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Making Trade Multilateralism Work for All: The Role of WTO Accessions

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Abstract

Trade multilateralism, i.e. global trade based on negotiated and agreed rules by the World Trade Organization (WTO) membership, faces various challenges. Slow economic growth, changes in the balance of global economic power and inequitable distribution of growth benefits have called into question the benefits of globalization and the rules-based global order. Trade has been the target of a barrage of corrosive criticism from many quarters and has become a lightning rod for policy failures, weaknesses in international cooperation and the adverse effects of rapid technological advances on jobs and incomes. The return of ultra-nationalism, populism, mercantilism, bilateralism and protectionism in several countries has also increased the pressure on trade multilateralism. In this tortuous and uncertain environment, concerted policy actions along several strategic axes are needed to put trade back on track and make trade multilateralism equitable once again. First, trade multilateralism must be used as a tool to restart global economic growth and job creation, while managing uncertainty and risks. Second, it must become more inclusive by encompassing bilateralism and regionalism, leveraging technology and supporting domestic structural reforms. Third, the new realities of the twenty-first century compel an upgrade of the multilateral trading system by the building of its upper floors[1] *on the foundation of the existing trade rules and accumulated* acquis *and expertise. Such a system would preserve the fundamental set of rules at the core of the multilateral system, abolish or revise obsolete rules, which have not stood the test of time, and adopt new rules that would reflect new realities. Fourth, accessions to the WTO are arguably the most vibrant component of the multilateral trading system and have already made important contributions to each of these policy directions. An updated and robust, rules-based multilateral framework, anchored in the WTO, remains indispensable to maximize the benefits of global economic integration and to ensure a stable global economic order.*

Trade Multilateralism in the Age of Ultra-Nationalism, Populism, Mercantilism, Bilateralism and Protectionism

Trade multilateralism has been under stress following the radical transformation of the global environment in recent years. Political developments have revealed a fraying consensus on the benefits of international economic cooperation. Nationalism has manifested itself in the resurgence of protectionism. In addition, populist anti-globalization backlash, as exemplified by Brexit, the 'permanent' withdrawal by the United States from the Trans-Pacific Partnership Agreement and its intentions to revisit the North American Free Trade Agreement, have undermined the international mobility of goods, services and people. The resurgence of mercantilism, attempts to gain advantage through protectionism, and to substitute, rather than to complement, multilateral agreements with bilateral trade deals have put in question the entire post-war multilateral trade architecture and its applicability to new international realities.

The international economic environment has not been particularly helpful in allaying these negative sentiments about trade multilateralism. After several years of lacklustre performance, however, economic activity is projected to accelerate in the medium term, especially in emerging markets and developing economies. Nevertheless, there is substantial uncertainty around these projections, given the yet to be clarified global policy stance of the United States and its international repercussions.

Insufficient global economic growth has led to a worldwide search for those responsible, and trade was quickly identified as the first culprit. As a result, political support for freer international trade has weakened, especially in advanced market economies. Although resistance to free trade has been observed in the past, recently the opposition to trade has gathered strength and become more vocal than in the past. The main trigger for this has been the perception that the benefits of free trade have not been shared evenly among countries and among their citizens. While some have gained, many have lost out. The result has been heightened income inequality, lower welfare and disrupted lives.

Ultra-nationalism has found a fertile ground in the understandable discontent at this unfair distribution of gains from trade. Most governments have failed to ensure that gains from economic growth – including those due to trade – are shared broadly. The low-growth environment has led to a decline in *per capita* income and has brought frustrations of those deprived of benefits from free trade to a boil. Costs and inefficiencies have been protracted and incomes have fallen severely, making long-run gains by the economy feel intangible and irrelevant. Under social pressure, some governments have switched to protectionism, started negotiating bilateral deals in search of rebalanced outcomes and quick wins, and revisited regional trading agreements, the benefits of which are often perceived as favouring certain partners over others.

Inward-looking policies have put in jeopardy not only multilateralism but even trade as an engine of growth *per se*. Protectionist trade measures have proliferated and have played a non-trivial role in trade slowdown, augmenting the negative impact on trade from weak overall demand. By turning their backs on trade with the application of protectionist measures, governments have been blocking a key driver of growth at a point when the global economy still needs all the support it can get. Also, by flirting with protectionist trade policies, governments have choked off investment, which is yet another critical driver of growth.

Trade multilateralism, along with its rules-based policy and legal framework for trade, is at risk of reduced relevance. The United States remains the centre of gravity in the global economy. Although the machinery of trade multilateralism could falter in the hypothetical scenario of a withdrawal of active support and participation by the United States, its institutional foundations are sufficiently strong and elastic to ensure resilience. Indeed, the WTO has become indispensable and irreplaceable. It could suffer serious harm, however, if it does not reinvent itself under the conditions of a new multilateralism in a radically and continually transforming global economy. The harm from any damage to the multilateral dimension of trade would be lasting because the principles and habits of multilateralism that were decades in the making would not be easy to glue back together again. The WTO is in transition in a global economy in transition. The results from accessions and recent successes, such as the Trade Facilitation Agreement (TFA), point the way to a positive transformation.

The multilateral system, anchored in the WTO, helped to overcome coordination failures and beggar-thy-neighbour behaviour. It brought a more open, stable and transparent global trade environment. This system should now promote more open trade in growing areas of the global economy, like services and electronic commerce. It should also promote competition on a level playing field through stronger provisions in areas like labour, subsidies and competition with state-owned enterprises. While efforts have been made to address these issues in recent trade deals, progress may require more flexible approaches to trade multilateralism. In this regard, the TFA has set an excellent and pragmatic standard.

How can trade multilateralism be made to work for all? Three policy directions stand out: (i) use trade multilateralism as a tool to reignite global economic growth and job creation opportunities, while managing uncertainty and risk; (ii) make trade multilateralism more inclusive to reduce inequality in gains distribution by leveraging technology and structural reforms; (iii) build a new, self-updating and self-learning multilateral trade architecture, adaptable to constantly changing economic realities and policy circumstances. WTO accessions have made important contributions to each of these policy directions.

Reinvigorating Trade Growth Amid Uncertainty and Risk

The outlook for global trade and growth depends on the interplay between the forces driving the recovery and those adding to already high vulnerabilities and external imbalances. The expansionary factors on the macroeconomic front include personal and corporate income tax cuts and higher infrastructure spending. Larger fiscal deficits can stimulate aggregate demand and lead to a strong supply-side response, although at the expense of ever-mounting debt (Blanchard, 2016). Fiscal deficits may have a lesser effect on growth and a greater effect on interest rates. High deficits would also lead to higher inflation. If inflation increases, central banks will have to raise interest rates. Higher interest rates in large countries may lead to appreciation of their currencies and, paradoxically, to larger trade deficits in deficit countries and shrinking surpluses in countries with trade surpluses. Weak productivity growth and a lack of inclusiveness are additional factors that limit the growth outlook (IMF, 2017b).

The contractionary factors for the world economy would substantially depend on the direction of trade policies. For instance, imposing bilateral tariffs to reduce imports in an attempt to level the playing field with trading partners would clearly dampen growth and lead to a prolonged recession. Tariffs may indeed reduce imports, increase domestic demand and increase output. However, the exchange rate would also appreciate as a result of tariffs, hampering exports and all export-driven growth sectors. Moreover, tariffs imposed to reduce imports would in all likelihood invite retaliation, with the risk of a tit-for-tat confrontation and a substantial uncalculated collateral damage as the negative spillovers of restrictions may hamper otherwise competitive sectors. The effect under such a scenario would be depressed growth and shackled exports.

The macroeconomic repercussions of the drop in trade would not be trivial. On the demand side, higher import prices would lead to further interest rate increases, with an ensuing negative impact on growth. On the supply side, higher tariffs would disrupt global supply chains and shrink productivity.

Risks to the global economic outlook are substantial, especially over the medium term. Unpredictable policy shifts may lead to sharp exchange rate swings that can potentially widen global imbalances. In response, some countries may resort to even heavier protectionist measures to defend their domestic economies. Increased trade restrictions would hurt productivity and incomes and worsen market sentiment. In addition, geopolitical risks and a range of other non-economic factors would continue to weigh on the economic outlook in various regions. They include civil war and other domestic conflicts; the tragic plight of refugees and migrants; acts of terror from outside and from within; the protracted effects of climate warming, leading to droughts, floods and other natural calamities; and the spread of deadly viruses. If these geopolitical tensions intensify, they can further dampen investor and economic confidence, and therefore growth and trade.

Securing greater prosperity for everyone implies that the global economy must grow and that municipal governments accept responsibility for equity and expanded opportunities inside their own countries. With growing population, just slicing the existing pie more fairly would help but will not be sufficient. And trade opening and integration are the right instruments to grow the pie.

The economic arguments in favour of free trade have been well known since Ricardo, but they are worth repeating (Obstfeld, 2016). Trade supports growth and welfare by delivering a greater variety of goods and services to households and businesses at lower prices. Also, and even more importantly, trade supports growth by improving productivity, i.e. the efficiency in the use of global resources to produce goods. Comparative advantage is the main reason why trade enhances productivity. In exploiting their comparative advantages, trading partners can specialize in the products that they can produce more cheaply relative to other goods, and trade them.

Trade offers a broader set of intermediate inputs that can contribute to lowering the cost of production. With trade, foreign competition forces local producers to raise their game if they want to survive. Exporters can learn better techniques and technologies through their engagement in foreign markets. Importers can help to instil better standards in domestic production by providing consumers with a direct – and often eye-opening – comparison between local and foreign goods. Those who trade are forced to compete for customers by raising efficiency and upgrading product quality. In short, trade always raises productivity. Hence, to accelerate growth, trade and market-based policies remain critical – a point often missed in the current public debate.

With protectionist attitudes on the rise, the task at hand for policymakers is, first of all, to make the right decisions to maintain sound macroeconomic policies and economic openness. This combination of sound policies and openness has already delivered many benefits for the world in the post-war period. If governments turn their backs on trade, a key driver of growth will be choked off at a time when growth is still fragile. To use a medical metaphor, restricting trade would be a clear case of economic malpractice (Lagarde, 2016). Rather than helping those sectors of the economy it means to shelter, protectionism would amount to denying workers and businesses important economic opportunities, raising the cost of staples and inflicting havoc even on well-established supply chains. All of this would hamper growth.

WTO accessions have already contributed substantially to reinvigorating growth through trade and they can contribute even more. Their impact on growth has been multidimensional, but it has come primarily through increased trade, improved institutions and strengthened competitiveness (see Dadush and Osakwe, 2015, for a detailed literature review).

For example, Subramanian and Wei (2007) find that there is robust evidence that the WTO has had a powerful and positive, albeit uneven, impact on trade. WTO membership has been associated with a large increase in imports, mainly for industrial countries and for developing countries that joined the WTO after the Uruguay Round, but not for other developing countries. Osakwe (2011) shows that trade by all recently acceded members increased significantly as they began to implement their accession-related reforms, some pre-accession, others upon accession, and some through agreed phased transition. Allee and Scalera (2012) explain the differentiated impact of WTO membership on trade volumes by the level of trade liberalization commitments accepted by countries in accession negotiations. Countries facing greater scrutiny from the WTO usually engage in greater trade liberalization and usually experience increased trade volumes upon joining.

The impact of WTO membership on growth has been found to be generally positive. Focusing on developing countries, Tang and Wei (2009) found that accessions to the WTO tend to raise *per capita* income of acceded economies, as higher growth and investment generally last for about five years after accession. This conclusion is valid only for those acceded countries that have undertaken substantial reforms. Li and Wu (2004) found that only high-income economies experienced significantly faster growth after accession. This conclusion implies that openness by itself is not sufficient to promote growth and needs to be combined with proper economic institutions. The reasons for the positive impact of WTO accessions on growth are not entirely clear. It can be explained by the fundamental commitment to reforms and the long-lasting nature of accession commitments, which are legally binding as long as the country remains a WTO member.

Accession to the WTO has been found to have a generally positive impact on acceded countries' governance as well. Drabek and Bacchetta (2004) point out that WTO accession goes hand in hand with higher institutional quality and efficiency, and reduces rent-seeking behaviour and corruption. Tang and Wei (2009) find that the beneficial effects of policy commitments made during WTO accession negotiations seem more pronounced among countries with initially poor governance. Maggi and Rodriguez-Clare (1998) show that by committing to free trade, governments may credibly distance themselves from domestic lobbies. However, Ferrantino (2010), using a number of governance indices, finds little impact of WTO accessions on governance and the overall policy environment. Using incidences of tariff evasion as an indicator for the evolution of governance, Javorcik and Narciso (2013) find that WTO accessions helped limit tariff evasion because the implementation of WTO rules limited the discretionary power of customs officials in assessing unit values of goods.

Accessions also have been instrumental in propelling member countries' competitiveness so that they can contribute more to global growth. The overall impact of accessions on competitiveness has been generally positive so far. About two-thirds of Article XII members (i.e. WTO members that acceded under Article XII of the Marrakesh Agreement Establishing the World Trade Organization, also known as the WTO Agreement) have not yet felt any impact on their competitiveness from accession-related reforms, as the difference-in-difference method did not detect any statistically significant differences between the treatment and the control groups (see Low *et al.*, 2016, Chapter 5 for details). This outcome should have been expected as earlier empirical evidence suggests that structural reforms translate into better macroeconomic outcomes and competitiveness only with a substantial lag. This may be driven by the fact that accession-related reforms take substantial implementation time as they require deep institutional changes. Also, these reforms are designed mainly to improve access by new WTO members to international markets and therefore may translate into better macroeconomic outcomes and competitiveness with time. The remaining one-third of Article XII countries seems to have experienced the impact of WTO accessions already. In most cases, the impact was positive and statistically significant.

Making Trade Multilateralism More Inclusive

Inequality has been traditionally and misleadingly blamed on trade. Clearly, there are short-run costs – adjustment costs – of redeploying an economy's resources out of a sector that shrinks under free trade. With open trade some workers are stranded in a contracting sector, perhaps unable to move to a more dynamic region or to quickly learn new skills. In the real world, 'costs and inefficiencies can be protracted and fall harshly on some, making long-run gains to the economy feel abstract and irrelevant to them' (Obstfeld, 2016). Even without adjustment problems, trade can worsen domestic income distribution by making some people worse off in absolute terms. In this case, although the country as a whole experiences increased productivity and income, some people may gain disproportionately, while others may lose in absolute terms. For the losers, this feels like a raw deal.

Trade has not, however, been the only factor behind rising inequality. Technology has also played a major role in it. Technological improvements benefit some parts of the economy more than others. The consequences of the introduction of new technology and of trade opening are almost identical. Free trade allows goods to be produced in countries and sectors where they can be produced more efficiently relative to other countries and sectors. Similarly, new technology allows commodities to be produced more efficiently in countries and sectors that have adopted the necessary technological innovations, compared to countries and sectors still using older technologies. As a result, those who are involved in production in a more efficient way – be it through trade, technology or both – win, while all others lose. Technological improvement is thus analogous to trade because it tends to redistribute income in a similar manner.

Recent research suggests that open trade and factor mobility are indeed associated with higher inequality. The effect is both statistically and economically significant. In particular, the magnitude of the estimated coefficient suggests that an increase in trade integration from the 50th to the 75th percentile of the distribution in the sample – which is similar to the increase in integration in Germany in the past twenty years – is associated with an increase in inequality of 1.6 percentage points – about half of the median increase inequality observed across countries in the past twenty years (IMF, 2017a). The effect is not different, statistically and significantly, between developed economies and emerging and developing economies. The effect of open trade on inequality has been heterogeneous across countries and has been larger in Asia and Eastern Europe. Technological change is also positively related to inequality. The effect is statistically significant and the magnitude is similar to the one of trade integration. Financial integration can also have adverse effects on distribution measures. Trade and financial integration are associated with lower labour share. Financial integration is found to increase the share of income at the top deciles of the distribution and to reduce the share of income at the bottom deciles of the distribution. The effect of economic integration on inequality varies over time and across countries. It has increased over time, almost doubling since 1996, when major trade agreements were signed and the WTO's membership expanded.

Obviously, nobody needs trade multilateralism at any cost; equitable multilateralism is required. Jobs are not lost to trade; they are lost to technology. But trade has been increasingly used by anti-traders, and even governments, as a scapegoat to mask their own incapacity to promote technology and improve international competitiveness. However, 'a proper argument for trade must recognize that it is not a panacea or silver bullet. Trade will not fix widespread shortcomings in terms of economic, social and educational policies that lead to low productivity and asymmetries in wealth distribution' (Azevêdo, 2016). Such quandaries would require a much more encompassing set of economic policies – fiscal, monetary, structural – in addition to trade and its companion policies. A proper case for trade would also need to recognize that it is not perfect just as other policies are imperfect. Despite the overall economic gains, it can hit some countries, businesses, individuals and at times many of them.

The responsibility of governments and their leaders is to respond to the negative effects of trade with pointed domestic reforms. In creating a better, more inclusive model of globalization, the gains of trade should be better shared across society. As unemployment and other dislocations are not strictly or mainly a trade issue, so trade measures alone will not be able to address this disorder. A more far-reaching response is required to deal with the challenges of a global economy driven by technology and innovation. It could include safety net policies to protect those who lose their jobs. Economic policies should protect vulnerable people, not antiquated jobs. In addition to traditional unemployment benefits, protection can be provided through financing and training that would act as a springboard to new skills and therefore to new jobs. Such programmes already exist in many advanced economies. In short, a coherent package of strong macro-policies and structural reforms is needed.

WTO accessions have contributed to WTO rule-making by bringing greater precision and clarity, and by strengthening the inclusiveness of the rules-based system. On market access, the outcomes of accession negotiations codified in goods and services schedules have already improved commercial opportunities for WTO members and therefore contributed to growth inclusiveness and job creation. To illustrate, the rules-based multilateral trading system, which covered 91 per cent of world trade in 1995, has expanded to cover approximately 98 per cent of world trade in 2015 and most likely even more in 2016. This is the result of the WTO's strategic focus on 'universality of membership'.

WTO accessions have contributed to trade inclusiveness in several ways. First, accessions insert new members into the orbit of the multilateral trading system and therefore improve inclusion by virtue of the process *per se*. Thirty-six recently acceded members and over twenty more economies in the accession pipeline – all countries that were previously outside the multilateral trading system – can now use the WTO as a negotiating forum to advance their interests in the international arena. Also, by being included in the multilateral system, the newer economies can benefit from the ground rules set for international commerce. Such rules guarantee important trade rights, including a predictable level of tariffs, most-favoured nation (MFN) status and national treatment. They also force governments to keep their trade policies in line with multilateral rules and within agreed limits. Finally, pursuant to the Dispute Settlement Understanding (DSU), acceded members may use the WTO dispute settlement system – one of the most effective systems for dispute settlement in public international law.

Obviously, incumbent WTO members also benefit symmetrically from including new economies in the multilateral trading system. Incumbent members can negotiate with new members based on the common platform of the WTO; they can expect that new members will follow an agreed set of multilateral trading rules; and finally, in the case of disagreements, incumbent members also have recourse to the dispute settlement procedure based on a predetermined set of rules.

Second, WTO accessions improve inclusion by promoting domestic reforms. Accession commitments lock countries into a negotiated set of policies for the length of their WTO membership and make them