turn out to be the losers. In the short term, though, it is more or less unlikely that the industrialized countries will succeed in concluding bilateral agreements with NICs and anchor countries, because the substantive points under dispute will not change that way either. Seen in these terms, the industrialized countries’ nod in the direction of a supposedly more favorable bilateralism must be seen, at least in part, as a shift in their own political rhetoric: from the carrot (of the development round) to the stick (of a possible erosion of multilateralism). Developing countries are now faced with the bitter question of whether to save multilateralism by consenting to a compromise unfavorable to them.

One further consequence of Cancún could be that the WTO member states will again depart from the principle of the single undertaking, a move that would give rise to a **“two-tiered” world trading system**. Not unlike the Tokyo Round under the old GATT, some agreements – on investment, for instance, – would then be signed only by the advanced member states. The two-speed principle could also be applied for talks on market access, where it was practiced as special and different treatment in the

past: with the big trading powers negotiating tariff reductions among one another, passing them along to other-WTO members in the guise of most-favored-nation treatment, and losing no sleep over whether the LDCs themselves lower their tariffs. This scenario is not without its pitfalls for LDCs: aside from the fact that, according to economic theory, all countries harm primarily themselves by imposing customs tariffs, under this scenario such countries would at the same time lose any possibilities to influence the further development of the multilateral trade rules. Compared with a further fragmentation of the world into regional trading blocks, this scenario would at least offer the one advantage of preserving the multilateral trading system.

The most desirable, and at the same time most unlikely, consequence of Cancún could be that industrialized countries and NICs alike will step back, take a hard look at their common interests, and start to work on building a **greater willingness to compromise**. The cooling-off period dictated by the failure of Cancún would now have to be used to reform the WTO’s decision-making structures (a more independent and stronger WTO Secretariat, transparent decision-making procedures) and to sound out potential fields for compromise. In substantive terms, the industrialized countries should above all make additional concessions on agricultural trade and further open their markets to nonagricultural products, while, in return, the NICs should be prepared to offer facilitated terms of access to their markets – including for labor-intensive products from LDCs. As far as the Singapore Issues are concerned, only transparency in government procurement and trade facilitation would be placed on the agenda. This scenario would call for the industrialized countries to dampen the influence of economic special interest groups on their national trade policies. NICs and anchor countries would have to succeed in developing from a blockade power into a creative force for change.



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