THE RECALİBRATİON OF INTERNATİONAL TRADE RULES UNDER WTO TO FURTHER ECONOMİC GROWTH: CHALLENGES AND PROSPECTS[#]

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Abstract

The system of international trade governed and regulated under the auspices of World Trade Organization (WTO) was built upon the basis of the Comparative Advantage Theory developed by 19th century economist, Davit Ricardo which has been heavily debated among commentators and economists. As the theory rested its credibility on the concept of perfect markets which is hardly the case for any markets in international trade, to what extent the existing legal system under the WTO built on a highly contested theory may suffice to ensure the effectiveness and feasibility of international markets has been an open question. This paper adopts a critical analysis on the application of the comparative advantage theory to trade among nations and provides prospects and proposals that address problems and inefficiencies within the international trade system.

Keywords: World Trade Organization, WTO, Economic Development, Comparative Advantage, Inequeality, Poverty, Domestic Market Failure, The Least Developed Countries, Developing Countries, Enabling Clause, General Agreement on Tariffs and Trade, GATT, External Market Failure, Most Favored Nation, MFN.

DÜNYA TİCARET ÖRGÜTÜ NEZDİNDE ULUSLARARASI TİCARET HUKUKU KURALLARININ YENİDEN DÜZENLENMESİ: ZORLUKLAR VE BEKLENTİLER

Özet

Dünya Ticaret Örgütü tarafından temsil edilen uluslararası serbest ticaret düzen, 19. Asır iktisatçısı David Ricardo'nun mukayeseli üstünlük kuramı üzerine inşa edilmiş olup, bahsi geçen düzenin günümüz ticari münasebetlere ve devletlerin küresel mali konumuna uygunluğu akademik camia tarafından tartışma konusu haline gelmiştir. Mukayeseli üstünlük kuramı geçerliğini kusursuz marketler modelleri üzerinden iddia etmekteyken, söz konusu modellerin mevcut ticari düzlemde karşılıklarının olmaması, bu kuram üzerine

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kurulan mevcut serbest ticaret sisteminin de etkinliği ve geçerliliği konusunda şüphe uyandırmaktadır. İş bu çalışma, mevcut serbest ticaret düzeninde mukayeseli üstünlük kuramının konumunu, kuramın bizzat kendisine yöneltilen eleştiriler ile birlikte sunmakta, ve merbut işlevsizliklere ve sorunlara yönelik olarak öneri ve beklentileri ortaya koymaktadır.

Anahtar Kelimeler: Dünya Ticaret Örgütü. DTÖ, Ekonomik Gelişme, Mukayeseli Üstünlük Kuramı, Eşitsizlik, Kıtlık, İç Piyasa Yetersizliği, Az Gelişmiş Devletler, Gelişmekte Olan Devletler. Yetki Hükmü, Tarife ve Ticarete ilişkin Genel Anlaşma. Dış Piyasa Yetesizliği. En Çok Gözetilen Ulus Kaydı.

I. INTRODUCTION

This paper is an examination of the relationship between international trade rules adopted under World Trade Organization (WTO) and domestic economic development. Developed under the Bretton Woods system, the WTO has been the main forum of international trade since 1947[1]. According to the Bretton Woods system, each country eliminating barriers to global trade flow for both of their exports and imports, will receive utmost benefit from globalization, and and thus be better off. This issue is well explained under theory of “Comparative Advantage”.

This system was highly inspired by the theory of Comparative Advantage, developed by the 19th century economist, David Ricardo. The theory asserts that when states liberalize their trade systems and eliminate any obstacles to international trade, they will increase their production capacity through specializing the production of those goods and services in which they have a comparative advantage. Consequently every country specializing its production through comparative advantage will be made better off in the sense that the general income and wealth of the countries will be increased.[2] The first paragraph of the preamble of the WTO recognizes the theory and states that “substantial reduction of tariffs and other barriers to trade” and “the elimination of discriminatory treatment in international trade relations are likely to contribute to raising standards of living and full employment while allowing for the optimal use of the world’s resources in accordance with the objective of sustainable development”[3].

Even though it is accepted among some economists that free trade has been successful for achieving the economic development goal, to what extent such an assumption is completely true is also contested.[4] Contenders of the comparative advantage focus on the models on which the theory built on and argue that an assumption that the openness to trade really benefits a country with a higher rate of economic growth has not applicable to all countries at all times and here are other factors to be taken into account other than international trade.

1 Even though the WTO was founded in 1995, its predecessor General Agreement on Tariffs and Trade has been operational since 1947. The underlying principles the GATT was built upon were later called Bretton Woods System named on where the final draft of the agreement was concluded.

2 Andrew T. Guzman & Joost H.B. Pauwelyn, International Trade Law 16 (Aspen Publishers, 2009).

3 Marrakesh Agreement Establishing World Trade Organization Preamble, para., 1.

4 Francisco Rodriguez and Dani Rodrik, *Trade Policy and Economic Growth: A Skeptic’s Guide to Cross-National Evidence* Working Paper (National Bureau of Economic Research, April 1999), http://www.nber.org/papers/w7081 337.

In Part One, the paper covers the applicability of comparative advantage theory to the current market conditions. In order to yield economic growth from free trade policy, theory requires some elements in both domestic and international level. Taking into account these elements, first, the paper addresses the "Domestic Market Failure" argument raised by the opponents of Bretton Woods system. According to the argument, not all of the domestic economies in the global system are operating properly as it is assumed in the main theme of comparative advantage theory. Question in this section is as to whether government intervention is required or not for a malfunctioning domestic industry. The proponents of free trade assert that free market without intervention of government is the best way to specialize domestic production tools and make them more effective and any intervention by government will distort the functioning of domestic markets. Opponents state that in case of imperfections in internal functioning, the pure comparative advantage theory actually harms production incentives and preferences in domestic economy. Second, there is a more contemporary debate about the free trade policy that global market conditions are far from justifying the contributions of comparative advantage. Supporters of this argument assert that in addition to the errors in the domestic economy, global market conditions are also different from the world David Ricardo lived. Emergence of new types of economic preferences and sectors renders the theory inapplicable.

In Part Two, this paper raises concerns on the distribution of wealth acquired through international trade. Again, comparative advantage theory does not say each individual in the domestic economy will be better-off. It, simply says that while some industries gain benefits from the liberalized trade, others may fall against more productive equivalent industries originated from other countries, but the gains of the former will compensate the loses incurred by the latter. The net economic growth would result in economic and social welfare. This is exactly where the distributional critiques are rising up. On the one hand, they attack the idea that free trade leads economic growth. On the other hand, they state that even if trade leads economic conditions in some circumstances, social welfare is a different concept and may not be acquired through such trade-off. According to the opponents, there is not any positive correlation between economic growth and social welfare. Income balancing within the domestic economy has hardly taken place and the gap between high and low income classes would widen, unless precautionary measures are utilized.

Part Three covers the WTO's approach to development. Recognizing the needs of developing countries within the global trade system, WTO applies some special and preferential treatments and measures for its developing members. In this part, first the organizational and provisional structures designed to assist development of developing countries are presented. Then the paper continues with the question; whether the current WTO system is successful in achieving the objectives addressed in its preamble. In this section several provisions are presented and the issues about the implementation of these provisions are examined. Finally, proposals about both organizational and provisional structure of WTO about development are covered and at the end of the paper, it concludes.

II. APPLICABILITY OF COMPARATIVE ADVANTAGE THEORY

The idea that there is a positive relationship between openness to trade and economic growth is widely accepted in North America and Europe.[5] Multinational institutions such as OECD[6] and IMF[7], and also highly acknowledged economists such as Anne Krueger[8] and Joseph Stiglitz[9] believe that trade is an important tool for promoting economic growth of developing countries.

The foundation of this though is the theory of comparative advantage. As it is defined earlier the theory says that free trade policy promotes the specialization of domestic production and states specializing the production of those goods and services, in which they have a comparative advantage, will enjoy the benefits of free trade through having economic development. However the theory rests upon the assumption that both importing and exporting countries have perfectly competitive markets with sufficient actors and prices reflecting the true costs of production in both international and domestic level.[10]

In this part, the paper provides arguments on negative effects of free trade involving both internal and external market failures. Although the main argument justifying both the ideology of trade liberalization and policy suggestions of WTO rests on the theory of comparative advantage, in reality, markets are far from perfectly competitive markets as the theory assumes The majority of WTO members consists of malfunctioning domestic economies and imperfect international market conditions which would render the theory inapplicable.[11]

A. Domestic Market Failure

According to the comparative advantage theory, market is the main determinant in identifying production incentives and preferences in domestic economy. Any government intervention such as subsidies and tariffs affecting these incentives and preferences are inefficient because they distort the theory by leading domestic economies to produce goods, in which they do not have a comparative advantage. The opponents of free trade policy, however, state that free trade policy is not desirable in imperfect market conditions and government intervention, which seems a

5 Francisco Rodriguez and Dani Rodrik, *Trade Policy and Economic Growth: A Skeptic's Guide to Cross-National Evidence* Working Paper (National Bureau of Economic Research, April 1999), http://www.nber.org/papers/w7081 337.

6 OECD. (1998). Open Markets Matter: The Benefits of Trade and Investment Liberalization. Paris: OECD. 1998**.**

7 IMF. (1997). World Economic Outlook, Washington.

8 Anne O. Krueger, *Trade Policy and Economic Development: How We Learn* Working Paper (National Bureau of Economic Research, January 1997), http://www.nber.org/papers/w5896.

9 Joseph E. Stiglitz and Andrew Charlton, *Fair Trade for All: How Trade Can Promote Development* (Oxford University Press, USA, 2006).

10 Joel R. Paul, "Do International Trade Institutions Contribute to Economic Growth and Development?," *SSRN eLibrary*, accessed November 11, 2012, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=468880, 3.

11 Carmen G. Gonzalez, "An Environmental Justice Critique of Comparative Advantage: Indigenous Peoples, Trade Policy, and the Mexican Neoliberal Economic Reforms," *SSRN eLibrary* (March 1, 2011), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1260048.

market distortion in perfect market conditions, actually can be an efficient way for balancing the consequences of market failures.[12]

The ways imperfections in a functioning of a domestic economy may vary, such as the existence of monopolies, oligopolies, lack of infrastructure, high capital costs, etc.. Any government intervention such as regulation, tariffs or quantitative restrictions may bring about benefits for domestic economy and development. For example it is common in most of developing and less developed countries, malfunctioning labor market conditions may require government actions. Subsidies to some labor-intensive sectors can be helpful for preventing the market producing more unemployment.[13] Accordingly, state intervention in those economic circumstances is actually fundamental to create comparative advantage in malfunctioning industries.[14]

Accepting the reality that economies we live in are not free from market failures, supporters of free trade develop two lines of defense for free trade. First they assert that domestic market failures can be corrected with a cost-benefit analysis at domestic level by internal policies aimed at sources of their problems[15]. For example, while a malfunctioning labor market, in a country, generates unemployment, a tariff may bring increase of social welfare by leading to additional production, despite its distortive effect on consumption. However, policy makers may come up with better ways, via efficient cost-benefit analysis such as domestic production subsidies, which for relevant products may also increase social welfare without increasing resale prices and decreasing demand for relevant products[16].

Second defense for free trade is the argument that it is very difficult to identify appropriate measures to be taken in response to market failure arguments[17]. For example, when there is a tremendous urban unemployment in a less-developed country, it is hard to prescribe a policy whose pros and cons many not be assessed easily. While a tariff measure to protect urban industry will draw the unemployed people into productive work and bring about social benefits, the same policy may result so much migration from rural areas to urban areas, thus it will increase unemployment. There are many ways in which markets can malfunction, and it is really hard to diagnose market failure well enough to prescribe policy.[18]

When it was first proposed, domestic market failure argument was thought that it would undermine much of the case for free trade. After all it is really hard to find a person who asserts that the world we live in is free from imperfections. However, difficulty of establishing the right trade policy supports the view in favor of free trade policy. Therefore it is recognized that domestic market failure should be corrected by internal mechanisms aimed at directly problems' resources.

12 Paul Krugman & Maurice Obstfeld, INTERNATIONAL ECONOMICS: THEORY & POLICY 214 (7th ed. 200).

13 *Ibid.*, at, 215.

14 Gonzalez, "An Environmental Justice Critique of Comparative Advantage", 762.

15 Krugman and Obstfeld, INTERNATIONAL ECONOMICS & THEORY, 215.

16 *Ibid*, at 216.

17 Krueger, *Trade Policy and Economic Development*, 4.

18 Krugman and Obstfeld, INTERNATIONAL ECONOMICS & THEORY, 217.

Because the a possible government intervention into the market may cause unintended consequences that worsens the conditions.

B. External Market Failures

A successful application of the comparative advantage theory requires the presence of perfect markets, defined as competition takes place in markets with abundant actors, no information asymmetry and no barriers to entry. The theory asserts that when both exporting and importing countries have perfectly competitive markets, elimination of trade barriers will yield benefits and economic growth among countries through lowering the costs of products to consumers who gain access to either less expensive imports or cheaper domestic production competing with external producers[19]. Opponents, however, argue that majority of goods and services in the world trade and global market conditions do not reflect to this assumption which is important for comparative advantage theory to work.

The global conditions of today's world are different than the one David Ricardo envisioned. Creating his theory in the early 1800s, and saying that free trade would produce shared gains for all nations, Ricardo assumed that main components of production such as soil, climate, geography and even the most workers could not be moved over international borders.[20] However, nature of international trade has changed and been changing. Today's vital factors of production –capital, technology and ideas— can be easily relocated to wherever they are most productive. For example, capital flows are substantially greater than the total volume of visible trade in goods and capital can move from jurisdictions with high labor costs to jurisdiction with lower labor costs more easily than which could do so in the era David Ricardo lived in[21].

Furthermore the world trade no longer consists of the flow of only tangible goods. In today's world, services including licensing, royalty fees, tourism, education, transportation and communication activities which may easily cross borders constitute a significant portion of world trade[22]. Today, more than 20% of the world's trade is made through trade in services.[23] Moreover, most economist believe that the actual import and export of services may be much greater than the official accounts. Services are generally traded at intra-firm level through telecommunication that defies government accounting and are not subject to custom valuation. Therefore, true rate of those services is expected more than the assumed rate of trade in services in world's trade.

Finally, a significant number of international markets are heavily concentrated. Large multinational enterprises control and dominate the access to foreign markets all over the world. [24] The Organisation for Economic Co-operation and Development (OECD) notes that more than 60% of World overall trade actually takes place among the subsidiaries of the same these large

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19 Paul, "Do International Trade Institutions Contribute to Economic Growth and Development?", 7.

20 Schumer, Charles and Paul Craig Roberts. 2004. "Second Thoughts on Free Trade," New York Times, 6 January, *available at* http://www.nytimes.com/2004/01/06/opinion/second-thoughts-on-free-trade.html

21 Paul, "Do International Trade Institutions Contribute to Economic Growth and Development?", 12-13.

22 *Ibid.,* at 12

23 World Trade Organization (Oct. 19, 2001) *available at* http://www.wto.org/english/news_e/pr249_e.htm.

24 *Ibid.,* at 10

multinational corporations[25]. Prices of products hardly reflect true market conditions of supply and demand as they are determined on the basis of intra-firm transactions which may aim at tax evasions and avoiding foreign exchange controls[26]. The concentration within the global market contradicts the market conditions assumed by the comparative advantage theory which requires that production incentives and preferences must be evaluated by a market in a great number of enterprises is present.

In contrast to the argument of domestic market failure, imperfection within the global market is relatively new debate on free trade. While suggesting the internal mechanisms to balance imperfection within the domestic market, supporters of free trade found themselves accepting that in international level, balancing the conditions in conformity with the comparative advantage is beyond the ability of internal mechanism. At the end, there are no longer shared gains by the theory but some countries win and others lose. Therefore, countries should reflect their policies to the senew realities.

III. INEQUALITY AND POVERTY

As noted above, the comparative advantage does not promise that everyone in a country will be better off because of trade. While the specialization of the production tools in accordance with the theory would bring about overall economic growth and social welfare, benefits from the industries that countries have comparative advantage would compensate losses incurred in domestic economy. In reality, this compensation almost never takes place, so the free trade policy that is supposed to increase prosperity for domestic economies, turns out widening the gap between rich and poor and resulting significant loss of social welfare. Conflict between opponents and supporters of free trade policy is not as to whether there is a distributional concern related to free trade. Both sides agree on the fact that comparative advantage has some distributional concerns that need to be dealt with. Where the both side at odds is that the nature and the extent of the policies that must be taken to deal with this inequality and to raise social welfare.

The idea that the inequality in the society diminishes, when the overall income raises is challenged by opponents. Even if, trade policies may have positive effects on economic development in some circumstances, they may not be correlated with the social welfare. Growth and welfare are not the same thing. Even if policies that restrict international trade were to reduce economic growth, it does not follow that they would necessarily reduce the level of welfare[27].

According to the opponents, international trade is the main contributor to the increase of both domestic and international inequality. In domestic side, trade is the main factor that while wealthy classes of society get the benefits of trade and become richer and conditions of lower classes are getting worse. A study by World Bank shows that domestic inequality increased in majority of countries, over 20 years period of trade liberalization[28]. In another study, the Bank also

[25] "Conning the Congo," *Greenpeace International*, accessed November 12, 2012, http://www.greenpeace.org/international/en/publications/reports/conning-the-congo/.

[26] Paul, "Do International Trade Institutions Contribute to Economic Growth and Development?".

[27] Rodriguez and Rodrik, *Trade Policy and Economic Growth,* 267.

[28] World Bank (July 7, 2000), *available at* http://www.worldbank.org/research/growth/pdfiles/squire.pdf.

finds that global income inequality increased 6% within half of last decade[29]. One example in Mexican corn industry,[30] after the North America Free Trade Agreement (NAFTA) came into effect, clearly illustrates the effects of international trade in domestic industry. After NAFTA, despite the severe decline of prices, corn production in Mexico did not raise. Farmers who want to keep income from corn stable, therefore, sought to reduce the number of hired labor working in the industry. This inevitably caused decreases at labor rate.

The NAFTA was also regarded as detrimental for social welfare in Mexico. Poverty and desperation that stemmed from the collapse of corn industry had many people and farmers migrate to urban areas and the United States. Every year, approximately 500,000 Mexican workers migrated from the rural areas and regions that have the highest levels of cultural diversity and corn agro-biodiversity. Such migration has threatened Mexico's genetic diversity and continuity of indigenous life style. Especially the migration of male workers also distorted the family and social structure that, most of the fields were left unplanted and women and children were forced to work the land, seek off-farm employment in order to supplement family's income. Result was tremendous social unrest including hunger strikes, civil disobedience and the replacement of corn production with marijuana.[31]

The assessment of winners and losers of trade liberalization in Mexican corn industry clearly shows that small and especially indigenous and traditional farmers and consumers in Mexico are the main losers of free trade. The elimination of tariffs and trade barriers to foreign agricultural products especially coming from the U.S., clearly destroyed the Mexican farmers' ability of competition and ruined the livelihoods of local communities. On the other hand, the main corn importers and the U.S agricultural enterprises that provided high subsidies from the U.S. government are the beneficiaries of free trade.

Effect of trade liberalization on the side of the U.S. economy, especially after NAFTA, is not also positive. Accordingly in 6 years period of implementation of the NAFTA, from 1994 to 2000, 1.9 million jobs in manufacturing in the United States were eliminated due to increase in imports.[32] Some manufacturing plants were forced to move to lower wage countries. Many industries relocated their business activity to low wage labor and non-unionized developing countries. In general, the fact that, workers who lose their jobs earn less when they are reemployed, explains the downward median wages in the United States during the period of increasing global trade flows.[33]

Supporters, however, assert that, in order to minimize this inequality, government should consider internal corruption and administrative problems[34] as well as some internal distributional

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29 World Bank (Feb. 2, 2002), *available at* http://poverty.worldbank.org/files/13254_Towards_a_better_understanding_of_the_global.doc.

30 For detailed information about the effect of accession to the NAFTA on Mexican Corn Industry *see;* Gonzalez, "An Environmental Justice Critique of Comparative Advantage."

31 *Ibid.*

32 Paul, "Do International Trade Institutions Contribute to Economic Growth and Development?".at 15.

33 I*bid.* at 18

34 Krueger, *Trade Policy and Economic Development*, 34.

and social protection mechanisms such as tax reforms, unemployment insurances or food-for-work schemes rather than regulating directly the trade policy and placing barriers to trade. Moreover, though having distributional consequences, openness to trade ultimately raises the overall income of the country[35] and an increase in overall income of a country would provide strengthened fiscal ability to deal with inequality.[36]

However the idea that trade increases overall income is also controversial. On the basis of a study by Sachs and Warner in 1995[37], which identifies globalized and non-globalized countries and is intensively cited by the supporters of free trade policy. World Bank in its report of *"Globalization, Growth, and Poverty: Building an Inclusive World Economy",* analyses four countries (China, India, Vietnam, and Uganda) identified them as star globalizers indicating that these countries greatly increased their integration with the world market, grew rapidly and made progress in reducing poverty.[38] Nevertheless, according to the factors taken into account such as the rate of import tariffs and non-tariff barriers, except for Uganda, these countries cannot be described as open economies. While the average tariff rates of India and Vietnam is more than 50%, China, with relatively lesser but still high average tariff rate applied trade subsidies and quantitative restrictions both before and after the accession to the WTO[39]. Again, since 1990s, while some fastest growing countries such as Lebanon and Lesotho, had trade-restrictive systems under the identification of Sachs and Werner's study, growth collapses can be seen in some of the most open countries such as Moldova and Mongolia. Taking into account this evidence, opponents conclude that there is not a strong relationship between openness and growth.

Armed with these arguments one could easily concludes that international trade is not the way to produce substantive equality among unequal trade partners. Especially the widening gap between developing and developed countries as well as rich and poor during the period of globalization clearly shows that benefits of international trade is not being shared equitably It is dangerous for developing countries to reduce trade barriers for the purposes of combating poverty and promoting economic development. That's why international trade institutions must seek a concept of fair trade rather than absolute terms of free trade. In the structure of WTO, one can see these arguments about providing efficient ways to developing countries for a fair integration into the world economy. Next part, some special treatments provisions for developing countries and arguments about their sufficiency are discussed,

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35 Sachs, J. D. and A. Warner (1995). "Economic Reform and the Process of Global Integration." Brookings Papers on Economic Activity, http://www.gsid.nagoya-u.ac.jp/sotsubo/Papers/Sachs_Warner_1995.pdf

36 David Dollar and Aart Kraay, "Trade, Growth, and Poverty," *SSRN eLibrary* (June 2001), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=632684, 4.

37 According to the Sachs and Warner, a country is considered as closed economy, if it has any one of the following five characteristics: "(i) its average tariff rate exceeded 40%, (ii) its non-tariff barriers covered more than 40% of imports, (iii) it had a socialist economic system (iv) it had a state monopoly of major exports, or (v) its black-market premium exceeded 20% during either the decade of 1970s or the decade of 1980s." Sachs, J. D. and A. Warner (1995). "Economic Reform and the Process of Global Integration."

38 Rodrik, Dani, How to Save Globalization from its Cheerleaders (September 2007). KSG Working Paper No. RWP07-038, Available at SSRN: http://ssrn.com/abstract=1019015, 4.

39 *Ibid.,* at 5.

IV. Development under the WTO

As it is mentioned in the beginning of the paper, first paragraph of the preamble to the WTO agreement refers to the objective of sustainable development. The second paragraph of the preamble places developing countries at the center of the WTO's efforts, by: *"Recognizing the need for positive efforts designed to ensure that developing countries, and especially the least developed among them, secure a share in the growth in international trade commensurate with the needs of their economic development"*[40].

Reading of the preamble clearly indicates that the representatives drafting the agreement are well aware that assisting developing countries and facilitating their economic development is an essential factor for the continuity of global trade system. This awareness led many development rounds and the last one called "Doha Development Round". Whether or not the WTO is effective in pursing these objectives is an open question.

It is reasonable to expect that countries with higher Grand Domestic Product (GDP) have more bargaining power than that with lower GDP as the former have more financial and political leverage against the latter to serve their interests. The WTO rules are generally determined and driven by reciprocal negotiations among countries[41]. Nevertheless the rise of new global actors among developing countries led by China, India, and Brazil, has started to change the balance between these negotiations, and eventually resulted in the suspension of the negotiations in the last development round (Doha Development Round).

In this part, the paper examines the current provisional and organizational system and the arguments whether the structure of the system really helps developing countries promote economic growth. At the end of the part, the paper also covers some proposals addressing how to deal with the problems caused by the current system.

A. Current WTO System for Development of Developing Countries

The duty to deal with issues on economic development of developing countries within the organizational structure of the WTO system is vested on the Committee on Trade and Development (CTD). Issues on economic development such as the implementation of preferential provisions, guidelines for technical and legal assistance, integration of developing countries in the trading system are the main concern of the committee. However, it should be noted that, the committee is not a decision—making body. Its scope is limited to just implementation of provisions and providing technical and legal assistance to the developing countries.[42]

Provisional structure of the WTO system is built upon rules such as tariff bindings, the prohibition on non-tariff barriers, the Most Favored Nation (MFN) provisions, and the national treatment obligations and exceptions thereto. These substantive rules apply to developing and

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40 Marrakesh Agreement Establishing World Trade Organization Preamble, para., 2.

41 Andrew Guzman and Joost H. B. Pauwelyn, *International Trade Law* (Aspen Publishers, Inc., 2009) 627.

42 Yong-Shik Lee, ed., *Economic Development Through World Trade: A Developing World Perspective* (Kluwer Law International, 2008), 11.

developed countries alike. On the other hand, WTO also includes some special rules for developing countries. These are called “Special and Differential Treatment” provisions and generally divided into six categories[43]: (1) Provisions aimed at increasing trade opportunities through generalized system of preferences. (2) Provisions requiring WTO members to safeguard the interest of developing countries. (3) Provisions providing flexibility to developing countries in rules and disciplines governing trade measures. (4) Provisions giving extended transitional periods to developing countries. (5) Provisions for technical and legal assistance. (6) Provisions about Least Developed Countries.

Although, there are nearly 100 provisions under this categorization that address to needs of developing countries, they, in fact, represent the modest deviations from the main substantive provisions because of the belief that, it is the substantive provisions that really contribute to economic growth rather than special rules[44]. However, these rules are not completely trivial in the consideration of development concept within the WTO. They are important in raising standards of life and economic growth in developing countries, when they are effective.

The question whether they are effective for development is the main argument debated heavily by the institutions of the WTO. In the next section these organizational and provisional problems faced by developing countries in the development process and negotiations are examined and some examples among the WTO provisions related to special treatment for developing countries are provided for the purpose of clarifying current system and its ineffectiveness.

B. Does The Current System Promote to Growth?

As mentioned, the WTO includes provisions aimed at the development of developing countries under the categories covered above. In order to provide an insight into their contribution to economic development, this section examines to what extent these provisions are capable of materializing economic growth they are adopted to accomplish.

Enabling Clause: General system of preferences (GSP) later called “Enabling Clause” is a provision articulated to promote trade and export earnings of developing countries through the establishment of generalized, non-discriminatory, nonreciprocal preferential tariff treatment in the markets of developed countries for products from developing countries. This provision provides opportunity to developed countries to waive the MFN provisions of the Article I of the GATT. In other words, developed countries can accord preferential tariff treatment to products originating in developing countries without applying the same tariff treatment to the other developed countries and fear of being subject to retaliatory sanctions, and developing countries have a better and much wider access to massive consumer potentials of developed countries. Moreover, the developed countries expect neither, reciprocity for commitments made by them in trade negotiations to reduce or remove tariffs and other barriers to the trade of developing countries nor contributions that are inconsistent with the particular situation and problems of developing countries[45].

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43 Guzman and Pauwelyn, *International Trade Law*. at 628-630

44 *Ibid.* at, 630

45 Lee, *Economic Development Through World Trade*. 9-10.

Although enabling clause and preference programs in the WTO do not oblige developing countries to act in a certain manner and do seem to provide them with at least some benefit, there are serious problems with the implementation of the provision.

First, enabling clause is directly related to MFN principle. and MFN tariffs are being reduced and removed through the WTO negotiations and regional agreements. Thus, as the MFN tariffs continue to fall, the advantages derived from the enabling clause are further eroded.[46] Second, the fact that enabling clause applies to products originating in developing countries brings about the concept of rules of origin, which requires that a substantive percentage of the inputs such as labor or material requirement, come from beneficiary countries. Such rules prevent the granted members form choosing the most efficient sources of inputs and result that a significant percentage of exports from those states fails to fulfill the requirements.[47] Therefore, compliance costs of rules of origin concept surely cut into the potential beneficial effects of GSP as well. Third, preference programs are discretionary and unpredictable that makes the investments made to take advantage of a preference scheme risky and unfeasible. Given their discretionary character, preference programs can be withdrawn anytime by granting member. Finally, in most cases, the members granting preference programs are allowed to seek additional requirements that developing countries are expected to fulfill in order to be the beneficiary of the program.[48] These additional requirements brought by granting state limit the number of developing states providing benefits from preferences and reduce the gains preferences provide to producers.

A**rticle XVIII of the GATT:** This provision recognizes the importance of infant industry protection and special conditions of developing countries.

"Developing countries should enjoy additional facilities to enable them (a) to maintain sufficient flexibility in their tariff structure to be able to grant the tariff protection required for establishment of a particular industry and (b) to apply quantitative restrictions for balance of payments purposes in a manner which takes full account of the continued high level of demand for imports likely to be generated by their programs of economic development."[49]

According to this provision, developing countries can grant tariff protection for their domestic producers, modify or withdraw concessions and subsidize domestic industries, in an effort to promote particular industry. Modification or withdrawal of concessions should be applied in a reciprocal manner. In other words, the developing member seeking to modify concessions should negotiate with other members and take some compensatory action for a mutual end.[50] Appropriate

[46] Wacziarg and Welch presents the MFN tariff rates in a country-based analysis. The paper clearly shows that special tariff preferences to developing members are meaningless, while the currents tariff rates are already low. Romain Wacziarg and Karen Horn Welch, *Trade Liberalization and Growth: New Evidence* Working Paper (National Bureau of Economic Research, December 2003), http://www.nber.org/papers/w10152, 39-45.

[47] Guzman and Pauwelyn, *International Trade Law*, 645.

[48] Appellate Body Report, *European Communities-Conditions for Granting of Tariff Preferences to Developing Countries, WT/DS246/AB/R* (adopted Apr. 20, 2004).

[49] GATT Article XVIII (October 30, 1947) (entered into force January 1, 1948), 58 U.N.T.S. 187, available at www.wto.org/english/docs_e/legal_e/gatt47_e.pdf .

[50] Lee, *Economic Development Through World Trade*, 7.

compensation may be arrived at through negotiations or, if those fail, by referring the matter to the general council.[51]

Though, the article provides a limited exception for developing countries to promote economic development through infant industry protection, reciprocity process consumes too much time for the purposes of development. Especially spending too much time for consultations and negotiations removes the limited contribution of the article and reduces its effectiveness.[52]

Part IV: In contrast to Article XVIII, the focus of Part IV is on export-led growth, instead of the protection of infant industries. Articles in Part IV establishes rules on when flow of goods and services originating from a least developed or developing country may not be possible due to inefficiencies for access to developed markets, developed countries are obliged to take necessary measures to provide effective access to their markets without reciprocal interests.

Article XXXVII states that: "The developed contracting parties shall to the fullest extent possible—that is, except when compelling reasons, which may include legal reasons, make it impossible— give effect to the following provisions."[53] As one can see easily that it is the language, which is the declaratory rather than obligatory and provides to developed countries enough room to do nothing.[54] The only remedy provided for developing countries in case of non-compliance by developed members is to submit a request for consultation to either individual developed countries or GATT council. This situation again raises serious doubt about the effectiveness of the provisions related to development.

C. Proposals

The WTO's organizational and provisional structure has proved to be ineffective in providing means for developing members' integration into the world system. When the conflicts reached at their peak in Doha and suspended the round, it became clear that solving the problem, in deed, requires a recalibration in the structure of the WTO.[55] Since then, there are proposals by highly acknowledged economists examining how to build an effective organizational and provisional structure with the purpose of answering the needs of poorer nations. They include both organizational structure of WTO and the provisions.

Current organizational structure of the WTO on development consists of Committee on Trade and Development (CTD) and subcommittee on LDCs. These institutions within the WTO are considered as ineffective due to their limited scope that is the CTD includes just the implementation of preferential provisions and technical and legal assistance for developing countries rather than a broader scope such as technology transfer, financial mechanism and debt relief.[56] The absence of an institution within the WTO concerning these issues has caused developing members have to deal

[51] Guzman and Pauwelyn, *International Trade Law,* 648.

[52] Lee, *Economic Development Through World Trade* 8.

[53] GATT Article XXXVII

[54] Lee, *Economic Development Through World Trade,* 9.

[55] Stiglitz and Charlton, *Fair Trade for All*.

[56] Lee, *Economic Development Through World Trade*, 11.

with these problems in the WTO's general council level in which the developed countries have excessive negotiation power. What is proposed to deal with this problem is to institute a new council covering all of these issues that the CTD does not cover.[57]

Elevating the existing committee to a council level that covers specific, complex and long term issues related development will help to resolve ineffectiveness problem of WTO institution. First, it would strengthen the organization in building effective specific development and preference programs by conferring a decision-maker characteristic to the institution. It would provide that developing countries do not have to deal with the provisional problems related to development within the general council level but they can bring the issues into an effective council whose main function is directly related to the development.[58] Second, this proposed council should cover substantial and essential trade related issues that the committee has not been able to address. Such new council will have a broader authorization to implement all necessary measures to contribute trade and development and capacity to handle substantial development problems that concern the developing members of the WTO.[59]

Proposals for an effective WTO system answering the need of developing countries related to the development also include a new provisional structure. The principle underlying these proposals is that all countries should participate in an enforceable system of preferential market access in which right and obligations are distributed progressively according to objective criteria.[60] Accordingly, they suggest that all WTO members should provide a free market access in all goods to those who have smaller and poorer market and economy. In other words, all developing countries can expect free access to all countries with both larger GDP and a larger GDP per capita.[61]

These proposals have many aspects. First they require a tremendous trade liberalization by the large developed countries so that industries of developing countries can reach developed markets and great amount of consumers. Second, without discretion of developed countries in evaluating special and differential treatment, there is no risk and unpredictable concerns for the investments made to take advantage of these treatments. Third, they also provide flexibility to developing members to use trade policy in the contribution of development through protecting their important industries from more efficient and advanced manufacturers and producers of developed members. Finally, these proposals do not involve complex negotiation processes and reciprocity that reflects countries that have bargaining power coming with lucrative domestic economies.[62]

There can be questions about motivational issues from the side of developed countries. Why would they support these proposals or adopt special and differential treatment? Which perspectives of these proposals can motivate them? These are serious questions, especially when political and economic constraints in the developed countries are taken into account. However, the trade practice

57 I*bid.*, at 12.
58 *Ibid.*, at 13.
59 *Ibid.*, at 13-14
60 Stiglitz and Charlton, *Fair Trade for All*.
61 *Ibid.*
62 *Ibid.*

among the developed members, leads optimism in the sphere of economists about the application of the proposals. For example, substantial share of trade among developed countries is already duty-free because of several bilateral trade agreements and developed countries actually are those who support the idea of free trade. Moreover, despite the threat of abusive use, those countries still have access to safeguard measures to reduce the adverse impacts of excessive number of imports. [63]

In order to build a satisfactory and well operating system of trade, both the organizational and provisional structure of WTO must provide significant benefits for developing countries with an enforceable capacity. Differences in circumstances and economic capabilities and the interests of WTO members must be evaluated carefully. Otherwise, the credibility of WTO will be damaged further and result being rejected by its developing members.

Conclusion

The understanding of free trade policy is changing. The idea that eliminating barriers to trade and liberalizing the market promote economic growth may not be regarded as a rule of thumb as it was so before. Free market may also prove to be a defective factor in specializing production tools and incentives. Countries with weaker production capacity are subject to the highly advanced imports from developed world and small industries within these countries get further harmed, because of the lack of ability to compete. When China and India are taken out of the data that academics provided, it can also be asserted that there is no sign for positive relationship between elimination of trade barriers and economic growth in developing countries. Moreover, it is accepted that free trade has distributional effects that it widens the gap between have's and have not's. Provisions provided by the WTO responds some concerns, however, it can be easily seen that the nature of the provisions, in deed, are designed for the favor of granting developed countries, instead of developing members.

It is self-evident that the WTO must have a new understanding and provide new effective provision answering the need of its developing members. In order to benefit the least advantaged countries of the current system, new provisions must be binding, non-exclusionary, and unconditional, if the goal is to implement it in a form that will reflect justice as fairness and contribute to justification of the international system. Otherwise, everything related to world trade and globalization is in danger which may consequently result in the demise of the WTO.

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[63] *Ibid.*

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