IPCS Special Report, No. 7, January 2006

WTO: THE HONG KONG MINISTERIAL

Surabhi Sharma
Research Intern
Institute of Peace and Conflict Studies

The Ministerial Conference, the highest decision making body in the WTO, which meets every two years, held the sixth summit meeting in Hong Kong in December 2005. The WTO, now includes 150 countries; 25 more countries including Russia, Bhutan, and Vietnam are waiting to be included.. Currently, the Doha round of Comprehensive Negotiations is ensuing which is the 9th round of Multilateral Trade negotiations.

The Doha round provides for negotiations on improving market access for agriculture, non-agricultural goods and services. On negotiations relating to agriculture, members are committed to "comprehensive" negotiations in all three pillars. Negotiations are to be undertaken to achieve "substantial" improvements in market access; reduce "with a view to phasing out" export subsidies, and achieve "substantial" reductions in domestic support.

Non agricultural market access (NAMA) negotiations aim at liberalizing trade in industrial and natural resources like fisheries, gems and minerals. Members have agreed on certain key issues of NAMA negotiations in the Doha round that includes reducing or eliminating tariffs, tariff peaks,[1] tariff escalation[2] and non-tariff barriers. Focus will be on products of export interest to developing countries and 'less than full reciprocity' in reduction commitments from developing countries. Product coverage is to be comprehensive with no a priori exclusions. The Doha round has a "development agenda", which finds expression in clauses requiring Special and Differential Treatment, including food security and rural development and less than full reciprocity from developing countries to be an integral part of negotiations.

I
THE DOHA ROUND AGENDA FOR NEGOTIATIONS

Agriculture

On agriculture issues, India is negotiating as part of the G-20 group of countries. There are three pillars of agriculture negotiations - market access, domestic support and export subsidies. Market access negotiations aim at reducing both tariffs and non-tariff barriers to trade. As regards tariffs, countries have agreed to convert specific duties (levied per unit of the product, as say, Rs. per unit) into ad-valorem duties (levied as a percent of price). Countries have also agreed to segregate duties into four broad categories or bands.

These categories of duties and the cuts to be made under each category are

[1] Tariff peaks: Relatively high tariffs amidst generally low tariff levels. For industrialized countries, tariffs of over 15 per cent are classified as tariff peaks

[2] Tariff escalation: Higher import duties on semi-finished or finished products than on raw materials

yet to be decided. It is also yet to be agreed on what should be the highest tariff for developed and developing countries. The G-20 group has suggested that developed countries reduce tariffs by 45-75 per cent, while developing countries lower their import duty on agricultural products by 25-40 per cent.

On Domestic support, the G-20 wants that trade distorting support extended by developed countries should be clubbed into three bands. Also they prefer that developed countries reduce the first band, comprising support of over $ 60 billion, by 80 per cent, while the lowest band (up to $10 billion) should be cut 70 per cent. The middle band of $10-60 billion should be reduced by 75 per cent. The G-20 has said developing countries with no AMS[3] support should be exempted from reductions. Countries are also negotiating a review of blue box[4] and green box[5] criterions.

Export Subsidy refers to payments made to local firms to boost exports when the domestic price is higher than the international price. This artificially drives down prices of agricultural products in international markets. Three issues are covered under export subsidy negotiations - export credits, state trading enterprises and food aid. The G-20 was pressing for the elimination of export subsidies within five years, (that is, by 2010).

Non-Agricultural Market Access (NAMA)

Since July, talks have focused on technical issues such as the tariff reduction formula, treatment of unbound tariff lines and conversion of specific duties into ad-valorem. As regards tariff reduction, talks have focused on two variations of the Swiss formula — the simple Swiss formula with one or two coefficients and a tariff average-based formula, suggested by Argentina, Brazil and India. (See Appendix)

India's Position on NAMA is based on its autonomous tariff liberalization. Countries undertake tariff reduction commitments on bound tariffs. As a result of the liberalization that India has undertaken autonomously, independent of its WTO commitments, applied tariffs are much lower than the bound rates. The intention is to leverage this autonomous liberalization in gaining important market access – in NAMA, agriculture and services. As regards the formula for tariff reduction, India is seeking to ensure the developed countries make the larger reductions and remove their tariff peaks and escalation. We want flexibility for developing countries and exemption for reduction commitment for a specified number of tariff lines. India has made a joint proposal for the tariff reduction formula along with

[3] Aggregate Measure of Support (AMS) is the cash equivalent of all the programs subject to reduction. It includes actual or calculated amounts of direct payments to producers (such as deficiency payments), input subsidies (on irrigation water, for example)

[4] Blue box policy is an expression that developed during the General Agreement on Tariffs and Trade (GATT) trade negotiations using a traffic light analogy to rank policies. The traffic light analogy was that an 'amber' policy could be converted to a 'blue' policy that could eventually become 'green'. Blue box policies were seen as acceptable, but temporary or transition. Blue box policies represent the set of provisions in the Agreement on Agriculture that are exempts from reduction commitments. They are typically payments that are linked to production–limiting programs

[5] Green Box policies are domestic support policies that are not subject to reduction commitments under the Agreement on Agriculture. These policies are assumed to affect trade minimally, and include support such as research, extension, food security stocks and disaster payments

Argentina and Brazil– the so called ABI proposal. India has said that it is willing to reduce its tariffs by 50 per cent with a co-efficient of 1 in the Swiss formula. This will reduce its average tariffs from 34 per cent to 17 per cent.

As regards sectoral commitments, India's position is that these are to be voluntary and are to have necessary differential measures for developing countries. On the issue of unbound tariff lines, India will increase its binding coverage (that is make commitments on hitherto unbound tariff lines) for concessions in other areas of negotiations. We want to ensure adequate flexibilities to address our developmental concerns and protect the domestic sensitivities. At present 68% of our non-agriculture tariff lines are bound that is, about 32% of the tariff lines remain unbound. Non tariff barriers are a cause for concern. Existing non-tariff barriers should be removed and mechanisms for their effective addressal built.

Services

Countries like India and the US have formed a "friends of service" group to take services negotiations forward. India wants to retain the request-offer approach in negotiations.

The General Agreement on Trade in Services (GATS) classifies services into 4 'modes':
Mode 1: Cross-border supply. Here services flow electronically from one country to another. For example, call centre operations.
Mode 2: Consumption abroad .For example, tourism
Mode 3: Commercial presence through subsidiaries (this clause pertains to FDI)
Mode 4: Movement of natural persons. For example, movement of Indian software engineers to the US.

Mode 1 and 4 are of special interest to India. It wants countries to open up their service sectors under Mode 1 and Mode 4. It has offensive interests in Mode 1 where it is seeking the removal of restrictions in BPOs. It wants the US and the EU to open up in sectors like R&D and health under Mode 1. Under Mode 2, India is liberal barring the finance and telecom sectors.

Under Mode 3 negotiations, countries are seeking liberalized foreign direct investment (FDI) regimes to facilitate the establishment of joint ventures, subsidiaries and branches of their domestic companies in other countries. India is seeking delinking of commitments under Mode 3 from those under Mode 4. It has improved its revised offers in select sectors by offering to bind the FDI limits for banking and telecom at 49 per cent and 26 per cent for insurance. It has, however, not offered any commitments in sectors like auditing, legal, retail and water. Commitments in sectors like medical and dental services and higher education have been offered with several restrictions.

Mode 4, at present, recognizes two categories - business visitors and intra-corporate transferees. Attempts are on to include two new categories - contractual service suppliers and independent service suppliers. India is seeking removal of limitations like the economic needs test. It wants immigration to be treated differently from temporary movement of professionals.

Implementation Related and Other Issues

Negotiations under the Doha round include 'implementation issues'. Intended benefits of liberalization commitments by developed countries did not accrue to developing countries because commitments were not 'implemented' properly. For instance, while developed countries reduced their average tariff levels, the problem of high tariffs peak and tariff escalations on products of export interest to developing countries limits access to advanced country markets. Continuation of high subsidies by developed countries is also a major problem.

Professionals from developing countries face barriers in developed countries like the economic needs test, minimum threshold of salary, visa delays etc. which in effect reduce the value of any commitments developed countries make under Mode 4.

Another issue is of very stringent Sanitary and Phyto-Sanitary (SPS) standards, many a time even higher than international standards, which hamper movement of developing country goods, particularly agricultural into developed countries. Also, the level of GI (geographical indicator) protection that wines and spirits have is not available to other items. The fact that TRIPS does not recognize the rights of traditional knowledge holders and does not provide for benefit sharing with them, although this is in direct contradiction of the CBD is another problem. There is no requirement to disclose the country of origin by the patent applicants which results in bio-piracy. Non-operationalization of S&DT clauses remains a cause for concern. Promises regarding S&DT for developing countries continue to be just that: empty promises.

India's concerns guide its negotiations and stance at the WTO. One of our foremost concerns is that the livelihood of our farmers is not to be compromised. We are not to allow shifting of subsidies from one box to another. Any tariff reduction is to be based on overall subsidy reductions. India is against allowing animal welfare etc. into negotiations as it may mean accepting linkage of trade with non trade issues such as labour standards or environment. Implementation related concerns and S&DT clauses are to be operationalized. There is to be no division / differentiation, such as creation of a category of advanced developing countries, among developing countries. India wants that patent applications should disclose the source of bio-resources. It is pushing for sharing of benefits if a patent is based on traditional knowledge. India recognizes the need to be vigilant at the WTO and to ensure that scope of framework agreement is not changed to its detriment by introduction of new elements.

II
THE HONG KONG DECLARATION

The Hong Kong ministerial which took place during 13-18 December was the sixth round of multilateral trade negotiations. The Declaration at Hong Kong has set a deadline of April 30, 2006 for reaching a draft pact for the Doha round.

Agriculture

Agriculture was the main focus of negotiations at the Hong Kong summit. But unfortunately, despite a lot of rhetoric by the developed countries, not much was achieved. Developed countries agreed to phase out export subsidies by 2013. But 2013 is later than what almost all countries wanted, that is, 2010. Moreover, export subsidies are a relatively minor part of the farm support. They are used mainly by the EU (to the extent of €2.5 billion), but constitute just 3.6 per cent of overall EU farm support. In any case, EU export subsidies have been falling for years, and would have largely been phased out by 2013 as part of the reform of the Common Agriculture Policy. To put a perspective on things, consider these figures: In the EU a cow earns $2.5 a day from the government and the U.S. subsidises its farmers to the tune of $1 billion a day.

On the whole domestic support issues remain largely unaddressed. On the Blue Box the language used in the text is stronger than before and it does open the way for tightening disciplines. But the amount spent and the loopholes that enable countries to exempt their subsidies via the Green Box have been completely ignored.

Developed countries have also agreed to eliminate all forms of export subsidies for cotton by 2006 and extend duty- and quota-free access from the commencement of the implementation period. The Cotton package is targeted mainly at African cotton producers. Unfortunately, export subsidies make up only 10 per cent of US subsidies for cotton. While there is some level of commitment to reducing other trade-distorting subsidies faster and further for cotton than for other crops, on the whole, the package is pitiful.

Developed countries and developing countries, in a position to do so are to provide duty and quota-free market access on a 'lasting' basis for all products from LDCs by 2008. For the LDCs this was a litmus test of the rich world's sincerity. The text reads "DFQF will be provided for all LDCs on a 'lasting basis' by 2008 for at least 97 per cent of all products." But looking beneath the surface, one realises that this too is eyewash. Since the EU and Canada had already unilaterally agreed to DFQF packages, the spotlight was almost entirely on the USA and Japan. Moreover, the commitment for 97 per cent of the products is a step back from the Doha mandate of full DFQF access. Today almost 94 per cent of tariff lines already enjoy access to the USA at low or zero tariffs. The fact that the commitment is only for 97 per cent of the products means that key products of most LDCs will be exempted. This is so because LDCs tend to export a limited range of products: the 3 per cent that is exempted comprises some 330 tariff lines; 20-25 tariff lines currently account for some two thirds of Bangladesh's total exports. The USA insisted on a ceiling of 97 per cent of tariff lines precisely because it allows it to protect its textile and garment sectors from imports from countries such as Bangladesh, Cambodia, and Nepal. Also, Japan can continue to protect rice, fish, and leather goods and footwear. Also, the commitment is to be 'lasting'; it is not a 'bound' commitment. It is thus not permanent, and is hostage to political opinion and special interests of the future. The importance of this can be gauged from the fact that the US refused to accept even 'long-lasting' as a basis for commitment.

As regards food aid, the problem is the dumping of non-emergency food aid. Thus food aid acts as a disguised form of export subsidy. There has been some progress in Hong Kong in producing a framework that is clearer than earlier commitments. The framework agrees on the need for new disciplines to prevent the abuse of food aid, and also allows for the creation of a 'safe box' for exemption of bona fide emergency aid.

The Hong-Kong declaration provides for both price and quantity triggers to enforce 'special safeguards'[6] against a sudden increase in imports. The fact that both price and volume triggers have been provided for imposition of the Special Safeguard Measures is a positive development. Developing countries can declare an "appropriate number" of Special Products.[7] But what treatment is actually given to these aspects, including deciding the number of special products will determine their practical importance-something that remains to be negotiated in Geneva.

The declaration says that "Developing countries with no AMS (aggregate measure of support) commitments will be exempt from reduction in de minimus and the overall cut in trade-distorting domestic support. Thus developing countries like India whose level of domestic support in agriculture is far below the limit allowed by the WTO will not have to undertake any cuts in its domestic support in this round. This is hardly a concession, but since the WTO agreement is a legal document, it was important that this be laid out in so many words.

The text also provides for an unspecified number of 'Sensitive products'[8] for developed countries. This is a new loophole that drastically reduces the value of any overall tariff and subsidy reductions by developed countries.

The announcement of 'Aid for trade' refers to the creation of a WTO task force will to build supply-side capacity for poor countries so that they can take advantage of trading opportunities. But concerns have been raised that this is unlikely to involve significant more money on top of that already pledged - for example at the Gleneagles G-8 summit. It is more likely that money already promised will be re-branded as 'aid for trade'.

Difficult negotiations on main and the most contentious agricultural issues stand postponed to 2006. The text sets an implausible deadline of 30 April 2006 for deciding modalities and 31 July 2006 for formulation of comprehensive country schedules. Given the pace of discussions so far, it is extremely unlikely that these will be adhered to.

Non-Agricultural Market Access (NAMA)

Developed countries pushed hard for a 'simple Swiss Formula' at the Hong-Kong meet. Since this would cut higher tariffs more than it cut lower ones, it would put developing countries at a disadvantage as their tariffs on non-agricultural products are generally higher. This is in direct contradiction of the 'less than full reciprocity' promised in Doha.

A new grouping known as the 'Core Group' comprising nine countries led by India and South Africa, along with Argentina, Brazil, Egypt, Indonesia, Philippines, Namibia, and Venezuela emerged at the Hong-Kong summit.

[6] Special safeguard measures: Flexibility to developing countries to impose quantitative restrictions in case of a surge in imports or a swing in international prices on a self-selection basis

[7] Special products: Agricultural products on which there will be nil or marginal tariff reduction

[8] Sensitive products' are agricultural products of developed countries so designated. They are given special treatment for political, social or cultural reasons and are subjected to lower tariff and domestic support cuts

This grouping sought to keep flexibilities for developing countries, while curbing Northern tariff peaks and escalation. They successfully fended off attempts led by the rich countries to push for a simple Swiss Formula.

However, even after prolonged negotiations, the status on NAMA negotiations remains more or less the same as before. India's proposal along with Brazil's and Argentina's continues to be on the table. The text declares countries' intention to focus on reduction of tariffs, especially tariff peaks and tariff escalation and on export products of developing countries. However, this is just a reiteration of what was agreed upon earlier.

Again, the text sets out unrealistic deadlines for NAMA negotiations. Modalities are to be decided by 30 April 2006 and draft schedules to be made by 31 July 2006.

Services
There is not much movement forward. Our Commerce Minister has said that India has succeeded in ensuring that there was no compulsion on developing countries to open up its service sectors. But this is just not good enough as our offensive interests in services today outweigh defensive interests.

The text sets implausible and inadequate deadlines. Plurilateral requests are to be submitted by end of February 2006 or as soon as possible thereafter, to which countries are obliged to respond by 31 July 2006. Thus a total of five months is provided for countries to consider the request, consult with the people affected and assess the potential impacts.

Geographical Indications and Biological Diversity
This was an area in which India had been pushing very hard. There was no movement forward except a recital to the efect that discussions are to be intensified in order to be completed by June 30, 2006.

In sum, very little was achieved at Hong Kong. There was virtually no movement forward in NAMA and services negotiations. Most decisions on contentious issues were put off till 2006. This includes the formula for reduction of trade distorting subsidies in agriculture as well as for reduction of industrial tariffs. The declaration has set a very unrealistic deadline of mid 2006 for completion of negotiations, which most delegates feel won't be adhered to. This is especially so given the pace of negotiations so far. One should keep in mind that the Hong Kong text was achieved after 16 months of hard bargaining after the July 2004 summit.

III
HONG KONG DECLARATION CONCLUSIONS

A. Why Did Developing Countries Agree?
If the Hong Kong declaration suffers from so many drawbacks, one could ask why the developing countries agreed to it. Well, firstly, almost all felt that another Cancun-style collapse would permanently damage the WTO as an institution. They were afraid of being blamed in case of a collapse. In fact, there were reports of Northern negotiators using this as a pressure tactic. Moreover, most of the big decisions on issues like NAMA, services, and agriculture were put-off and the doors were left sufficiently open in the complicated negotiations that almost all ministers left feeling

that at least something could be achieved for their countries in the future. And ministers were keen to return from the ministerial with something tangible to show their voters and businesses.

Also, for most LDCs many future lobby groups do not exist as yet-the future industries and service sectors that might one day be undermined by bad NAMA or services agreements. But, perhaps the biggest reason is that the U.S. President's 'Fast Track authority' expires in June 2007. Under the US government's 'trade promotion authority' Congress is only able to vote for or against trade agreements negotiated by the government, but cannot amend them. Without Fast Track authority, Congressional assent of a trade agreement is considered legislatively impossible.

B. Has Any Good Emerged Out Of This At All?

Ironically, perhaps the biggest success of the Hong Kong meet was that it didn't result in a Cancun-style collapse. A failure at Hong Kong would have terminally damaged the WTO as an institution. This shows the desire of countries around the world to remain engaged in multilateral trade negotiations, despite the rapid mushrooming of RTAs which are being touted as an alternative to a multilateral system.

C. Why Do We Need The WTO?

If after so much noise and fuss, and prolonged negotiations, what has been achieved at the Hong Kong conference is 'prevention of collapse'- and that is being touted as a success; and developing countries are being apparently given a raw deal, the question arises: why bother with the WTO at all? Isn't it better to instead focus our energies on RTAs? They seem to be much easier to negotiate and implement, and their terms are much more to our liking. Countries are increasingly becoming a part of them, as evinced by their rapidly increasing number.

One would think that even limited liberalization in an RTA would be beneficial since it would increase trade. However as it turns out, the formation of a PTA is neither necessarily trade liberalizing, nor does it automatically lead to greater economic efficiency. This was first pointed out by Nobel laureates- Jacob Viner and James Meade. They showed that a PTA had two kinds of effects: 'trade creation' and 'trade diversion'. Trade creation occurred when (as a result of a PTA) a country's domestic production was replaced by lower cost imports from a partner country. Trade diversion occurrs when low cost imports from the rest of the world (outside the PTA) are replaced by higher cost imports from partner countries because of tariff preferences.

If partners to a PTA have widely different factor endowments and economic structures, then PTAs will be welfare enhancing. The reason for suspecting that PTAs might not make 'economic sense' arises more so because PTAs are often driven by non-economic or extra-economic reasons. Such as motivations of political cooperation and solidarity as in the case of SAPTA (and now SAFTA), MERCOSUR and ASEAN.

South Asian countries and countries of the ASEAN are closer to us in economic structure and resource endowments than industrialised countries, and therefore we should not expect huge gains as could be expected if we were to enter a FTA with US or EC.

Then there are problems associated with defining and policing rules of origin (ROOs). This can prove to be very costly. For example, NAFTA had nearly 200 pages of ROOs! In the words of Jagdish Bhagwati, they lead to the creation of "ever-more complicated trade barriers."

Many of the economic downsides of PTAs (including trade diversion costs) in the recent past have been contained by the general trend of lower tariffs and trade barriers brought about through multilateral and unilateral trade liberalisation in the past half century.

Despite all this, the ASEAN countries are much more open economies than India- it would benefit us to join these trade-friendly clubs. Having said that, there is a lot to be gained from unilateral trade liberalisation. Consumers will benefit from lower prices. The increased competition will help companies to improve efficiency and productivity at home, and then help them in expanding operations abroad. However, crucial decisions and reform at home are essential to reap the benefits of trade. Infrastructure especially power and policy reform are areas of special concern. This is something that we can do on our own and this must proceed irrespective of the status of multilateral trade negotiations.

Appendix
Swiss formula

'Harmonizing' tariffs refers to greatly narrowing the gap between high and low tariffs. The "Swiss formula" is a special kind of harmonizing method. Given a wide set of initial tariffs, it uses a single mathematical formula to produce a narrow range of final tariff rates. Usually the required cuts are then divided into equal annual steps. The formula was proposed by Switzerland in the 1973–79 Tokyo Round negotiations, hence its name.

A key feature is a number- the "coefficient", which is negotiated and plugged into the formula. This determines the maximum final tariff rate.

The Formula

Z = AX / (A+X)
Where:
X = initial tariff rate
A = coefficient and maximum final tariff rate
Z= resulting lower tariff rate (end of period)