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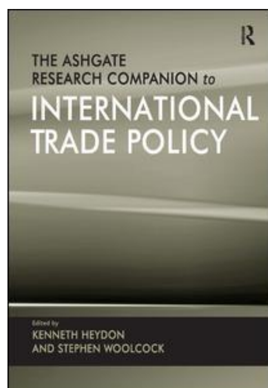

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The Political Economy of International Trade

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The Political Economy of International Trade

Kenneth Heydon

Introduction

Through successive General Agreement on Tariffs and Trade (GATT) rounds, extensive unilateral liberalization and the liberalizing effects of global supply chains, international trade has become more open. But much remains to be done and the job is getting harder. This chapter examines why. The first section looks at the recent record of market opening, before an examination, in the second section, of the political economy of trade liberalization's concentrated costs and dispersed gains. The third section addresses some new challenges facing trade policy – multi-polarity and bilateralism, increased complexity, and the role of non-state players – and suggests that their importance stems from their linkage to the 'old' issue of the political economy of trade. The chapter concludes with some suggested ways forward – most importantly the need to place trade policy firmly within the overall framework of sound domestic economic management.

The Job gets Harder: Resistance to Liberalization

Economic analysis has long established free trade as a beneficial economic policy. Douglas Irwin has even claimed that free trade has achieved an intellectual status unrivalled by any other doctrine in the field of economics (Irwin 1996).

Moreover, there is clear evidence of past movement towards freer trade. A series of multilateral negotiations under the GATT saw industrialized countries' average tariff on manufactures come down from close to 40 per cent in 1947 to under 5 per cent at the close of the Uruguay Round in 1994. Many countries, particularly developing countries of south-east Asia and South America, have engaged in unilateral trade liberalization (Sally 2008). And the two major financial crises of recent times have failed to trigger the protectionist responses that many feared.

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Recovery from the Asian Financial Crisis of 1997–8 was facilitated by export-driven growth as markets stayed open. And in the global financial crisis of 2008–9, the share of the value of trade covered by new direct trade policy instruments amounted to only 1 per cent of world imports (WTO 2009). Commitments to stay open to foreign products and services and concerns to keep global supply chains open – effectively lowering the optimal tariff (see Chapter 11) – together with the disciplines stemming from the WTO's rules-based system, helped countries to resist protectionist pressures (OECD 2010).

Yet, notwithstanding the support for the principle of free trade and evidence of progress towards its realization, the job remains incomplete and appears to be getting harder. Trade in agriculture and in sensitive areas of manufacturing is subject to tariff peaks and tariff escalation, as border impediments rise with higher degrees of processing. Where countries have unilaterally reduced their tariffs, this has often been accompanied, as in the case of India (Panagariya 2008), by increased resort to non-tariff barriers, such as antidumping action. Behind-the-border distortions such as domestic subsidies and local preference in government procurement abound. And a plethora of domestic regulations serve to impede international trade in services.

We thus see that during the global financial crisis, the share of imports affected by direct trade policy instruments was very high in selected sectors, reaching 36 per cent and 29 per cent respectively in the agricultural sector and the base metal industries. In the course of the crisis, a significant number of non-tariff measures (NTMs) were activated to restrict trade, such as the tightening of licensing requirements, safeguard measures and antidumping investigations, with developing countries accounting for 80 per cent of all antidumping initiations in the period October 2008–October 2009. And the crisis triggered widespread resort to behind-the-border trade-related measures. One-third of Organisation for Economic Cooperation and Development (OECD) countries offered some form of financial support to their motor vehicle industry and a number of countries incorporated preferential treatment in public procurement as part of their macroeconomic stimulus packages (OECD 2010).

While it may be argued that periods of acute crisis are not the norm, the trade policy response to the crisis of 2008–9 serves to highlight the vulnerability of open markets when political sensitivities are at their sharpest. Moreover, during a much longer period, there has been a marked failure to advance the Doha Development Agenda (DDA). Experience with the DDA serves to demonstrate the pervasive reluctance to further liberalize trade.

In July 2007, major players declined to commit to disciplines that were less onerous than the status quo, whether in agriculture, where the United States refused a domestic support cap of $13 billion though current outlays were only $11 billion, or in non-agricultural market access (NAMA), where Brazil refused tariff bindings that would have required no change in levels of protection. The situation was ripe for a continued standoff.

The standoffs came in many forms. Most critically, some parties (including the agricultural protectionists) showed reluctance to move further on agriculture

until others moved on services and NAMA, while other parties (including some developing countries) baulked on services and NAMA until they saw progress in agriculture. Japan resisted agricultural liberalization without assurances that there would be matching action in the rules area, notably that antidumping disciplines would be strengthened. There were also standoffs within sectors, as in services for example, where developing country expectations on mode 4 (the 'presence of natural persons', or the short-term movement of service providers) were pitted against developed country expectations on mode 3 (the supply of a service by one Member 'through commercial presence in the territory of any other Member') (see Chapter 9). Nor were standoffs an exclusively North–South affair. In agriculture, US demands that the EU do more on market access were matched by EU demands that the United States introduce more discipline on its domestic support.

The WTO ministerial meeting of 21–30 July 2008 moved some way in turning standoffs (I will do nothing on agriculture until you do something on NAMA) into trade-offs. However, the trade-offs tended to be negative (I will let you exclude X from liberalization if you let me exclude Y) rather than positive (I will liberalize X if you liberalize Y). The result of the mutual lowering of ambition was that in the end the potential deal was not worth fighting for. For example, allowing the special safeguard mechanism in agriculture to be triggered by an import surge of only 10 per cent, as sought by a group of developing countries, would mean that 82 per cent of China's food imports and 64 per cent of India's would be subject to a tariff as high as 30 percentage points above pre-Doha bound rates.

Why is progress so difficult?

The Political Economy of International Trade: Understanding and Responding to an Old Problem

The underlying failure in recent years to advance multilateral trade liberalization stems from insufficient political will to confront the vested interests benefiting from the rents of protection.

The Political Impediments to Open Markets

Trade liberalization yields overall benefits to the liberalizing country. But because it causes domestic prices to converge on those applying in the international market, the resulting change in relative prices within the domestic economy affects the returns to different factors of production – whether wages in different sectors, wages at different skill levels, or returns to capital. There are winners and losers. The politics of trade is then highly dependent on two key factors: the relative size of the stakes of winners and losers and the respective ability of winners and losers to organize and defend their interests.

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Political influence tends to be greater for those seeking government assistance or protection because those who stand to gain have more at stake than those who stand to lose. In the words of Vilfredo Pareto, 'a protectionist measure provides large benefits to a small number of people, and causes a very great number of consumers a slight loss' (Pareto 1971: 379). The validity of this observation is amply demonstrated by recent experience with the Common Agricultural Policy (CAP) of the European Union. In 2009, 1,212 individual recipients received at least one million euro in CAP support (farmsubsidy.org cited in Bridges 2010). The number of beneficiaries is impressive, but it is dwarfed by the number of consumers living in the EU27 – close to 500 million.

Relatively concentrated groups, whether geographically, by number of enterprises or by subsector (the top CAP beneficiaries are predominantly sugar producers), are also better placed to meet the costs of collective action by monitoring political contributions or excluding free riders (Olsen 1965). This observation helps to explain the urban–rural tensions in many developing countries, not least in Africa, where a well organized and politically active manufacturing sector benefits from protection and overvalued exchange rates, at the expense of the politically disorganized agricultural sector, despite the comparative advantage in agricultural goods (Bates 1981).

It is these two elements of the political economy of international trade – the concentrated benefits of protection and the organizational strength of well-focused groups – that helps explain the enduring feature of protection: once protective policies are in place they are very difficult to change (Irwin 2002). Hence the unwillingness of trade negotiators, from both developed and developing countries, in the course of the Doha negotiations to move away from the status quo. It is these elements that also explain why, in very broad terms, resistance to reform and market opening is particularly acute for developed countries in the area of agriculture and for developing countries in the areas of manufacturing and services.

In recognition of the political impediments to free trade, and consistent with the writings of the Political Capture theorists, attempts have been made to shelter the process of trade policymaking from the influence of sectional interests and to prevent financially powerful groups from prejudicing the interests of the majority (Alt et al. 1996; Cohen et al. 2003; Destler 2005; Krasner 1976; Rogowski 1989; Stigler 1971, 1974). Hence in the United States, the Trade Act of 1974 introduced a 'fast-track' procedure whereby Congress would vote expeditiously on trade legislation without the possibility of amendment. According to Access Point theory, such delegation to the president makes it harder for interest groups to lobby policymakers (Ehrlich 2008). And in the EU, the Treaty of Rome delegated to the European Commission the implementation of trade remedies and the conduct of negotiations.

As the country chapters in this volume show, these attempts have had only mixed success. The question then arises: what might be done to address the challenge arising from the political economy of trade? Attention here will focus on three requirements: communicating the benefits of open markets, helping those who lose, and putting trade policy in a broader context.

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Communicating the Gains from Trade

Communicating more effectively the gains from market opening means resolving the problem, identified in behavioural economics, of 'bounded rationality' or the tendency to avoid policies that are rational but counterintuitive (Brennan 2007: 137). It is not immediately obvious that exposing domestic producers to more intense competition will yield overall benefits to the economy. But this indeed is the case.

If we think of a continuum – trade, innovation, growth – then, while the link between innovation and growth is fairly well understood, the link from trade to innovation (and hence to growth) is less so. There are four channels through which trade stimulates innovation, involving a mixture of market opening and the strengthening of trade rules (OECD 2007a).

- Increased competition: a number of studies find that trade openness makes markets more competitive, reducing prices and raising incentives to innovate (Licandro and Navas 2007) while also raising productivity (Melitz and Ottaviano 2005). Bigsten et al. (2004) have shown that trade can also improve productivity through efficiency gains from learning by exporting. There is recent evidence that stronger competition has particularly powerful effects on productivity in countries far away from the technological frontier, reflecting stronger incentives to adopt new technologies (OECD 2007b). Underpinning these observations is the work of Robert Solow pointing out that there are two components to productivity growth (Ten Raa and Mohnen 2008): a Schumpeterian technical change element centred on the more efficient use of *capital* (Schumpeter 1954), and a neoclassical efficiency change element centred on the more efficient use of *labour*.
- Technology transfer: trade, particularly when accompanied by foreign direct investment (FDI), is likely to promote the transfer of skills and innovation. Beyond this direct transfer of technology embodied in trade, or as spillovers from trade (Nordas et al. 2006), there is also an indirect contribution as trade serves to lower prices and hence the cost of accessing such embodied technologies. In short, trade allows firms to access technologies that are essential for improving their productivity and competitiveness.
- Economies of scale: companies producing for both the domestic and foreign markets are better able to recoup research and development (R&D) investments over a larger quantity of sales than if selling only for the domestic market.
- Globalization of value chains: trade and trade reform can help foster the global fragmentation of production processes. They do so in a number of ways: by promoting harmonization around international technical standards to which firms in fragmented value chains must conform; by addressing the danger that restrictive rules of origin (designed to ensure that only imports from partners in bilateral or regional Preferential Trade Agreements (PTAs) have preferential access) will disadvantage low-cost suppliers within the chain; and by encouraging trade facilitation, enabling suppliers to respond quickly to developments further down the value chain.

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In summary, despite differences of opinion on the strength and the direction of causality, there is strong analytical support for the view that openness to trade, backed by stronger trade rules, generally leads to welfare gains (Dollar and Kraay 2002; Winters 2004). Putting numbers on this is difficult, but there is evidence that an increase in the share of trade in gross domestic product (GDP) of 1 percentage point raises the income level by between 0.9 per cent and 3 per cent (Nordas et al. 2006). Economies with more open trade policies tend to perform better than those with more restrictive trade policies, as evidenced by the experience of South Korea and Taiwan, which began to liberalize their trade policies in the 1960s, Chile, in the 1970s, and China, India, Mexico and Vietnam, which undertook measures of market opening in the 1980s and 1990s.

But there is a fourth element in the continuum: trade, innovation, growth and *poverty reduction*. Economic theory tells us that trade should contribute directly to reduced poverty in developing countries through the process whereby trade increases the returns to the most abundant factor of production, which in developing countries tends to be low-skilled labour. The fact that income inequality has risen in most countries over the past two decades is due more to technological progress increasing the wages of skilled relative to unskilled workers, than to trade (Billmeier and Nannicini 2007; Cling 2006). As we have seen, some technological innovation will of course be undertaken in response to the intensified competition arising from trade. But this is nevertheless likely to represent a relatively small – though still significant – proportion of overall technological change. It has thus been estimated (Bloom et al. 2011) that between 2000 and 2007, 15 per cent of technology upgrading in Europe can be explained as a response to competition from China.

Recent events have underlined the importance of the trade link to productivity improvement. The unprecedented fiscal expansion in response to the 2008–9 global financial crisis and associated debt only add to the existing long-term imperatives for increased productivity growth needed to address demographic ageing and greenhouse gas abatement and other costs. Productivity growth can help service the debt now accumulating from fiscal deficits, as well as offset the effects on future income of withdrawal of governments' stimuli from consumer spending (OECD 2010; Productivity Commission 2009).

The other side of the gains-from-trade coin is the cost of protection. Following the work of Max Corden, this cost is now commonly addressed in terms of the effective rate of protection (ERP) (Corden 1966). The ERP calculates the effect on the returns to labour and capital in an industry of the use of tariffs and other forms of assistance by measuring the entire structure of protection, taking into account the effect of tariffs and NTMs on inputs (raw materials and intermediate products) as well as on outputs. The higher the tariffs and NTMs on imported inputs, the lower the ERP will be for the goods that use those inputs (Hoekman and Kostecki 2009). When allowance is made for the effect of restrictions on the import of services – and hence on services as an input – the results are striking. It has been found that when account is taken of barriers to services imports, the ERP for motor vehicle production in Brazil actually becomes negative: the protection of both services and non-services inputs results in the effective taxation of this industry (Dihel and Dee 2006).

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It is analysis such as this that underpins the broader, and no less striking, proposition that a tax on imports is a tax on exports, both directly, as the cost of inputs increases, and indirectly, as the reduced incentive for import-competing industries to contain costs spreads to the economy at large. But exporters are generally unable to pass on any cost increases. They will either lose export sales or become less profitable. Either way, jobs will be lost.

There is thus a weighty body of analysis in favour of open markets. The challenge is to communicate effectively this analysis, through all channels available: through government agencies, such as the Productivity Commission in Australia; through communications of the international agencies, such as the Trade Fact Sheets prepared by the OECD (OECD 2009); and through dissemination of the academic literature. What these channels share in common is that they engage organizations that are concerned with improving the welfare of the community at large, rather than of sectional interests within it (Olsen 1982).

Helping Those Who Lose

Public acceptance of the case for open markets requires more than simply demonstrating the gains from liberalization. It also calls for acknowledgement that there are losers as well as winners from market opening and that support will be given to those who lose – support that will be less costly than the protectionist alternative (Bhagwati 1988).

In principle, such support should rely on economy-wide action, in order to treat individuals in similar circumstances equally, to provide assistance to those in genuine need and to avoid compounding distortions in the economy (OECD 2005; WTO 2008). In practice, however, experience suggests that successful episodes of trade-related structural adjustment have almost always involved some measure of sector-specific assistance. Recalling the Pareto principle of concentrated gains from protection and hence concentrated costs of liberalization, targeted assistance may be called for particularly where structural decline in a particular sector causes geographically concentrated job loss beyond what existing labour market programmes can cope with.

The United States Trade Adjustment Assistance (TAA) legislation, appears to have been the source of innovative practices related to the provision of earnings-replacement benefits, such as the wage insurance programme introduced in 2003 (Kletzer and Rosen 2004). But the economic rationale of TAA has been controversial because it is not evident that trade-displaced workers should receive more adjustment assistance than other job losers. A similar scheme in Australia was abandoned for the same reason (OECD 2005).

Should governments consider it necessary to target assistance in particular cases, experience suggests that problems of both equity and efficiency will be minimized to the extent that such assistance is: time-bound, with a clear exit strategy; decoupled from production with incentives to adjust and innovate; aimed at re-employing displaced workers; compatible with general safety net arrangements;

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and transparent and accountable (OECD 2005. See also Evans-Klock et al. 1998; Kaivanto 2007; Leigh 1990; Winter-Ebmer 2003).

Putting Trade Policy in a Broader Context

As well as communicating the gains from market opening and helping to compensate for the losses, an effective response to the challenge of the political economy of trade will also require that trade policy be seen in a broader context. Advancing *multilateral* trade liberalization – whether in the present round of negotiations or within the continuing work programme of the WTO – will, somewhat paradoxically, necessitate placing trade liberalization more firmly within the framework of *domestic* economic management.

This idea was well articulated some 25 years ago by former Australian Prime Minister Robert Hawke who, while calling for the launch of a new GATT round, spoke of the need:

> for trade policy to be seen more as an integral part of broad domestic economic management and less exclusively as the subject of international negotiations. (Speech to the Centre for European Policy Studies in Brussels, 4 February 1985, cited in Snape et al. 1998: 415)

The idea was later elaborated by the OECD, in observing that:

> The benefits of a liberal trade regime will only be fully realised in an economy with appropriate macroeconomic policies, efficient labour markets and a regulatory environment which facilitate mobility of workers and the entry and exit of firms, and an education system which enables skills to match evolving needs. (OECD 2005: 16; see also Sally 2008: 91)

In short, market opening works best – and maybe only works at all – in a coherent, holistic policy environment that facilitates the movement of labour and capital from declining to expanding areas of activity. While trade liberalization is positively linked to growth, it is associated with a lower standard of living in economies that heavily regulate new entry or impose high costs on exiting or downsizing (Bartelsman et al. 2004; Bolaky and Freund 2004; Hoekman and Javorcik 2004).

Placing trade policy in its broader setting is another way of saying that *trade cannot do it all*. And here we are reminded of the crucial point identified by Jan Tinbergen that for policy to work there must be as many independent effective instruments as there are feasible targets (Tinbergen 1956). This highlights the challenge faced by the poorest countries where the entry of new firms calls for 'effective instruments' in the provision of human capital and bank finance – each of which, as Joseph Stiglitz has pointed out, may be in serious short supply (Stiglitz 2002: 59). But this is an argument for policy action in those areas of deficiency, backed by necessary development assistance, not for forgoing the benefits of more

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open markets. Similarly, when developing countries' trade-related adjustment is complicated because they are dependent on tariffs for revenue, the answer is not to forgo the benefits of their own liberalization but to broaden the tax base, as many developing countries have managed to do (OECD 2005).

Through this wider lens, trade reform can be promoted as one of a number of tools of growth and development rather than as a concession paid to others. Something of this spirit prevailed in Australia in the 1980s, when each of the three policy elements discussed here was evident (see Box 2.1).

Box 2.1 The political economy of Australian trade liberalization

During the 1980s, Australia, on a largely unilateral basis, began successfully dismantling protection of highly sheltered sectors, such as automobiles, dairy, shipbuilding and textiles and clothing. Market opening – and consequential improvements in productivity and growth – was facilitated by action in the three key areas identified in this chapter.

Communicating the gains was effected by:

- the Industries Assistance Commission (later the Productivity Commission) playing the role of Mancur Olsen's 'encompassing organization' by fostering a culture of evaluation (Messerlin 2006), demonstrating the economy-wide benefits of reduced domestic protection;
- the public advocacy of a strongly reformist Prime Minister, Robert Hawke, and Treasurer, Paul Keating, and their close personal advisors, working hand-in-glove with the permanent bureaucracy, thus effectively combining the top-down and bottom-up drive for reform; and by
- the public support given to liberalization by those emerging sectors – notably in services – which stood to gain and which served to weaken the lobbying power of traditional protectionist forces in the Country Party.

Helping losers and encouraging structural adjustment saw transitional budget support given to textiles and clothing producers to help them compete in a low-tariff environment; time-bound and decoupled assistance (see Chapter 8) to dairy farmers to compensate for adjustment-related falls in the value of farm assets; and more rigorous eligibility criteria for shipbuilding bounties, designed to focus assistance on those enterprises most likely to succeed in the future.

Putting trade in a broader policy framework saw complementarities developed with *macroeconomic policy*, via the floating of the Australian dollar in 1983 and the real depreciation needed to cushion adjustments in the traded sector following reductions in protection. Supportive *labour market policies* were introduced, which, via the Accord with the trades unions, preserved the real depreciation and associated competitive benefits by discounting wages from full indexation. Fiscal policy saw a *broadening of the tax base*, including through the taxation of capital gains. *Regulatory reform* of inefficient government monopolies began the process of upgrading vital transport,

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communications and energy infrastructure. *Competition culture* was strengthened through the identification and correction of anticompetitive arrangements. And reforms were undertaken of the *education system*, including through changes to the basis of university funding.

Underpinning these domestic factors was an international environment conducive to reform, characterized by relatively strong growth, the implosion of the Soviet system, developing country abandonment of policies of import-substitution and the widespread embrace of the market economy.

Source: Edwards 1996; OECD 2005; Snape et al. 1998; Productivity Commission 2001.

A Changed Context: Understanding and Responding to Some New Challenges

Three new factors are often invoked as helping to explain why trade liberalization has become more difficult: the onset of multi-polarity and the growth of bilateralism; the increased complexity of issues; and the rise of non-state actors, accentuating concerns about a perceived race-to-the-bottom in trade-related areas. Each of these new factors will be considered briefly in turn, together with their links to the not-so-new underlying political economy of trade.

Multi-Polarity and the Rise of Bilateralism

The replacement of Cold War certainties with a more multi-polar world has had one decisive effect on the international trading system. Multi-polarity, by limiting the ability of the United States to control the agenda, has prompted a moderated US commitment to multilateral approaches to economic diplomacy and, correspondingly, to reduced US leadership of such approaches. Moderated US engagement has been compounded by ongoing American concerns about 'free riding' in the multilateral trading system, through application of the Most Favoured Nation (MFN) principle, and periodic US disenchantment with the dispute settlement system.[1]

A moderated US commitment to multilateralism has also been fuelled by the need to keep things simple given the transparency of US domestic politics and the requirement for the administration to engage and be accountable to Congress and to work within the constraints imposed by US domestic interests (Bayne and

[1] See Chapter 3 for more detail on the evolution of the trading system from a US-led to a multi-polar system.

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Woolcock 2011). The role of Congress and the need to be accountable to it have greatly contributed to the pursuit of bilateral deals, in the interests of simplicity.

The United States has not been alone of course in the pursuit of bilateralism. Preferential agreements have become the principal arm of trade diplomacy. Though political and strategic factors are often an important driver, PTAs are also widely seen as a way of dealing with the political economy of trade liberalization's concentrated costs and dispersed gains: by focusing on a narrow range of selected partners and thus making it possible to exclude politically sensitive sectors; by avoiding MFN commitments and alleged free riding; by securing reciprocity from partners; and by addressing perceived unfair competition linked to noncompliance with labour or environmental standards.

As well as diverting scarce negotiating skills away from multilateral efforts, bilateral arrangements can frustrate multilateral efforts in other ways: by creating vested interests against multilateral liberalization on the part of those benefiting from preferences; by weakening the incentive to negotiate multilaterally on the part of countries for whom excluded issues, like investment and competition, are particularly important and which can be addressed in bilateral agreements; by spoiling the atmospherics of multilateral negotiations by bringing controversial issues like core labour standards into the trade debate; and by complicating the agenda with a proliferation of rules.

But the dangers arising from reduced US leadership and the rise of bilateralism should not be exaggerated. The United States is still engaged. And bilateral deals through their ambition, particularly in the area of rules, 'can complement the multilateral system – but only if that system is itself robust – strengthening trade rules and bringing down MFN barriers so that the distorting effects of PTAs are held in check' (Heydon and Woolcock 2009: 260).

Increased Complexity: More Players and More Issues

It is frequently asserted that the multilateral liberalization of trade has become more difficult because of the greater number of participants and topics involved, and because of associated shifts in negotiating power and the emergence of new coalitions (Baldwin 2006; Gallagher 2008; Hurell and Narlikar 2006; Krugman 1997; Odell 2007). But it is not the increased numbers of players and issues per se that creates the challenge but rather the way in which the wider scope of the liberalization debate has changed the conception of gains and losses in the political economy of trade.

The WTO, which now (spring 2012) has 157 Members, is a more complicated place in which to do business than was the GATT in its early days. But the number of present Members is not greatly different to the 128 at the end of the Uruguay Round. Moreover, the new Members, who are essentially developing countries, have brought with them a record of, albeit qualified, unilateral liberalization. The challenge comes rather from the fact that the new Members, concerned about the development dimensions of trade and a need to redress perceived injustice, have

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come to place greater emphasis on the *relative*, as opposed to the *absolute*, gains from liberalization. The failure to advance in NAMA is due in no small measure to the concern of many developing countries to maximize their share of the gains from market opening even if it means forgoing greater absolute gains that would come from deeper own-liberalization – an outcome that is distributionally attractive but suboptimal in terms of efficiency.

The range of issues under active discussion has also become more complex. While the Uruguay Round introduced valuable frameworks for freer trade in agriculture and services, much of the actual job of liberalizing and of strengthening rules was left undone (Irwin 2002). At the same time, the debate has become much broader, with increased recognition of the importance of the conditions relating to FDI and competition policy for the conduct of trade.

But again, it is not the number of issues per se that creates the problem. The 2003 WTO ministerial meeting in Cancun is a case in point. Notwithstanding suggestions to the contrary (see for example Maswood 2007), the failure at Cancun was not the result of North–South conflict over an overloaded agenda. As the Cancun negotiations drew towards a close, it is true that the Africa Group was still demanding withdrawal from the negotiating agenda of all four Singapore Issues (investment, competition, government procurement and trade facilitation). However, with the agreement of the EU, the main *demandeur*, to remove all but trade facilitation, the Singapore Issues were no longer a deal breaker. The cause of breakdown lay rather in a well-established issue involving long-standing players. Luis Ernesto Derbez, the Mexican minister chairing the negotiations, brought the ministerial to a premature close not because of the new issues, but because he believed, from talks with representatives of the US Department of Agriculture, that there was no way that agreement could be reached between the United States and EU on agriculture, and therefore no prospect of movement in other areas, including NAMA and services. In short, failure at Cancun was the result of insufficient political will to tackle core business – the 'old' issue of the political economy of trade.[2]

Experience at the 2008 WTO ministerial meeting serves also to refute the too-many-issues argument. The chances of success at that meeting would have been enhanced, not weakened, by bringing in the opportunities from services liberalization and making more of potential cross-issue trade-offs (Diego-Fernandez 2008; Fergusson 2008).

The challenge of issue-complexity comes rather from the fact that the scope of the debate has changed. The pursuit of deeper integration has focussed attention on domestic issues such as sanitary and phytosanitary standards (SPS), technical barriers to trade (TBT) and intellectual property protection (Sally 2008; Wolf 2005). The notion of market access – including in the key areas of agriculture, manufacturing or services – has thus come to embrace behind-the-border policies and regulations, adding a new dimension to the notion of the costs of liberalization and intensifying concerns about national sovereignty and the political economy of trade.

2 Based on discussions in Cancun with officials engaged in the negotiations.

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The Complicating Role of Non-State Actors

Non-state actors, principally in the form of non-governmental organizations (NGOs), have in recent years become much more significant players in economic diplomacy (Bhagwati 2007; Robertson 2006). On occasion, NGO activity has been for the better, as when Oxfam drew attention to the damaging effects of US cotton subsidies on producers in sub-Saharan Africa (Alston et al. 2007) or when various medical NGOs urged changes to the Trade-Related Aspects of Intellectual Property Rights (TRIPS) agreement to facilitate developing countries' access to medicines. Some commentators even speak of NGOs as embodying disinterested objectivity, so raising both efficiency and legitimacy in the conduct of trade policy (Albin 1999; Pigman 1999; Scholte 1999).

Such views are misplaced. NGOs are themselves largely unaccountable. They are no substitute for the ballot box (Anderson and Rieff 2005; Henderson 1999). In Member-driven bodies, like the WTO, IMF or World Bank, it is the job of democratically elected governments to formulate and implement policy, and to take responsibility for it. 'The bedrock of the trading system is enforceable agreements *among states*, most of them embodied in domestic law' (Wolf 2005: 209 [emphasis added]).

On balance, NGOs have made it harder for governments to deal with the political economy of trade, by exaggerating the costs of market opening and questioning the gains. The campaign of disinformation about the supposed risks to national health, culture and education (Sinclair 2000) that would come from the liberalization of trade in services has been both unhelpful and wrong. The General Agreement on Trade in Services (GATS) enshrines the right to regulate and countries are totally free not to liberalize any sectors of their choice (OECD 2002). And NGO-urging that developing countries seek the removal of investment, competition and government procurement from the multilateral trade agenda was a pyrrhic victory. Conditions of investment and competition are now a vital dimension of market access and it is developing countries that suffer most from the often arbitrary and opaque allocation of government contracts.

In addressing the costs of market opening, NGOs have been particularly active in stressing the trade-related dimension of liberalization and the perceived dangers of a race-to-the-bottom as countries supposedly disregard environmental and labour standards in order to gain a competitive advantage. In fact there is no evidence of such a race-to-the-bottom and, rather to the contrary, strong analytical and empirical indications that trade and trade liberalization have served to improve compliance with both environmental objectives (World Bank 2000) and core labour standards (OECD 2000). But this, perhaps counterintuitive, view is not easy to convey. NGOs, by claiming the higher moral ground have, in the words of Jagdish Bhagwati, 'put the proponents of free trade into a battle that is harder than ever to wage' (Bhagwati 2002: 48).

The role of NGOs should not be exaggerated. It is the exercise of government will, or lack of it, that ultimately determines the success, or failure, of policy. But neither should the role be unquestioningly welcomed, particularly at a time when

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the pro-trade voice of business seems particularly mute. As multilateral negotiating cycles get progressively longer and product cycles get shorter it is not surprising that business is attracted to the promise – not always realized – of PTAs. The result is a mixture of fear and complacency – fear on the part of a public, ever more attentive to the critics of liberalization, and complacency on the part of a business community, ever more supportive of bilateral deals (Heydon 2006).

Concern about the challenges raised by these new issues has led to suggestions as to how they might be dealt with. These often amount to a policy of capitulation: bilateral PTAs would be embraced as an alternative to multilateral negotiation; growing complexity would be met by narrowing the scope of the agenda, lowering ambition or seeking agreements among subsets of the willing; and the increased presence of NGOs would be met by giving them a more formal role in the process of policy formulation.

The conclusions reached here are rather different. Just as an understanding of the political economy of trade helps us judge the significance of the new issues so it provides guidance on ways to deal with them:

- *Articulating more effectively the case for broad-based multilateral liberalization* would increase the chances that a strengthened multilateral system would foster complementarity with bilateral PTAs and that cross-linkage of trade topics would reduce the dangers inherent in a mutual lowering of ambition to the point where a multilateral deal is not worth fighting for (Sutherland 2010).
- *Helping those who lose* from market opening would allay many of the concerns expressed by non-state actors and obviate the need to give them a formal role in policy formulation.
- *And placing trade liberalization in its broader domestic policy context* would address the complexity of issues while ensuring that distinct objectives, such as those linked to the environment or social standards, were addressed directly by dedicated policies and not by misguided attempts to enforce compliance through restrictions on trade.

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