

How Much Further Can the WTO Go? Developed Countries Issues

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How Much Further Can the WTO Go? Developed Countries Issues

Patrick MESSERLIN[1]

ABSTRACT

A lack of political leadership is often perceived as the main source of the repeated difficulties of the WTO. The paper argues that such a lack of leadership is a systemic problem for many years to come. The large industrial democracies have constitutional rules making particularly difficult trade liberalization in agriculture, and their governments rely on majorities which are increasingly thinner, hence less resistant to even tiny pressure groups.

Then the paper argues that bilateral trade agreements ("bilaterals") do not offer a solution to such a lack of political leadership. Firstly, it shows that the often mentioned recent increase in bilaterals grossly overestimates the true evolution. Secondly, it stresses the fact that, so far, the push behind these bilaterals comes mostly from the small countries, not from the large ones. Lastly, it shows that the 2006 initiative of the European Commission – the first proactive move of a large country – would launch a race to bilaterals so costly that they are unlikely to be sustainable in the long run.

Lastly, the paper argues that improving the efficiency of the WTO negotiating process can offer an appropriate solution to a lack of leadership. It highlights six sources of reform which have one common goal – shooting at shorter Rounds – and which would "flexipline" the WTO process, that is, discipline it – by focusing on the core WTO business of market access and relying on formulas for negotiating market access in goods – and make the WTO process more flexible – by reassessing the value of binding tariffs, relying on plurilaterals for negotiating market access in services, re-interpreting the Single Undertaking principle, and mellowing the bilaterals by more WTO-friendly rules of origin..

Keywords: Domestic politics and trade, Regional trade agreements, Doha Round, WTO

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How Much Further Can the WTO Go?
Developed Countries Issues

Patrick MESSERLIN[1]

INTRODUCTION

A lack of political leadership is often perceived as the main source of the repeated difficulties – indefinite suspension ? – of the Doha Round. This observation triggers two opposite reactions. First is the belief that this situation will be transitory – sooner or later, political leadership will be back. Section 1 argues that this is a dangerous illusion. The current lack of leadership in the WTO is a systemic problem for the many years, or even decades, to come. Of course, visionary and courageous leaders could emerge at some point in the future, but many reasons suggest that such a hope is unwarranted, almost irrational.

The alternative reaction is that the lack of political leadership is here for a long time, and condemns the WTO-based multilateral trade system to enter a long coma, all the more because of the massive increase of the WTO Members. Supporters of this view argue that these combined evolutions make necessary to turn to the substitute of preferential trade agreements (PTAs), that the shift to PTAs has already begun a decade ago, and that it is accelerating. Section 2 shows that the evidence often used for supporting this view grossly overestimates and misinterprets the increase in PTAs. It also argues that the 2006 initiative of the European Commission represents a serious danger to the multilateral trading regime because, although probably unsustainable in the long run, it may launch in the short run a race to more PTAs among the large WTO Members (which are so far "marginal" players in this game, contrary to what is widely believed).

How to cope with a systemic lack of political leadership while minimizing the risks created by PTAs? Section 3 argues that the medicine usually suggested today – a better monitoring of the PTAs by the WTO – is far to be enough. There is a need to improve the efficiency of the WTO negotiating process: the more efficient this process will be, the less attractive bilaterals will be. Section 3 highlights six sources of reform which have one common goal – shooting at shorter Rounds. These sources aim at "flexiplining" the WTO process, that is, disciplining it – by focusing on the core WTO business of market access, and by relying on formulas for negotiating market access in goods—and making it more flexible – by reassessing the value of binding tariffs, by relying on plurilaterals for negotiating market access in services, by re-interpreting the Single Undertaking principle, and by mellowing the bilaterals by more WTO-friendly rules of origin. As these sources reinforce each other, each of them can be used more gently than it were alone. Section 4 concludes by looking at the countries which could promote such changes, and by underlining the absolutely crucial role of domestic support in such an endeavor.

I. Domestic politics and leadership in the WTO

The five first Rounds of multilateral trade negotiations lasted less then 18 months each, the two next ones (the Kennedy Round in the 1960s and the Tokyo Round in the 1970s) less than six years, and the last one (the Uruguay Round) eight years if one assumes that the Uruguay Round started at the Punta del Este meeting (1986-1994), more accurately twelve years if one takes into account the failed start in 1982 – twice the time necessary to conclude the Tokyo Round. The reasons for this drift are well known: negotiations cover an increasing number of issues (technical barriers to trade, customs valuation, government procurement, subsidies and dumping, services, agriculture, intellectual property rights, etc.) all of them being much more difficult to negotiate than tariffs, and they involve many more WTO Members.

This evolution is putting increasing pressures on the politicians of the developed countries for two reasons. They abide by constitutional rules which are unchanged since the end of the Second World War (and

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sometimes much before). They are operating in democracies which are delivering increasingly thin majorities – eroding the permissive consensus in favor of freer trade which prevailed until the 1990s.

Constitutional Rules and Multilateral Trade Negotiations

Key constitutional rules happen to be often biased against further trade liberalization in industrial countries. Some rules have a long term impact. In the U.S., the President has a short four-years mandate that can be extended once. The U.S. President has thus a maximum of eight years for launching and concluding multilateral trade negotiations, with a presidential campaign in the middle of these negotiations. As the President needs a year or so to convince Congress (which has the key power of ratifying trade agreements) in order to get the "fast track" authority for a full mandate of negotiations, his/her window of opportunity is reduced to roughly six years. This time constraint played no role in the GATT Rounds until the Tokyo Round because all these Rounds were concluded in less than six years, but it begun to generate concerns during the Uruguay Round, and it is a major constraint for the Doha Round. [2]/

Other constitutional rules have a shorter term impact. The U.S. Constitution amplifies the weight of agriculture by giving two senatorial seats to every U.S. State. The 23 U.S. States with farm products sales representing a share of the Gross State Product larger than the share for the entire U.S. economy are represented by 46 senators, whereas they represent only 24 percent of the Gross State Product of all the U.S. States – a huge over-representation. [3]/ The constraint did not play any role until the Uruguay Round simply because liberalization in agriculture was not on the agenda and because the Uruguay Round did not generate substantial tariff or subsidy cuts in agriculture. But as long as farm tariff and subsidy cuts will be major issues of negotiations, it is likely to play a crucial role.

The EC constitutional regime is a strong handicap to an EC significant leadership in multilateral trade negotiations. The EC is a collective decision-maker, with the majority rule as the most frequent decision process in case of trade in goods. However, this majority rule faces a severe limit. Everytime a topic is of critical importance for a Member State, the Member State can exert an indirect veto, by threatening to use its veto rights in the other issues which continue to be subjected to consensus (internal taxation, for instance). As the EC enlargements are likely to expand the range of trade issues of critical importance (it would be surprizing that the new Member States do not bring "their" own critical trade agenda) they are likely to reduce the EC capacity to take initiatives in multilateral trade negotiations, or at least to slow it down, in order to find the time necessary to strike a deal on intra-EC trade-offs capable to unlock the EC trade strategy [Messerlin 2007].

Increasingly Thin Majorities

Economic analysis shows that trade is beneficial for a country as a whole, but is detrimental to certain people in the country. It thus provides an explanation to an apparent paradox – the multi-secular push towards freer trade, and the permanently re-emerging opposition to it. But it also raises another paradox which has attracted surprizingly little attention so far. At the beginning of the post-War liberalization process of the industrial countries – from the 1950s to the 1970s – import-competing vested interests were large compared to export lobbies, because export sectors are initially embryonic and import-competing sectors cover a vast range of products. However, despite the unfavorable balance of domestic forces during these years, governments were able to generate a momentum in favor of trade liberalization. [4]/

In sharp contrast, today developed countries are characterized by smaller import-competing sectors, often routinely adjusting to foreign competitors, and by wider and strong export interests. As a result, a smoother ride towards freer trade should thus be expected. This is not the case. Today, further trade liberalization is slow to progress in most developed countries.

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[2] /President H. Truman was able to conlcude three GATT Rounds, and President D. Eisenhower two Rounds. The Kennedy Round was the first to be launched, but it was concluded by his successor (L. Johnson) who was Vice-President during the Kennedy Presidency. The Tokyo Round was the first to involve two Presidents from different parties (G. Ford, a Republican, and J. Carter, a Democrat) while the Uruguay Round lasted three Presidencies (R. Reagan, G.H. Bush, two Republicans, and W. Clinton, a Democrat).

[3] /These 23 U.S. States do not include six States (California, Texas, Illinois, Georgia, Florida, Ohio, Michigan and Pennsylvania) which have the largest farm output in the U.S., but which have GSP farm shares smaller than the share for the entire U.S. economy. The EC exhibits a relatively similar feature [Messerlin 2007].

[4] /Introducing "political" weights for sectors which would counterbalance their size effect (as done in the literature) "solves" the problem, but without explaining the nature and the emergence of such political factors.

Why such a slowing down? A first potential culprit could be the lack of interests from the export sectors, and, more generally, from the business community of the developed countries. But, if this community has been slow to enter the debate of the Doha Round (an attitude quite easy to understand when confronted to the confused debates of the WTO negotiators) it has been very active since a couple of years [International Chamber of Commerce 2007, UNICE 2007, National Association of Manufacturers 2007]. A second potential culprit could be the peoples of the industrial countries, and their loss of appetite for freer trade. But, recent polls show quite the contrary – a strong support for international trade in the public opinion of the U.S. and in the EC (on average 70 percent) [German Marshall Fund 2006]. A third potential culprit could be vested interests opposed to freer trade, tiny but well organized and strong [Baldwin 2006]. But, strong and tiny ("striny") lobbies are not a new story in trade matters. The less than 30,000 U.S. cotton farms and 25,000 EC banana farms echo the candlestick makers so eloquently described by Bastiat [1845] some 150 years ago.

The erosion of the permissive consensus in favor of freer trade that occurred during the two last decades requires thus a better explanation. A convincing candidate is the increasingly thin majorities in the major industrial democracies since the late 1980s. Thinner majorities grant to the striny vested interests a power increasingly out of proportion with their real importance, suffocating the huge support among the people and business for freer trade.

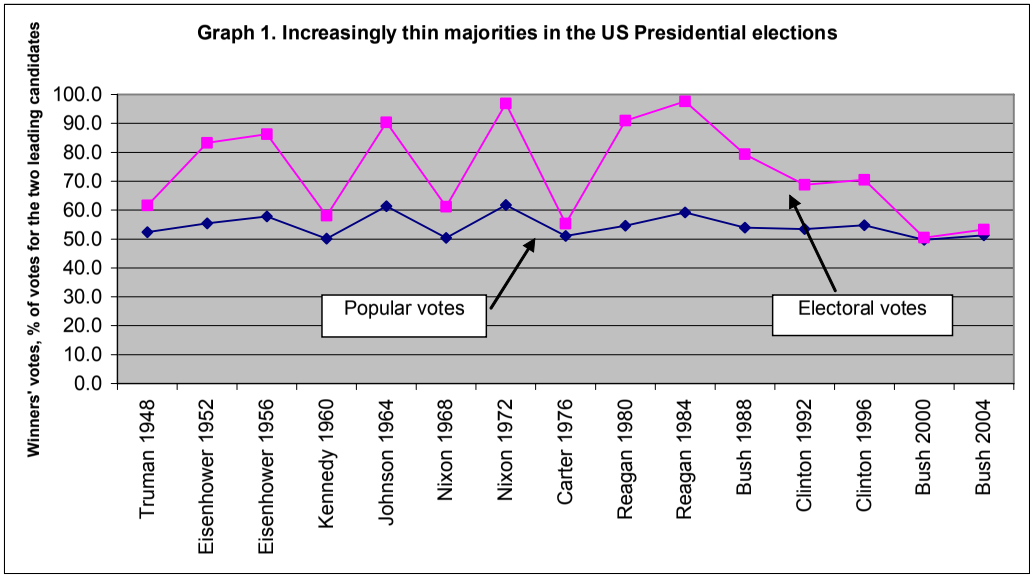
Graphs 1 to 4 illustrate the evolution of the governing majorities in the four largest founding GATT Members since the 1950s. They focus on majority margins, that is, the ratio of the winners in the examined elections over the loosers, independently from which political party is the winner. They focus on the elections that are the most crucial from a trade perspective.

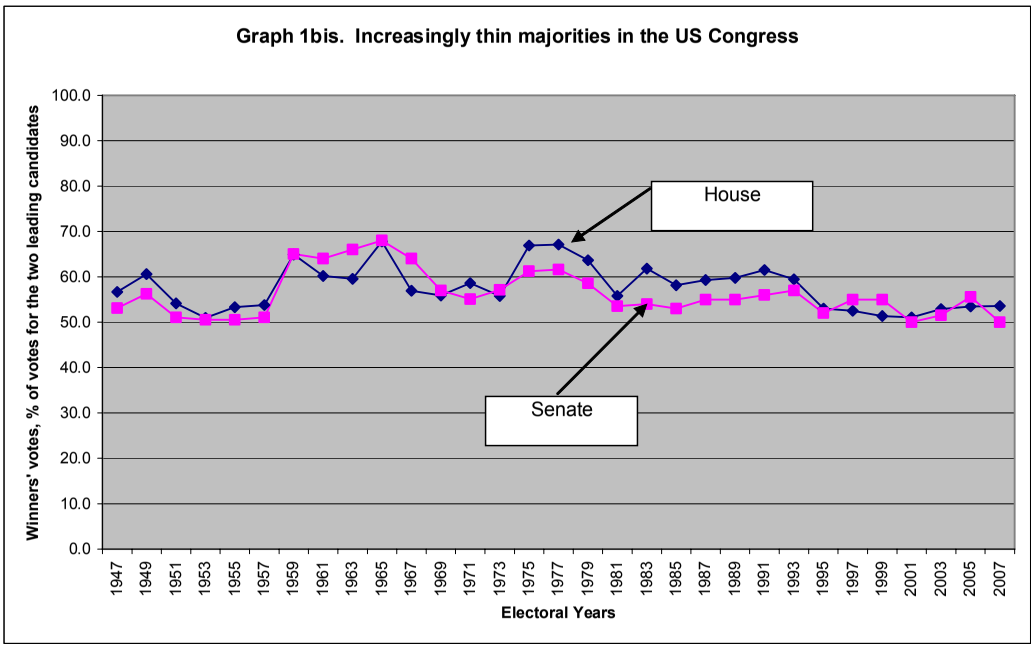
U.S. presidential elections are crucial for trade policy since it is the President who takes the initiative in trade negotiations – first by consulting trading partners, then by deciding to go to Congress for getting approval for launching formal negotiations, lastly by tabling a package acceptable to Congress. Since the mid-1980s, the decline in the presidential majorities has been phenomenal among the electoral voters who are the key ones under U.S. Constitution. The ratio of the votes in favor of the elected President to those for the losing candidate has collapsed by 45 percentage points, with all-time lows in 2000 and 2004. The corresponding ratio in the American people's votes has also substantially declined (by 8 percentage points).

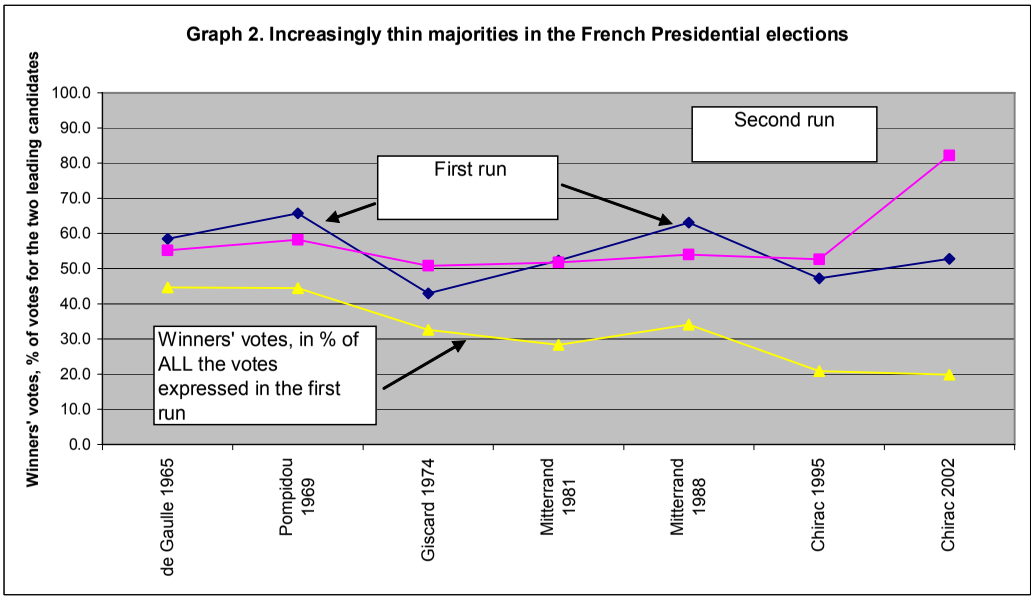
One also notes a steady and substantial decline in the majority margins at the House of Representatives (often considered by the U.S. trade observers as the most important of the two Chambers in terms of trade policy). This decline has begun earlier (late 1970s) than in the presidential elections. The majority margins at the Senate follows the same pattern, albeit in a more moderate manner.

French presidential elections are also the key ones in trade policy because the President plays a dominant role in foreign policy matters (his "domaine réservé"). These elections consist in two runs ("tours") with the two best placed candidates in the first tour being the only ones allowed to run in the second tour. Since 1988, the first tour shows a decline of the votes for the best placed candidate, compared to those in favor of the second best placed candidate. [5]/ But, the best sense of the real political strength of an elected President is given by the votes supporting him in the first tour compared to all the French votes because this ratio captures the relative size of the core supporters of the elected president. The ratio has dramatically (by 25 percentage points) and continuously decreased since the first direct presidential election in 1965.

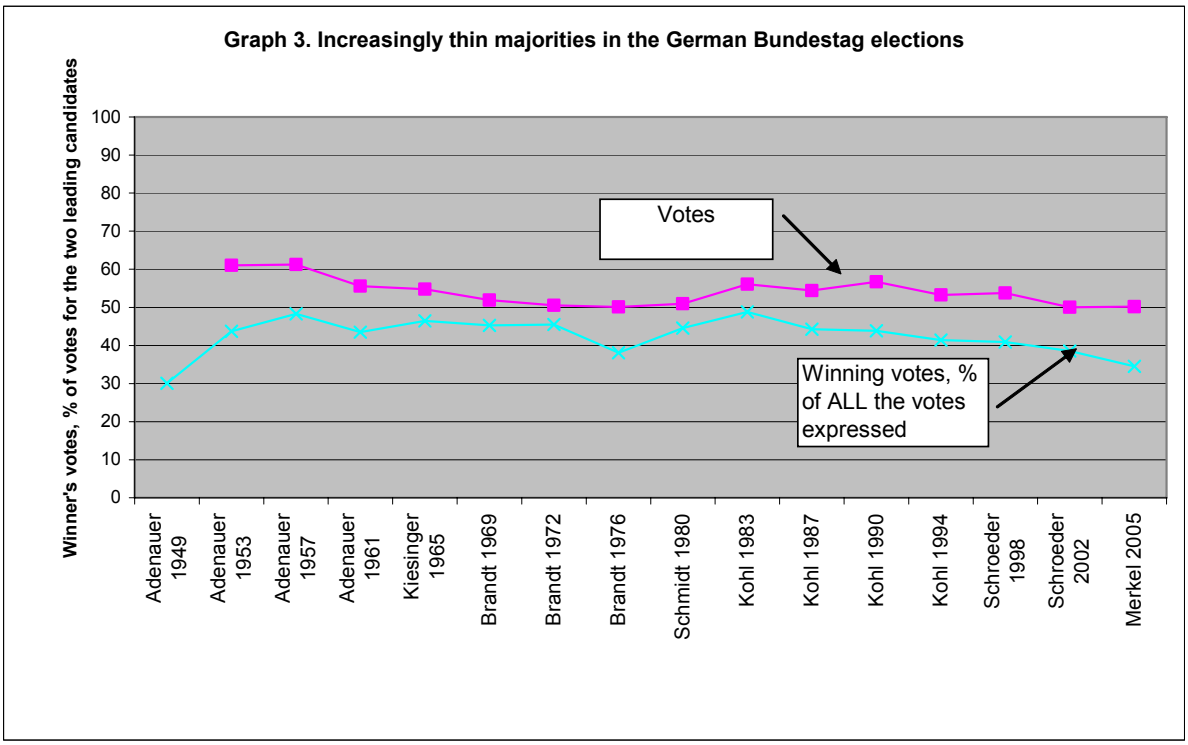
[5] /The second tours do not show a very clear evolution because they reflect loose coalitions of voters. In 2002, the second tour was atypical. It opposed the remaining conservative candidate, J. Chirac, to the extreme-right candidate, J.M. Le Pen. As a result, the "left" votes have little possibility other than to vote for Mr. J. Chirac.


Graph 1. Increasingly thin majorities in the US Presidential elections
Winners' votes, % of votes for the two leading candidates
100.0
90.0
80.0
70.0
60.0
50.0
40.0
30.0
20.0
10.0
0.0
Popular votes
Electoral votes
Truman 1948
Eisenhower 1952
Eisenhower 1956
Kennedy 1960
Johnson 1964
Nixon 1968
Nixon 1972
Carter 1976
Reagan 1980
Reagan 1984
Bush 1988
Clinton 1992
Clinton 1996
Bush 2000
Bush 2004

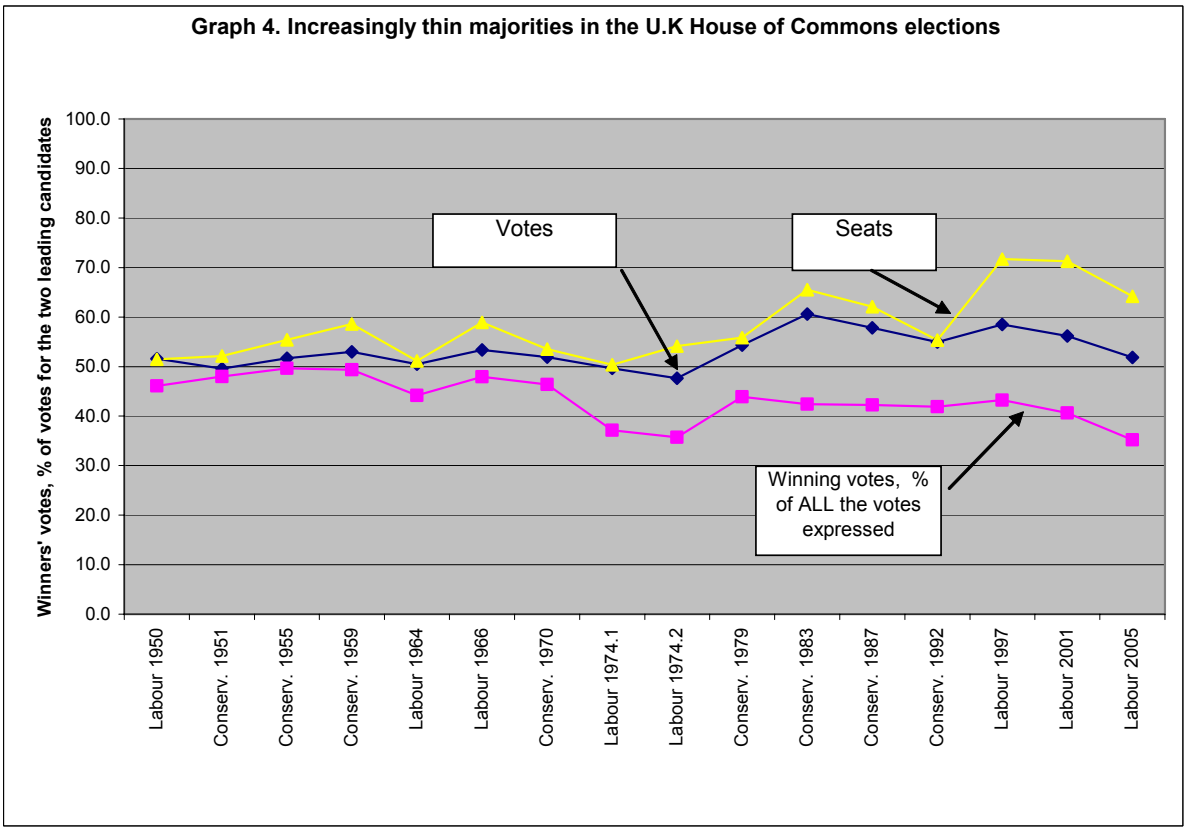

Graph 1bis. Increasingly thin majorities in the US Congress
Winners' votes, % of votes for the two leading candidates
100.0
90.0
80.0
70.0
60.0
50.0
40.0
30.0
20.0
10.0
0.0
House
Senate
1947
1949
1951
1953
1955
1957
1959
1961
1963
1965
1967
1969
1971
1973
1975
1977
1979
1981
1983
1985
1987
1989
1991
1993
1995
1997
1999
2001
2003
2005
2007
Electoral Years


Graph 2. Increasingly thin majorities in the French Presidential elections
Winners' votes, % of votes for the two leading candidates
100.0
90.0
80.0
70.0
60.0
50.0
40.0
30.0
20.0
10.0
0.0
Second run
First run
Winners' votes, in % of ALL the votes expressed in the first run
de Gaulle 1965
Pompidou 1969
Giscard 1974
Mitterrand 1981
Mitterrand 1988
Chirac 1995
Chirac 2002

Graph 3. Increasingly thin majorities in the German Bundestag elections



Graph 4. Increasingly thin majorities in the U.K House of Commons elections



In Germany, the crucial elections are those for the Bundestag (the Lower House). Looking at votes or seats does not make a difference because the German electoral system allocates seats proportionally to votes according to a complex procedure aiming at eliminating too small parties. Since the late 1980s, there is a noticeable erosion in the share of seats of the winning party, compared to the seats of the loosing party –

leading all the German governments since 1969 to rely on "small" coalitions [6]/. In 2005, this ongoing erosion went as far as to require a recourse to a "grand coalition" of the two largest parties (CDU-CSU and Social Democrats). [7]/ That said, the best illustration of the erosion of the majorities in Germany is the decreasing ratio of the winning largest party (whichever it is) in the total German votes expressed. This ratio has declined by 14 percentage points between its last highest peak (1983) and 2005.

At a first glance, the United Kingdom seems a strong exception to our working hypothesis. Far to decline, British winning majorities have an increasing share of votes since the mid-1970s, although there is some signs of erosion since 1983. This impression is amplified when one looks at seats – not a big surprise since the British electoral procedure gives a huge seat premium to the election winners. However, all these observations hide an opposite evolution, that is the noticeable decline (by almost 10 percentage points) of the wining party in the total amount of British votes. (This is due to the increasing number of votes in favor of a third party which has never been able to get a noticeable number of seats.) This increasing gap between the majority in the House of Commons and the situation in the country has a cost. It requires a careful handling by the reigning Prime Minister, hence imposes an increasing limit to its full authority.

Don't count on leadership?

Very little – if anything – can be done for changing constitutional rules. Indeed, when proposed, changes generally tend to shorten presidential mandates rather than to lengthen them, as best illustrated by the change in the French Constitution shortening the presidential mandate from seven to five years (starting in 2002). Such changes happen to be counter-productive from a trade perspective because shorter mandates make more difficult for a President to support freer trade liberalization which is generally characterized by fast-emerging costs and late-coming benefits. Similarly, it is hard to see how to deal with the issue of increasingly thin majorities without endangering the basic functioning of democracies. Indeed, it would be important to understand the reasons behind this evolution in modern industrial democracies in order to have a sense whether it is a long term phenomenon (triggered by higher income enlarging the possibilities of society's goals, hence fragmenting the opinion) or a transitory change subjected to rapid reversals.

In a nutshell, the current lack of leadership is here for a long time. Of course, visionary and courageous leaders could emerge at any point in the future, and make a difference. But it would be foolish to count on them. The period where trade Rounds were shorter than U.S. Presidential mandates, with the U.S. as the natural and benevolent hegemon, seems over.

Combined with the increasingly number of WTO Members, this lack of leadership seems to many observers to condemn the WTO to enter a long coma period, already illustrated by the permanent difficulties faced by the Doha Round since 2001, and that bilateral trade agreements are the only remaining solution. Section 2 looks at this point.

II. How Strong Are The Winds of Bilateralism?

Supporters of an increasing recourse to preferential trade agreements (PTAs) see their views justified by the increasing number of PTAs concluded since the 1990s – culminating to more than 200 PTAs notified to the WTO as of September 2006. This figure is so often quoted, its weight in the WTO debate is so heavy that it deserves attention before turning to substance.

[6] /The coalitions were as follows: CDU-CSU with the Free Democrats (1969-1982), the Social Democrats with the Free Democrats (1982-1998) and then with the Greens (1998-2005). The CDU-CSU is itself a coalition of the Christian Democrats and the Christian Social Union (CSU). The CSU is based in one key German State (Bavaria) characterized by a strong farm lobby. The CSU votes are crucial since they represent, on average, 20 percent of the total votes for the CDU-CSU coalition when the coalition is governing (21.4 percent in the 2005 elections).

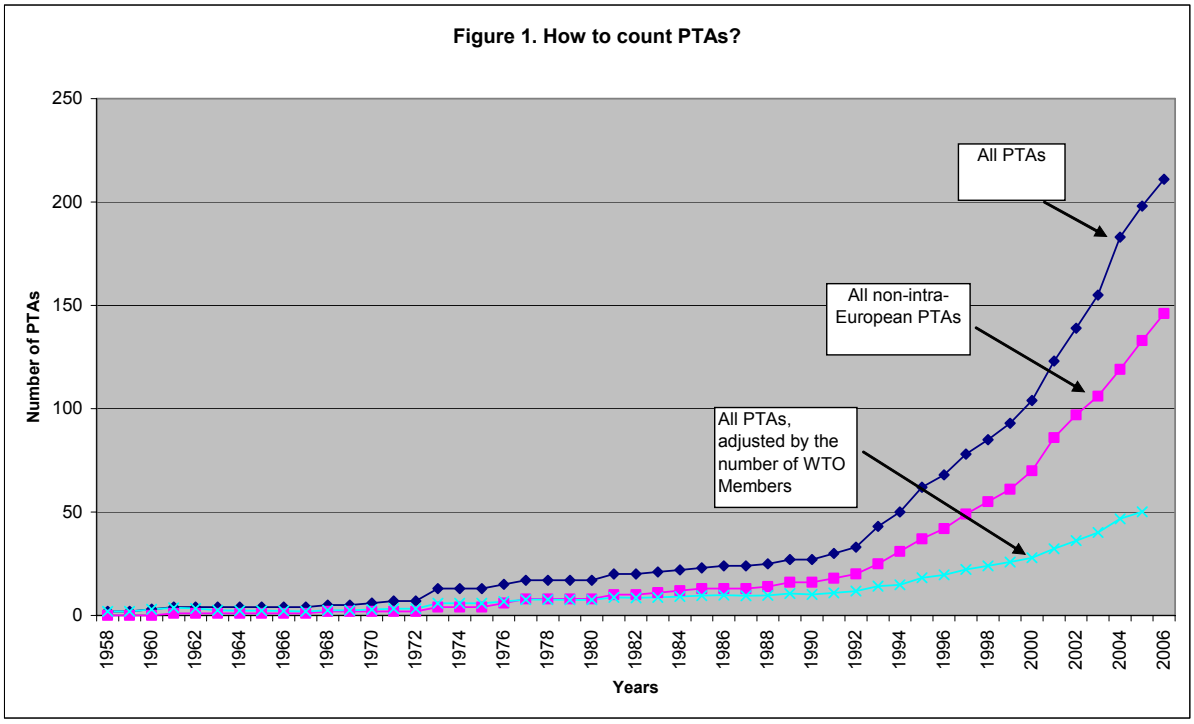
[7] /There was a first "grand coalition" experience from 1966 to 1969.

A. Little Bit of Accounting [8]/

The following sentence (written three decades ago) introduces some immediate caution in the current belief of a PTA boom as a new phenomenon: "The U.S. draftsmen of the ITO Charter did not foresee that post-World War II commercial policy would be dominated by the rise of a multitude of regional agreements which would challenge the draftsmen's universal principles in the most fundamental manner" [Dam 1970, own underline]. Keeping this in mind, Figure 1 shows that the 200 plus PTAs figure gives a seriously exaggerated and misleading view of the recent attraction for PTAs.

Firstly, this figure still includes a very substantial proportion (more than 30 percent in the most recent years) of intra-European trade agreements (defined as deals between countries located in the European continent, excluding Belarus, Russia and Ukraine). The large number

Figure 1. How to count PTAs?



of intra-European deals mirrors the inefficient way (from a purely institutional point of view) Europeans are building their Single Market. Any trade deal negotiated by the EC generates almost mechanically "clone" deals by the EFTA countries, Bulgaria, Romania and Turkey. As a result, every time the EC trade policy changes, a vast number of bilaterals can disappear (as when ten Central European countries joined the EC in 2004, or when the 27 PTAs between the Balkan countries were replaced by one deal under the EC aegis, as decided December 19, 2006) or emerge (for instance, if the EC decides to implement the new policy of bilaterals outlined in 2006 by the Commission, see below).

Secondly, the increase in the number of PTAs notified to the WTO reflects somewhat the increase in WTO membership (for instance, a substantial number of bilaterals involve former Soviet Union republics which have recently acceded to the WTO). Figure 1 "deflates" the (increasing) number of PTAs by the (increasing) number of WTO Members. The "deflated" number of PTAs shows a much more modest increase of PTAs – one-fourth of the unadjusted increase.

Lastly, the few pre-1995 PTAs listed in the WTO 2006 database do not include the PTAs which were negotiated before 1995, but which did not survive, hence are not recorded in 2006.

In short, simple accounting misses the key question – how many of the current 200 PTAs will survive? Answering this question requires to make a difference between PTAs focusing on market access (which tend to survive) and those looking after trade preferences (which tend to fail) for reasons shown in the coming sub-section.

[8] /For similar observations, see Pomfret 2006.

B. The Perpetual Rise and Fall of Preferences

Contrary to unilateral or multilateral liberalization, economic analysis is at pain to provide a clear answer about the net benefits of bilateral trade liberalization [Schiff and Winters 2003]. For most of the economists, bilaterals constitute a second best solution in a vast majority of the cases – and a second best can be far away from the first best. Available evidence confirms the economists' dominant view by suggesting a bad performance of bilaterals in opening new markets. They are credited for only 10 percent of the world market opening having occurred between 1983 and 2003, compared to 65 percent for unilateral liberalization, and 25 percent for WTO-based liberalization [World Bank 2005].

Such a bad performance is not surprizing for the pre-1990s bilaterals which mostly involved countries enforcing high tariffs on imports from the rest of the world (hereafter, "erga omnes" tariffs). In such a case, the two signatories grant to each other high "preferences" (defined as the differences between erga omnes and preferential tariffs). High preferences distort trade flows because they induce consumers to buy goods from inefficient production sources located in the two countries rather than goods more efficiently produced in the rest of the world. The higher the erga omnes tariffs (hence preferences) are, the more distorted the bilateral trade flows may be, the higher the costs of the bilateral (compared to a multilateral liberalization) may be for the consumers of the products imported from the trading partner, the higher the likelihood of the bilateral collapse is.

If the EC, the EFTA and the NAFTA countries have escaped this fate, it is largely because many erga omnes common external European tariffs have been moderate since the very early years. It is also because the EC integration has been immersed in an almost permanent multilateral liberalization process – only 14 out of the 36 years between the EC launch and the end of the Uruguay Round (1995) have not witnessed GATT Round negotiations. During the first years of the EC, this immersion has made easier for EC Member States to compromise on lower external tariffs, and afterwards, it has helped the EC trading partners to reduce the risks of an EC "fortress".

Since the late 1980s, many countries have lowered their erga omnes tariffs. Logically, that should have triggered a loss of interest in bilaterals for two reasons: lower erga omnes tariffs generate reduced preferences; and they subject the pre-existing bilaterals to a painful "erosion" of the initially granted preferences. [9]/

How thus can one explain the continuing attraction to bilaterals in a world with more moderate average applied erga omnes tariffs? Firstly, it may simply reflect that tariff cuts made since the late 1980s are far-to-perfect. They have been made on a wide range of products, but high tariffs and/or non-tariff barriers have been kept on a substantial range of goods, hence ensuring high preferences for the non-liberalized products.

Secondly, most tariff cuts of the two last decades have been done in terms of applied tariffs, not of "bound" tariffs. Under WTO rules, only bound tariffs cannot be raised without compensating the affected trading partners (hence the importance of the WTO negotiations on bound tariffs, see section 3). Today bilaterals may then offer limited preferences on applied tariffs, but still offer high preferences on bound tariffs, hence shifting the risk of tariff increases to the countries without preferential market access.

Lastly, the two last decades have witnessed a shift of interest towards trade in services (as shown by Table 1 below) freer international investment flows. The current WTO framework is at pain for addressing these issues. It is loosely structured with respect of services liberalization, it has a minimal set of provisions on investment in services, and none in goods. Moreover, when including all its 150 members, the WTO does not offer the level of trust that negotiating liberalisation in services and investment does require (see section 3).

That said, bilaterals on trade in services and investments may be attractive for the same reason that the pre-1990s bilaterals on trade in goods were: the existence of high preferences. Hence they may be doomed to the same fate since today, most services are highly protected in most countries, as it was the case for goods

[9] /For instance, following the fall of the Berlin Wall, the EC signed new bilaterals with the Central European economies, breaking up the existing ranking of preferences among its partners in bilaterals (most of them being developing or least developed countries). The political strains of this evolution were so heavy that, in 1997, the Community decided a "pause" in its policy on bilaterals. It renounced to envisage new bilaterals and decided only to conclude the already ongoing negotiations – succeeding with Chile and Mexico, but failing to do so with Mercosur.

before the 1990s. [10]/ The magnitude of this problem depends on whether discriminatory practices are hard to embed in services and investments bilaterals [Roy, Marchetti and Lim 2006] or not.

C. The Current Pattern of PTAs

Table 1 suggests a few key features of the current PTA situation. [11]/ Firstly, the PTAs notified during the WTO years (post-1995) are almost exclusively bilateral trade agreements (hereafter "bilaterals") in sharp contrast with those notified during the GATT years (pre-1995) which are almost equally split between regional trade agreements and bilaterals. [12]/ This conclusion is reinforced by the clear drift from customs union to free trade areas between the two periods. As well known, the trade liberalization brought by free trade areas are severely limited by the use of complex rules of origin, compared to those in the case of customs unions.

Secondly, the breakdown of the non intra-European PTas presents large countries as followers in the recent PTAs wave, rather than as leaders, in sharp contrast to what is widely believed. [13]/ There is no bilateral between the top 10 economies (defined as those having the 10 largest GDPs, including those of the individual EC Member States, under PPP-based exchange rates). And there are only half-a-dozen of bilaterals combining a top 10 and a top 20 economy (in fact, they consist in only three "pairs" of countries, with an agreement in trade in goods coupled with an agreement in trade in services, that is, U.S.-Australia, Japan-Mexico and Thailand-Australia).

Table 1. Preferential trade agreements notified to the WTO from 1958 to 2006, as of September 2006

	Number of agreements			Shares (in %)		
	All years	GATT years	WTO years	All years	GATT years	WTO years
PTAs by type and activity						
Regional vs. bilateral PTAs	211	50	161	100.0	100.0	100.0
regional trade agreements	36	26	10	17.1	52.0	6.2
bilateral trade agreements ("bilaterals")	175	24	151	82.9	48.0	93.8
PTAs on trade in goods and on trade in services	211	50	161	100.0	100.0	100.0
Trade in goods: customs unions	8	5	3	3.8	10.0	1.9
Trade in goods: f\ree trade areas	165	44	121	78.2	88.0	75.2
Trade in services	38	1	37	18.0	2.0	23.0
PTAs by type of signatories	211	50	161	100.0	100.0	100.0
Intra-European deals [a]	65	19	46	30.8	38.0	28.6
Deals with no signatory among the top 20 economies	35	5	30	16.6	10.0	18.6
Non intra-European bilaterals	146	31	115	69.2	62.0	71.4
Breakdown of the non intra-European bilaterals	146	31	115	100.0	100.0	100.0
Bilaterals with one signatory among the top 10 economies	51	6	41	34.9	19.4	35.7
Bilaterals with the U.S.	17	3	14	11.6	9.7	12.2
Bilaterals with the EC	20	2	18	13.7	6.5	15.7
Bilaterals with one signatory among the 11-20 largest economies	34	1	33	23.3	3.2	28.7
Bilaterals with both signatories among the top 20 economies [b]	6	0	6	4.1	--	5.2
Bilaterals with no signatory among the top 20 economies	32	2	30	21.9	6.5	26.1

Source: WTO notifications, WTO website. IMF data on GDP at PPP exchange rates.

Notes [a] Trade deals within the European continent (includes the EC, EFTA, Bulgaria, Romania and Turkey, see text).
[b] There is no bilaterals with both signatories among the top 10 economies.

In addition, one third of the bilaterals involve a top 10 economy with a "small" economy (defined as an economy not among the top 20 economies). The role of the U.S. and the EC is relatively limited, with the EC slightly ahead of the U.S. (a remark useful when assessing the possible U-turn in the EC trade policy in terms of bilaterals). In relative terms, the top 11-20 economies have been more active during the last ten years.

The mirror image of these observations is the large share of the small countries in the recent wave of bilaterals, echoing the long queue of Trade Ministers willing to negotiate a bilateral with the U.S. or the EC at the sudden end of the WTO Cancun Ministerial, though many of these Ministers were much vocal on the risks

[10] /For instance, questions are raised about the real impact of intra-European bilaterals [Aslund 2006].

[11]/Table 1 includes the agreements between the EC and the African-Caribbean-Pacific countries by counting the ACP regional PTAs.

[12] /The change is underestimated by Table 1 to the extent that seven (out of the 10) regional agreements signed during the WTO years are related to the EC trade policy with respect to the African, Caribbean, and Pacific countries, and may not have existed in the absence of this policy. The fading of regional agreements reinforces the conclusion reached in Figure 1 according to which the mere accounting of PTAs magnifies grossly their recent economic impact.

[13] /Intra-European deals are definitively shaped by the EC trade policy

of liberalization a few hours before. Annex 1 offers reasons for the dominance of the small countries in the recent increase of bilaterals.

D. The 2006 EC Initiative: Launching a Race to Bilaterals? [14]/

In November 2006, Peter Mandelson, the EC Trade Commissioner, released a working document spelling out the various options for Europe's trade policy for the coming years [European Commission 2006]. The document reaffirms the support to the Doha negotiations. But, it develops such a massive European strategy in terms of future bilaterals – no less than 24 bilaterals are envisaged – with such a sense of urgent need for action that it has left the strong impression of a change of course in European trade strategy if the Council decides to follow the Commission's proposal. The document was rather coolly received at the European Parliament, and it has not convinced a large share of the European business community about the need to go on the bilateral track [Wallenberg 2006, Seillière 2006]. Since then, the Commission has tried to minimize the initial impression of haste – almost panic – without much success. But, at the same time, it is pushing hard the Member States' Trade Ministries to start as quickly as possible feasibility studies.

The Commission's document suggests that Europe is late in an allegedly ongoing race to bilaterals, hence that it should "catch up". Such an assumption is not supported by evidence. Table 1 shows that Europe is still – by far – the most important source of bilaterals (a point confirmed by Table 2 below). The second most important source of bilaterals are small economies, as shown above, and this is unlikely to threaten severely European trade flows.

The Commission's fears seem to be caused by the fact that, during the recent years, the U.S. has seemed to have the bilaterals game all to itself. This perception is not supported by Table 1 which shows that U.S.-related bilaterals represent only 14 percent of all the post-1990 bilaterals notified to the WTO (a result reinforced by Table 2 based on the size of the bilaterals in question, see below). In addition, there is little evidence of an U.S. strategic approach in terms of bilaterals. The U.S. Administration has taken few initiatives in terms of bilaterals (with Australia, Bahrain, Morocco) and these initiatives were fundamentally driven by foreign policy motives (the Irak war). In contrast to the Commission's approach, the U.S. has no pending "grand vision" in terms of bilaterals. The Free Trade Area for the Americas looks a sleeping beauty, the U.S. calls for an Asian Pacific initiative are incantatory but inconsequential, while the China-U.S. dialogue will most probably reduce the current trade flows between Asia and the U.S., be via exchange rate adjustments by Asian trading partners or via U.S. retaliatory measures. Lastly, the ordeals to get the recent bilaterals approved by the U.S. Congress and the mood of the newly elected Congress (revealed by the request to review of the bilaterals asked by the new Democrat majority) do not suggest that strategic changes are on the agenda.

In such a context, the Commission's aggressive approach could trigger precisely what the Commission fears – a race to bilaterals – to the extent that the Commission's proposal may push the U.S. and other large trading partners to "catch up" in terms of bilaterals.

There is thus a strong need to go beyond impressions and intents by providing a few indicators showing what has been recently effectively achieved in terms of bilaterals and what could be achieved if the ongoing negotiations and those envisaged are concluded. However, what follows does not attempt to do the usual economic analysis – that is, to estimate the net economic gains from bilaterals. Such estimates are notoriously difficult, but, above all, they are subjected to strong limits that their results are easily flawed. For instance, they assume that the two signatories of a bilateral will dismantle their respective trade barriers, and that the resulting situation will last for a long time. As suggested above, they are many reasons to seriously doubt about these premises.

When assessing the current and expected bilaterals, the crucial objective is to make the difference between bilaterals focusing on market opening (likely to be a stepping stone to world trade liberalization) and those focusing on market preferences (likely to be a stumbling stone to world liberalisation). Table 2 presents simple but useful evidence in this respect. It focuses on the EC and the U.S., but, in order to provide a richer perspective, it includes a small economy (Chile) which is the world most active signatory of bilaterals, as shown by column 1 which gives the number of co-signatories of the bilaterals involving these three countries.

[14] /This sub-section relies heavily on Messerlin [2007].

Columns 2 and 3 give the GDP shares of the three countries' trading partners in the world GDP (both at current and PPP exchange rates) give a sense of the market coverage of the possible preferences related to the size of the trading partners involved in the existing and future bilaterals negotiated by the three countries in question. Combining the coverage indicator with indicators focusing on the level of preferences gives a sense of the magnitude (that is, the coverage times the level) of the expected preferences. Columns 2 and 3 reveal a striking difference between the EC and the U.S. on the one hand, and Chile on the other for the bilaterals enforced and signed. The EC and U.S. bilaterals cover a very low share of world GDP, whereas Chile's bilaterals cover almost three quarters of the world GDP (ten times more than the EC and U.S. coverage). Looking at the bilaterals under negotiation or consideration changes dramatically the picture. The Commission's aggressive approach is launching a real race to bilaterals, with the risk that the U.S. could react with its own aggressive strategy.

Table 2: Bilaterals: Three Strategies

	Number of partners	Market size [a] at current USD	Market size [a] at PPP USD	Average industrial tariff [b] applied	Average industrial tariff [b] bound	Regulatory ranking [c] trading across borders	dealing with licences	ease of doing business	regis-tering property	protec-ting investors
	1	2	3	4	5	6	7	8	9	10
A. Bilaterals signed										
Chile	20	79.0	70.4	5.5	8.0	34.1	70.8	41.5	39.6	46.3
USA	15	7.6	6.5	7.5	19.6	42.9	41.9	29.2	50.1	34.0
EC	14 [d]	6.4	8.2	9.2	18.3	76.8	91.9	67.1	80.4	53.4
B. Bilaterals under negotiations or consideration										
Chile	9 [e]	81.6	77.7	6.4	10.3	43.2	77.8	49.4	45.5	45.1
USA	14	14.9	16.5	8.8	21.3	54.1	69.7	52.2	64.7	44.2
EC	24	23.4	44.2	10.3	17.8	71.1	125.6	91.2	61.8	64.8

[a] GDP (in USD, 2004) as a share of world GDP. [b] WTO Trade Profiles. [c] Doing Business 2007.
[d] Counting as one the 10 countries having acceded to the EC in 2004. [e] Counting as one the EC.

Columns 4 and 5 of Table 2 focus on tariffs, the first key instrument that could determine the level of preferences in trade in goods. Low applied average tariffs suggest that partners in the bilaterals have kept relatively few peak tariffs, hence that they offer limited opportunities for preferences, while such opportunities are likely in the case of high applied tariffs (and the same can be said for high bound tariffs). Columns 4 and 5 reveal another striking difference between the EC and the US on the one hand, and Chile on the other hand – for both the existing and envisaged bilaterals. The average applied and bound tariffs of the EC and of the U.S. co-signatories are relatively high, they are low in the case of Chile's bilaterals. In other words, the EC and the U.S. are, volens nolens, looking for tariff preferences – perhaps "nolens" in the U.S. bilaterals since the U.S. has been mostly a follower, clearly "volens" in the proposed EC strategy.

Columns 6 and 7 of Table 2 focus on non-tariff barriers, the other key instrument that could determine the level of preferences in trade in goods. As there is no direct measure of such barriers, Table 2 relies on the ranking of the co-signatories of the EC, the U.S. and Chile in two respects – the ease of trading across borders and the ease of dealing with licences as estimated by the Doing Business database [Doing Business 2006]. Ranks are crude indicators (there may be a much bigger difference between the first and second rank than between the second and third rank, or vice-versa). However, averaging the ranks of the EC, U.S. and Chile co-signatories show differences which are large enough to be meaningful. Columns 6 and 7 suggest that by far the EC is the WTO Member which focuses the most on co-signatories having high non-tariff barriers, particularly with its recent strategy – once again, suggesting the intent to look for market preferences.

Column 8 to 10 of Table 2 are attempts to deal with services and investments. They also rely on ranks provided by the Doing Business database. The services dimension is captured by the global indicator of the ease of doing business in the various co-signatories, whereas the investment dimension is reflected by the quality of property registering and of investors protection in the co-signatory. Once again, these three indicators oppose the EC on the one hand, and Chile and the U.S. on the other hand. The EC tends to look at markets highly protected by inefficient regulations – hence potentially offering high preferences – whereas the two others are more attracted by countries having relatively sound regulations. Market preferences are a mix blessing: it may be useful to get them if other large trading partners do (but this is definitively not yet the case with the countries targeted by the Commission, contrary to what the Commission suggests) but they can also create costly trade distortions generating negative dynamics of preference erosion tensions and risk of collapse of the bilaterals in question.

All the results for the EC are largely, but not exclusively, driven by four targeted countries, namely Brazil, China, India and Russia. Table 2 assumes that this strategy is meaningful, that is, that the bilaterals to be concluded are delivering a real trade liberalization in the EC co-signatories – an assumption far to be granted in the case of bilaterals with "not-so-small" countries (see Annex 1). Moreover, these four countries are not especially known for being easy partners to negotiate with. One really wonders what the EC could get in a bilateral setting that it could not get in the WTO forum by forgeing an alliance with other countries.

III. "Flexiplining" the WTO

Since bilaterals are far to be the panacea, the WTO remains the main road to go. But, a "quick fix" limited to a relaunch of the WTO negotiations (be in 2007 or in 2009) without a serious effort to reshape the WTO negotiating process is almost certain to get minimal results. And these results could be welfare-deteriorating because of the distortions introduced by the many exceptions envisaged by the negotiators, and by the economically unsound instruments to which the negotiators may have recourse for implementing these exceptions (such as tariff-rate quotas). So far, there has been scant attention for making such an effort, if one excepts two decisions adopted at the 2005 Hong Kong Ministerial but still fruitless for reasons explained below. Indeed, the four-years long Doha discussions on "negotiating modalities" have gone in the opposite direction, making the WTO negotiating process more confused and inefficient, hence making the fortune of the bilaterals.

The section argues that there are many possible sources of increased efficiency in the WTO negotiating process. It argues that the current process is prisoner of interpretations which have been shaped a long time ago (and were often very useful then) but which are harmful today, and can be challenged while fully abiding by the WTO principles.

The section highlights six sources of efficiency which have one common goal – shooting at shorter Rounds. All these sources would help to conclude faster WTO Rounds. They are self-reinforcing, a characteristic allowing to use each of them more "gently", a favorable feature for achieving compromises. They aim at "flexiplining" the WTO process, that is, on the one hand at disciplining it – by focusing on the core business of market access and by relying on formulas for negotiating market access in goods – and on the other hand at making it more flexible – by re-assessing the value of binding tariffs, by relying on plurilaterals for negotiating market access in services, by re-interpreting the Single Undertaking principle, and by mellowing the bilaterals via some multilateralisation of their rules of origin. An important side effect of these improvements would be to reduce the attraction for bilaterals in general (and bilaterals focused on market preferences in particular) and to make the current and future bilaterals more friendly to the multilateral trade regime.

Before examining these points, the usual medicine recommended today – a stricter use of GATT Article XXIV for monitoring the bilaterals – deserves a comment. Although useful, this medicine has no capacity (nor claim, to be fair) to relaunch the WTO negotiations, and it has very little chance to have an impact on the proliferation of the bilaterals. This is because it should rely on GATT Article XXIV for trade in goods which has won the hard-to-win qualification of being "deceptive" and "based on a legal error" [Dam 1970] and on its equally cryptic twin GATS Article V for trade in services. Years of negotiations will be needed for agreeing on a common interpretation of such deceptive provisions and of their stricter use. In short, the medicine may be operational too late – once the damage will be done, that is, after that too many PTAs will have been negotiated and enforced.

E. Shooting for Shorter Rounds

Having shorter Rounds is not a new idea, but so far, it has been justified by unconvincing reasons. First is negotiators' fatigue. But negotiators have fixed term assignments in the diplomatic traditions of many countries, and the alternative – a race to bilaterals – will be much more demanding for the negotiators, as well

as for the politicians, the businessmen, and the people. Secondly, it is often said that bilaterals are fast to be negotiated, but anecdotal evidence does not support such an assertion. [15]/

Shooting for shorter Rounds has a much firmer ground when one takes the domestic political constraints examined in section 1 (particularly in the U.S., the most important WTO player) and the erosion of the permissive consensus in favor of freer trade caused by increasingly thin majorities in the major industrial democracies. Ideally, no Round should last more than 6-7 years, mirroring the constraint on U.S. Presidents.

Shorter Rounds mean more limited objectives for each Round. It is often argued in WTO circles that limited targets (a "Round light") is the death of kiss in domestic trade politics, especially in the U.S. Congress. There is a lot of rhetoric in this view, but not a lot of evidence supporting it. In 1994, the Congress passed the Uruguay Round that had a limited trade liberalization component per se, but that has also offered long term perspectives of liberalization. More limited Rounds require to be cast in a sequence of Rounds, and to turn the back to the always deceptive concept of the "Big Last One". A sequence of Rounds has many advantages. In particular, it would smooth domestic concerns about high adjustment costs of the agreed liberalistaion, a key point for both developed and developing countries. And it would have the huge advantage of making the WTO better able to "catch up" in services liberalisation by multilateralising more often bilaterals in services (see below).

F. The WTO Should Focus on its Core Business: Market Access

The WTO should focus on its core business: market access in goods and services. It should not be burdened by other issues which, sooner or later, have to be abandoned. The unceremonious overboard throwing of three Singapore issues at the 2003 Cancun Ministerial has shown the heavy cost of such miscalculations for the WTO as a whole, and for the EC, its staunchest supporter, in particular.

Industrial countries have generally justified the introduction of issues other than market access by arguing that they have nothing left to offer in terms of market access concessions. This argument ignores a basic point: most remaining tariffs of industrial countries target the exports from developing countries [Laird 2002]. The high tariffs imposed by the industrial countries on their imports of manufacturing products may be few, but their economic value for developing countries' exporters is huge. The same can be said for industrial countries' agricultural protection: it inhibits the growth of a critical sector for developing countries – particularly for the poorest ones – even if the importance of agriculture will fade away as and when these countries will grow. Last but not least, this argument ignores the universe of services largely untouched, although it represents 70 percent of rich countries' GDP and it is of prime interest for most WTO Members. In short, there are still plenty of deals about market access to be done.

The best way to eliminate topics not closely related to market access is to deal with them in a better place than the WTO. This is particularly important for international investment because of the intrinsic importance of this topic, and because it has fuelled the recent move to bilateralism via bilateral investment treaties or via investment provisions in bilateral trade agreements [OECD 2006a, 2006b]. The WTO is badly equiped to multilateralize investment bilaterals. The GATT text has no rule on international investment in goods, and the GATS text only general provisions. The OECD has lost its chance to host a worldwide agreement on investment because it mismanaged the last attempt to design such an agreement [Henderson 1999] and because it has a too narrow membership. The International Monetary Fund (IMF) has the appropriate membership, most of the needed expertise, and, last but not least, a need to redefine its role. The IMF (perhaps with the Bank of International Settlements) should thus waste no time for launching an initiative aiming at establishing a multilateral investment framework – undercutting any velleity of the WTO negotiators to grab the issue, especially if they feel jobless in the case of an indefinite suspension of the Doha Round.

[15] /It is impossible to compare the negotiating time required by bilaterals and by WTO negotiations because of the high variability of the trade content of bilaterals. Vague provisions in bilaterals may indicate the absence of real commitments, or, alternatively, they may reflect a "neo-imperial" aspect, particularly if they deal with basic principles (as often in the EC-related bilaterals).

G. Market Access in Goods: Using the Swiss Formula for "Peeling the Onion"

At the 2005 Hong Kong Ministerial, after four years of endless discussions on negotiating "modalities", the Doha negotiators have agreed, almost in despair, to use the Swiss formula for trade in industrial products (NAMA). [16]/

This was a huge step forward which should be adopted permanently because the Swiss formula is an instrument of liberalization both extremely efficient and flexible. From an economic perspective, it cuts tariff peaks by more than the smaller tariffs, hence maximizing the economic benefits from trade liberalization, and improving tariff revenues for countries needing this source of public revenue. From a domestic political economy perspective, it puts more pressure on the high tariff beneficiaries, but it reduces the pressure on the low tariff sectors, hence offering to governments the opportunity to mobilize the support of the large number of moderately protected sectors against the few highly protected. In addition, it moves protection toward a greater neutrality of protection across goods – a key feature helpful for addressing the touchy binding issue (see below). From a negotiating perspective, the formula offers, for any Swiss coefficient envisaged, instant and costless information on the post-liberalization tariff rates, hence facilitating considerably the negotiations, especially for the poorest countries short of negotiating staff. Last, but not least, the formula efficiency allows to treat differently various groups of countries by agreeing on different coefficients for each of these groups – a key feature helpful for addressing the Single Undertaking issue and the trade and development nexus (see below). In short, the Swiss formula is extremely well adapted to the concept of shorter but more frequent Rounds.

Unfortunately, two decisions amounted to void the Hong Kong decision on the Swiss formula of its substance. Firstly, the WTO negotiators agreed on various exceptions to the use of the Swiss formula for "sensitive" industrial products. Secondly, they are still using a much less efficient formula in agriculture, combined with even more exceptions. The potential coverage and magnitude of all these exceptions are so large that they amount to void the formulas adopted of substance.

Why such strategic mistakes? First, and foremost, is that the negotiators of the industrial countries have stuck to a very narrow interpretation of the Binding Tariff principle equating liberalization to a change such as all the post-Doha bound tariffs should be lower than the pre-Doha applied tariffs (see below). [17]/ This interpretation has induced the negotiators of the industrial countries to "overshoot" their initial requests in industrial products by requesting "too" low Swiss coefficients from their trading partners, hence pushing the latter to react by requesting vast exceptions, and ultimately offering the EC and almost a dozen of industrial countries (the so-called G10) to do the same in agriculture – a sequence making the final package of concessions in industrial and agricultural products unpredictable to the point to become useless. [18]/

That said, it is unrealistic to believe that multilateral trade negotiations could be based on a mere formula without exceptions. The lesson is thus that the implicit trade off between any level of the Swiss coefficient and the magnitude of the accompanying exceptions (the higher the Swiss coefficient is, the smaller the demand for exceptions is) should be made explicit as quickly and simply as possible. The magnitude of the exceptions could be expressed as a deviation from the average post-Round bound tariff (negotiators tend to use average tariffs as ways of negotiations) generated by a given Swiss coefficient, and certain conditions could be imposed on the distribution of this deviation over the individual tariffs of the country in question. For instance, if a Swiss coefficient of 20 generates an average post-Round tariff of 15 percent for a given country, the agreed exceptions could allow the average tariff to go up to 16 percent, conditionally to the fact that this "degree of freedom" would not generate an individual tariff higher by more than 10 percentage points than the tariff generated by the Swiss coefficient 20.

Shorter and more frequent Rounds mean that agreeing on a higher Swiss coefficient (that is, on a lower level of liberalisation) may be the price to be paid for granting less exceptions in the current Round, but also that this price is affordable because it will not be paid for a long period of time, with another Round coming in a not

[16] / The "Swiss" formula is $T=(r*t)/(r+t)$ where r is called the Swiss coefficient. This coefficient r defines the highest possible post-liberalization tariff.. When t is very small, $r/(r+t)$ approaches 1 so that T equals t (post-liberalization tariffs will be about the same as the low pre-liberalization tariff). When t (pre-liberalization tariff) is very high, $t/(r+t)$ approaches 1 so that T (post-liberalization tariff) equals r.

[17] / In addition, clearly many negotiators did not initially realize that a Swiss coefficient defines the highest possible post-Doha tariff for initial tariffs much higher than those observable in the real world. For instance, if the coefficient is 20, the post-Doha tariff becomes higher than 19 percent for a pre-Doha tariff close to 500 percent, a tariff level very rare in the real world. For the highest tariffs not too rare in today world (say 100 percent) the post-Doha tariff with a Swiss 20 is 14 percent only.

[18] /As usually in negotiations, once the exceptions were written down in the July 2004 text, it becomes very difficult to negotiate a trade-off based on "buying" a lower level of exceptions by a higher Swiss coefficient.

too distant future. In short, the repeated use of the Swiss formula should work as a patient peeling of the onion.

H. A Necessary Condition: Re-assessing the Value of Binding Tariffs

There is a necessary condition for an efficient use of the Swiss formula: a re-assessment of the Bound Tariff principle. Bound tariffs are the only ones to generate legal commitments in the WTO. Moreover, the principle of bound tariffs makes a lot of sense from an economic point of view. Evidence shows a strong relation between a low level of average tariff water and good domestic governance (as measured by the ranking of the ease of doing business) among the WTO membership.

That said, the current interpretation of the Bound Tariff principle as equating liberalization to a change such as all the bound tariffs enforced after a Round should be lower than the tariffs applied before the Round misses a key point. This is the fact that the Doha Round occurs at a very special time, that is, at the end of a period where many developing countries have substantially lowered their applied tariffs, while still being reluctant to decrease their bound tariffs. Available information [WTO 2006] shows that 104 WTO Members (out of 143, or more accurately 117 if one counts the EC as one Member) enforce applied tariffs lower than their bound tariffs, with 70 of these Members having an average "tariff water" (the difference between their bound and applied tariffs) higher than 10 percent. Tariff water can reach impressing average levels in some cases (around 100 percent). Out of these 70 countries, 21 can be classified as emerging economies, the rest being developing countries. [19]

This special situation makes easy to understand why the current interpretation of the Bound Tariff principle is a major stumbling block in the Doha Round. However, there are three good reasons to challenge this interpretation.

Firstly, if binding has a value because it brings legal certainty, cutting bound tariffs should have a value for businesses even if these cuts leave unchanged the existing applied tariffs. Such an interpretation is particularly suitable to a situation characterized by large tariff water, as today. Even if short to cut applied tariffs, cuts in bound tariffs can be substantial, hence delivering a lot of this certainty that businesses appreciate above all. The Doha Round should be seen as a "Round of transition" which could leave some differentials between bound and currently applied tariffs, but which should reduce them enough to ensure their elimination in the Round following the Doha Round.

Secondly, the value of the binding principle for the trading partners of a country is not absolute, but relative. It may first depend on international factors, and it happens to be the case of the Doha Round, another specificity of this Round that should be taken into account. In particular, the fact that India would bind some of its tariffs at a level higher than their currently applied rates represents an affordable risk for its trading partners in the current context. This is because, if India wants to be as attractive as China for the world traders and investors, it has to offer roughly the same tariff conditions than Chinese bound tariffs. In short, Chinese bound tariffs work as proxies of bound tariffs in India (and a few economies at the same stage of development). "Peer pressure" counts.

Lastly, the value of a country's bound tariffs for its trading partners may also depend on domestic factors in the country in question – in particular, the dispersion among the country's tariffs. Because protection granted to some domestic producers gives them an advantage at the detriment of the other domestic producers, domestic producers lobbying for an increase in a given applied tariff are likely to face increasing opposition from their fellow domestic producers as and when the requested tariff increase comes closer to the highest existing tariffs of the country. In short, the most dispersed the tariff rates imposed by a country are, the riskier its unbound tariffs are for its trading partners, hence the higher the value of bindings is for the partners.

Such a link between the value of binding and domestic tariff dispersion has an important corollary. There are strong incentives not to raise applied tariffs in a country which is enforcing an "uniform" tariff (the same tariff on all the products it imports) even if these tariffs are not bound. This is because domestic producers would immediately oppose a move favoring one of them (the producer getting a higher tariff) but disadvantageous to all the others. It is not by accident that two (Chile and Singapore) out of the three WTO Members having unilaterally adopted an uniform tariff structure have still not bound their tariffs at their applied level (the tariff

[19] /All the existing coalitions have strong links with the bound tariff issue. 23 out of 24 Small and Vulnerable Economies, 29 out of the 32 Least Developed Countries, 32 out of the 38 members of the G33, and 5 out of the 6 Recently Acceeding Members (RAMs) exhibit average tariff water. The averages are high (respectively 37.3 percent, 32.8 percent, and 31.3 percent) except for the RAMs group (3.2 percent), a striking illustration of the unbalanced situation faced by the new Members.

water is huge for Chile which has bound its tariffs at 25 percent while applying an uniform tariff of 6 percent). In short, the more uniform the tariffs of a country are, the less the absence of binding these tariffs could have negative consequences for the trading partners of this country.

In short, the demand for binding tariffs should be modulated in order to take into account the "transition" feature of the Doha Round, the intensity of the "peer pressure", the magnitude of dispersion of the tariff structure of the country in question, and, as shown below, the level of flexibility in the interpretation of the Single Undertaking.

I. Market Access in Services: Plurilaterals and the "Coalitions of the Willing"

Opening market in services requires trust in partners for undertaking the adequate pro-competitive regulatory reforms. The dimensions of trust are manifold: overcome reluctance over movement of people (mode 4) and sensitive sectors (maritime, health, education, audiovisuals, etc.) promote conclusions of mutual recognition agreements without GATS Article VII disciplines, etc. Trust is all the more necessary because regulatory reforms call for a dynamic process of continuous changes which is very hard to forecast when negotiating the initial trade agreement. The huge WTO membership (150 Members) is so heterogeneous in terms of both regulatory capacities and willingness to undertake the necessary reforms that it is a strong handicap for reaching substantial liberalization in services in the WTO forum – hence the attraction of bilaterals in services. But, as already underlined, bilaterals in services can be very costly because the high level of protection in services would induce many of them to focus on market preferences with its negative consequences.

At the Hong Kong Ministerial, the Doha negotiators have made a first step for enhancing the WTO negotiating process in services when they have agreed to undertake negotiations in a "plurilateral" framework limited to the countries willing to open their markets on a sector by sector basis. This initiative is close to a very successful negotiating process used for the first time at the 1996 Singapore Ministerial for the Financial Services Agreement and for the Information Technology Agreement which have both been successful.

Plurilaterals at the WTO offer a good compromise between bilaterals and the fully multilateral approach if they address a few additional pending issues [Adlung 2006, Hoekman 2006]. [20] In particular, they should define the "critical mass" of Members (in number or economic size) to be reached for materializing potential agreements. They should also design the "reference papers" spelling out the basic regulatory disciplines that the signatories should aim at establishing in each service sector. And they should ensure that any latecomer to a sectoral agreement will not be subjected to commitments other than those included in the initial agreement.

As suggested above, bilaterals may remain relatively attractive in services because of the need of deep trust between the signatories. This may be particularly the case of agreements on the transitory movement of persons (mode 4) which looks much easier to develop initially on a bilateral basis. As a result, in addition to generating plurilateral agreements, an essential role of the WTO in services liberalization would be to multilateralise the existing or future bilaterals in services. In this perspective, the Rounds should be relatively frequent in order not to leave too long periods without opening the possibility to launch a catching up process. In sum, in addition to reasons related to the likely "lack of leadership" among the major trading partners, the huge domain of services (by far, the most important in size and in welfare gains for the coming decades) offers a good intrinsic reason to have more frequent Rounds.

J. Re-interpreting the Single Undertaking Principle: "Positive Discrimination"

The prevailing interpretation of the Single Undertaking principle is that every WTO Member shall sign all the agreements negotiated during a Round (or, at least, to achieve consensus on the conclusion of negotiations across all areas). The principle was adopted during the Uruguay Round, and it was then felt necessary for making the multilateral trade regime more consistent. At this time, such an interpretation made a lot of sense for two reasons. Firstly, the Uruguay Round agreements concentrate on general goals and rules (liberalizing trade in agriculture and services, regulating subsidies, norms and standards, etc.) that every WTO Member should agree on in order to ensure a minimal consistency of the multilateral trade regime. Secondly, the

[20] /Exanples for MFN-based plutilaterals are the Fourth and Fifth Protocols on basic telecommunications (February 1997) and on financial services (December 1997).

Uruguay Round negotiations on market access remained de facto limited to industrial products, a process initiated so many years ago that it was rightly felt reasonable to involve all the WTO Members in it, all the more because many developing countries were unilaterally liberalizing.

Ten years later, such a strict interpretation is backfiring. It has greatly compounded the problem raised by the enlargement of the WTO membership by making the WTO negotiating process a hostage of the Members which are the most reluctant to liberalise. And it has fuelled a process of systemic evasion from the WTO framework through the definition of groups of WTO Members getting exempted from various specific WTO obligations. The Least Developed Countries were the first to get a special status, early in the Uruguay Round. They were followed by the Net Food Importing Developing Countries during the very last days of the Uruguay Round negotiations. Since the launch of the Doha Round, other exceptions have been tabled: the Small and Vulnerable Economies, the Cotton Producers, the Recently Acceeding Members (RAMs).

And the list is not closed. In particular, there is the increasingly loud request by a substantial number of developing countries to have a status distinct from those enjoyed de facto by the emerging economies and de jure by the least developed economies. If such a new group is created, very few "developing countries" would still be abiding by all the WTO rules – making a mockery of the Single Undertaking principle. Even worse, such an approach (based on the skills of negotiators able to sneak in their country at a propitious moment) generates an irrational, chaotic and ultimately unjust WTO forum: some recent WTO Members do not enjoy the LDC status although they are as poor as the richest LDCs (or are being pushed to the limits, such as Cambodia and Nepal); many WTO Members are more genuinely dependent from food imports than the few which extracted a special status ten years ago [Zedillo and Messerlin 2005]; the SVE coalition includes the 68th world largest economy (out of 182 economies), etc.

Such an approach based on "negative discrimination" is unsatisfactory on several other grounds. Firstly, it requires to find objective criteria for defining a group. The task has not been too difficult when defining the "poorest" countries (although there are still pending questions) but it is much harder in all the other cases, as best illustrated by the SVEs' struggle to define their own group. Secondly, the agreement from the WTO Members not pertaining to a proposed group is very hard to get, risking to block the whole WTO machinery for years. Thirdly, once created, groups are hard to be dissolved (even if the rationale behind them has disappeared) meaning that exceptions are granted for ever. Lastly, and perhaps crucially, a group tends to be a "prison" for the most dynamic members of the groups to the extent that it is very difficult for a group member to breach the ranks, and to opt for a freer trade policy if it suddenly realizes that it is in its own interests.

The WTO is thus at a crossroad. Either, the current strict interpretation of the Single Undertaking prevails, and there will be permanent centripetal forces to make "group exceptions", and to desintegrate the WTO forum. Or the Single Undertaking principle is re-interpreted in such a way that it preempts the creation of such groups. In this perspective, it should be conceived as enforceable at distant periods of time, not continuously. Between two enforcements, the WTO negotiation process should allow Members to "discriminate positively", that is, to open further their markets by participating in plurilateral agreements subject to MFN-consistent implementation without waiting for an agreement among all the Members – an extension of the approach suggested for services to other topics.

A key side-benefit of the positive discrimination approach would be to reduce the pressure imposed on the WTO system by its vastly enlarged membership. By definition, plurilaterals will involve a lower number of countries. This will dramatically change the level of nuisance that reluctant countries can exert on the whole system. The lower the critical mass of signatories imposed for giving birth to a plurilateral agreement is, the easier it will be for the plurilateral to avoid to be hostage of reluctant negotiators.

Of course, a "positive discrimination" approach would require several clarifications. Firstly, which could be the topics concerned by a positive discrimination approach (a question to be approved by all WTO Members)? An obvious candidate is public procurement (already under this approach). By contrast, tariff cuts in industrial products should still involve all the Members because it is the core of the multilateral trade regime since five decades, and all the more because a subtle use of the formula approach can provide all the necessary flexibility. Secondly, how much time would lapse between two enforcements? There is no a priori answer to this question. It depends on the boldness of the liberalization moves made by the coalitions of the willings, and on the winds of bilateralism vs. those of multilateralism.

K. Mellowing the bilaterals: Multilateralizing the Rules of Origin

The above suggestions should greatly reduce the attraction of bilaterals in general. By targetting protection peaks in goods and services, they should particularly cut the ground under the bilaterals focusing on trade preferences – the most costly type of bilaterals for the signatories as well as for the multilateral trade regime. That said, bilaterals are unlikely to disappear totally, if only because some of them have a political dimension that the WTO will never be able to cope with. There is thus a need to reduce the harm that existing and future bilaterals could do to the WTO trade regime.

The rules of origin imposed by bilaterals are generally seen as the biggest source of problems created by these deals [Baldwin 2006, Cadot 2006]. [21]/ "Multilateralising" these rules seems the best way to significantly reduce these costs. It is a hard task because the many criteria defining the rules of origin (tariff schedules, tariff level, content level, sectoral specificities, etc.) change from bilateral to bilateral [Cadot and de Melo 2006]. "Harmonising" the rules of origin seems largely out of reach in the short and medium run, except around hubs (the EC or the U.S.) with the risk that such hubs have substantial perverse effects.

As a result, the most accessible option for multilateralising the rules of origin seems to rely on the notion of "equivalent" tariffs, that is, tariffs close enough to each other for having no noticeable differences in their economic impact [Wonnacott 1996]. The lowest key version of this option would be to consider all the tariff lines with tariffs comprised between 0 and (say) 5 percent enforced in the world as equivalent, so that all the products subjected to such tariffs would be considered of "domestic" origin. A more ambitious version would be to define all tariff lines with tariff preferential margins smaller than (say) 5 percent as equivalent. It is useful to observer that both versions have the additional advantage to induce WTO Members to shift their tariffs close to the ceiling tariff inside the tariff band.

IV. Concluding Remarks

There is no way to impose the above described effort on WTO negotiators. But, the six proposals support each other, so that each of them could be used more gently, a feature favoring compromises. None of these proposals infringe the basic principles of the current multilateral trade regime. They merely re-assess the current interpretation of these principles.

Who could be the "agents" of such an effort? An easy answer is the U.S., Japan and the EC, still the three largest economies and those with the longest experience in the WTO. Indeed, there are already proposals in this direction [Atlantic Council 2007] and key politicians have launched ideas in this direction (German Chancelor Merkel, U.S. Senator Baucus).

However, if these countries are necessary, they are not sufficient. The current balance of forces in the WTO forum and a really business-friendly perspective require a broader support which requires an active role from medium-size economies. For obvious reasons, the GATT/WTO history has always focused on the largest players, with the U.S.-EC "tête à tête" of the 1960s to the 1980s, the Quad (Canada, EC, Japan and the U.S.) in the 1980s and 1990s, and the Five (or Six) Interested Parties, the last incarnation of this tendency before the pre-Hong Kong Ministerial. However, in the past, the role of the medium-size economies has always been essential for moving the GATT/WTO process at critical times. Australia, Canada, Columbia, New Zealand, Sweden, Switzerland, etc., have often been critical for preparing crucial deals. Asian medium-sized economies, such as Korea for instance, should join the group.

The paper has focused on the WTO per se. But, as well known, the success of WTO negotiations – and of trade liberalisation – ultimatly depends on the domestic forces working in the Members. A strong domestic support is essential to a more efficient WTO negotiating process. Such a support should not be stated only in general terms (average tariff cut, gains from trade and domestic regulatory reforms, etc.) as it is too often today, because such terms are difficult to grasp by the public opinion.

[21] / Paradoxically, strict rules of origin may be positive from a WTO perspective because they limit so much the impact of the bilaterals that their signatories ultimatly have to have recourse to the existing multilateral trade regime. However, this argument is limited to the bilaterals focusing on trade-preference, and it ignores the fact that strict rules of origin generate a high level of frustration which ultimately hurts the WTO regime as well.

Rather, domestic support should focus on providing the best possible, most concrete information on the highest domestic barriers – be the peak tariffs on imports of goods, the most inefficient regulations in services, the highest subsidies in goods and services, etc. Paradoxically, and ironically, a support focused on peak protection would also help negotiators. For instinctive reasons, trade negotiators tend to ask more from their trading partners than their own businesses. For instance, European negotiators have insisted on tariff cuts from the emerging economies in NAMA much larger that those requested by the EC businesses [Messerlin 2007].

A focus on peak protection would help to dissipate a frequent misunderstanding in the public opinion – that protection is in the "public interest" whereas freer trade favors narrow-minded "private interests". After all, economic analysis, history and good political sense suggest that, by definition, protection is keeping the statu quo situation, hence that it can only favor the most powerful groups in place, at the detriment of the infant economic and social forces. For instance, the debate on agricultural protection has profoundly changed in Europe since the 2001 Doha Ministerial, when it has shifted from generalities on farm liberalization to a very concrete point, that is, the largest beneficiaries of the current protection. As a result, not only Europeans are in favor of serious cuts in subsidies (including in France) [German Marshall Fund 2006] but the most dynamic European farmers are beginning to distance themselves from the existing CAP.

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Annex 1. Why Have Small Countries Led the Bilaterals Game So Far?

The continuing attraction for bilaterals has another source than the pure economic costs and benefits to be expected from them which have been underlined in section 2. It flows from political economy considerations based on the domestic costs and benefits of concluding bilaterals relative to those of concluding WTO deals. This approach is interesting because it offers an explanation of the leading role of the small countries in the post-1995 bilaterals documented by Table 1 – a fact that the economic analysis of regionalism based on "optimal tariff" is not able to cope with.

The balance of domestic forces in a small country are likely to be the same, or even to be more favorable, in the case of a bilateral than in the case of a WTO deal. The small country's import-competing industries are likely to face roughly the same competitive forces in the case of a bilateral with a large country than in the case of a WTO agreement because the large country producers are roughly as efficient as world producers for a wide range of goods. Meanwhile, the small country's exporters are likely to perceive a bilateral as providing them as many as (or possibly even more) export opportunities than a WTO agreement for two reasons: the large country markets are large enough for absorbing their export capacities, and the bilateral may exclude their competitors – this last reason shifting the balance of domestic forces in favor of a bilateral, compared to a WTO deal, and pushing the small countries to be "leaders" in terms of bilaterals.

From a large country perspective, the domestic costs and benefits of a bilateral relative to a WTO deal are quite different. A bilateral subjects the import-competing industries of the large signatory to a much more limited competition than a WTO deal, and it provides much more limited opportunities for the domestic exporters than a WTO agreement. In sum, a bilateral with a small country may simply get unnoticed in the large country, hence their tendency to be "followers".

Going beyond pure trade interests, bilaterals can be attractive for three other reasons. Firstly, they are a much more malleable foreign policy instrument than a WTO deal. Many negotiations on trade bilaterals have been launched on the assumption that they will strengthen infant political relations, or that they will rejuvenate fading political relations. Once again, this feature is likely to reinforce the leading position of the small countries – it is much more rewarding for a small country to talk to a large country than the converse. By contrast, the WTO is a place where political considerations are "dissolved" by the non-discriminatory principle. This feature may be very useful in specific cases (for instance, the accession of Iran to the WTO allows to avoid direct talks between the U.S. and Iran while still opening their markets to each other). But, the WTO can hardly be helpful for smoothing the ups and downs of the day-by-day international relations.

Secondly, bilaterals are also a much more malleable domestic policy instrument than a WTO deal. Trade Ministers are generally junior ministers with little or no control over the country's global political agenda – be the timing of the liberalization programme, the scope of the industries to be covered, the balance of the domestic interests to be included, etc. [22]/ Bilaterals fit much better the limited power of Trade Ministers (and their hope for more prestigious ministerial portfolios) because they offer more freedom than WTO negotiations in managing the timing and the marketing of the deal, in carving out its coverage and defining the domestic interests to be involved. By contrast, WTO negotiations are hardly manageable in terms of timing, they are exposed to negatively-charged media, hence difficult to handle by the junior Trade Ministers, and their scope is hardly under control since it has to accommodate a large number of Members.

Lastly, bilaterals have the formidable capacity to include "trade-related" issues which are too contentious to be easily managed in the WTO. These so-called "WTO Plus" issues range from intellectual property rights enforcement to geographical indications to competition policy, etc. The capacity of bilaterals to deliver WTO-Plus provisions may be their Achilles' heel for two reasons. Firstly, "WTO-Plus" provisions included in the bilaterals tend to be much stricter than the similar WTO provisions [Fink and Reichenmiller 2005]. Indeed, they are often introduced by the large signatory with the hope to re-import them into the WTO forum. Secondly, the implementation of WTO-Plus provisions may be more closely monitored by tailor-made provisions included in the bilaterals. As a result, "WTO-Plus" provisions in bilaterals can be easily perceived as a "neo-imperial" approach pursued by the large country, all the more because they generally deal with truly domestic "behind-the-border" policies.

[22] /There are exceptions, such as Australia or Chile, where trade policy is so much intertwined with foreign policy that it is handled by the Ministry of Foreign Affairs. In the case of loose federal unions (such as the EC) bilaterals offer to the Trade Ministers of the union's Member States room for autonomous initiatives.

In sum, taking into account the above trade and non-trade interests suggests that negotiations on bilaterals between a small and a large countries are likely to be successful. However, this conclusion faces limits. The two first ones concern mostly the small signatories. Bilaterals have difficulties to handle crucial "rules" problems, such as subsidies (it is impossible to design subsidies so that they would have no impact on specific trading partners, as best illustrated by the severe difficulties faced by Mexico with subsidized U.S. maize) and they create a huge source of problems when enforcing the rules of origin. The "neo-imperial" dimension of the WTO-Plus provisions creates serious risks of bitterness and conflicts in the small signatory, as illustrated by the TRIPs dispute between Thailand and the U.S., or by the recurrent disputes between the EC and Turkey. The third limit concerns mostly the large signatories. The tiny costs and benefits of the bilaterals with small countries are not for them an insurance against sudden and violent oppositions from domestic stringy vested interests which may have the sufficient magnitude to stop (or at least endanger) the envisaged bilateral, as best illustrated by sensitive farm or food products (such as sugar, bananas, tuna, etc.).

This discussion deserves a final remark. The above arguments suggest that bilaterals between a large country and a "not so small" country are doomed to be much more difficult, as best illustrated by the EU-Mercosur negotiating saga or by the U.S.-South Africa case. This is because the domestic balance between the relative costs and benefits of bilaterals compared to WTO negotiations is likely to be negative in both countries. In the large country, import-competing industries may fear, with good reasons, that the competitive pressures of the "not so small" partner's exporters could be as powerful as those generated by full scale WTO negotiations (if the not so small country's exporters are among the most efficient in the world, such as Brazilian sugar producers) triggering the same strong opposition to a bilateral than to a WTO deal. And the large country export interests are likely to continue to find the market access opportunities offered by the bilateral much less interesting than those provided by a WTO deal – simply because the markets of the not-so-small partner may still be significantly smaller than the world markets available with a WTO deal. Meanwhile, in the "not-so-small" country, the exporters' lobbies may find the large country's markets not large enough for their export capacities, whereas the import-competing lobbies may be as afraid of the large country's competitors as of those from the entire world.