What You Should Know about Globalization and the World Trade Organization

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ABSTRACT

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This paper reviews the essentials of economic globalization, as well as the major institution that has recently gotten much of the credit and blame for it, the World Trade Organization (WTO). It first defines globalization, which is just the increasing economic integration of the world economy. It then asks who gains and loses from globalization, drawing primarily upon economic theory to identify its benefits and costs, and who within and among the world's economies get these benefits and costs. That part of the discussion concludes by asking briefly what can and should be done about globalization.

The second half of the paper turns to the WTO, which was the focus of so much negative attention at its Seattle meeting in December 1999. For it too, we first ask what it is, trying to clarify several mis-perceptions about what it does and why. We then ask which groups gain and lose from the WTO, some simply as a byproduct of its role in facilitating globalization, but others from particular WTO rules and procedures. This takes us to the controversies that raged in Seattle, and we describe those events as they have been described to us by those who were there (we were not). We conclude with our suggestions as to what might be done to change both the WTO itself and the public's perceptions of it.

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What You Should Know about Globalization and the World Trade Organization [*]

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I. Introduction

The term "globalization" has only recently become commonplace, yet trade economists like us have been studying and teaching about it for decades, even centuries. The institution of the World Trade Organization (WTO) has only recently come to exist, yet legal experts on international trade have been studying and teaching for almost half a century about its predecessor, the GATT, as well. In both cases, specialists in international trade have argued the benefits, but also acknowledged the costs, of international economic integration and the institutions that facilitate it. Yet until recently ours was a specialty that only a few paid attention to, especially in the United States where the size of domestic markets seemed to render the rest of the world of only secondary importance. Only in the 1990s did America begin to wake up to the significance of world markets and institutions. By the end of the decade, at the Seattle ministerial meeting of the WTO in December 1999, a host of voices were raised against both. This has turned our academic specialty from obscure to reviled in barely a moment. In this paper we try to set the record straight.

Our purpose is to clarify, for both globalization and the WTO, what they are and what they mean to the world. We do not primarily intend to be advocates of either, and we will acknowledge and explain both the costs and benefits of both. But inevitably, having spent our careers consistently finding the benefits to outweigh the costs, we will conclude that here. Yes, there are those who lose from world markets and institutions, and some of them are understandably opposed when these intrude into their lives. But overall, we agree with almost all others who have looked at these issues carefully and objectively (and many, admittedly, who have not), that the vast majority of people in the world are ultimately made better off by the spread of global markets and the efforts of the WTO to keep those markets reasonably free. To be sure, there are problems that need to be addressed, and we will mention them too and possible solutions for them. But even in their current imperfect form, the WTO and the open international markets that it has fostered are far better for the world economy than the alternatives that would likely arise if they were disbanded and reversed.

Our paper will be in two parts, the first on globalization and the second on the WTO. In both, we will first define and document the phenomena at issue, then identify the major groups who benefit and lose from their effects. Much of this discussion, especially for globalization, will inevitably repeat what trade economists have been saying about trade for two centuries, for the issues are not new. However, they have taken new forms in recent years, and the WTO has likewise expanded the institutional scope of its predecessor, the GATT, in ways that also need to be addressed. In particular, events in Seattle raised many issues that had only recently been seen in discussions of international trade, and we will do our best to describe what these were and what actually happened in Seattle. In both parts of the paper, we will conclude with some discussion of what the options are for action, if any, and what we believe should be done. The paper concludes with a final section that tries in much briefer form to answer the question of our title, listing what we believe to be the most important things that the public should know about globalization and the WTO.

II. Globalization

What Is It?

Everybody is writing about globalization these days, and the word means different things to different people. We take it to mean the increase in international transactions in markets for goods, services, and some factors of production, plus the growth and expanded scope of institutions that straddle national borders – including firms, governments, international institutions, and nongovernmental organizations (NGOs). At the most basic level, globalization is growth of international trade. But it is also the expansion of much else, including foreign direct investment (FDI), multinational corporations (MNCs), integration of world capital markets and resulting financial capital flows, extraterritorial reach of government policies, attention by NGOs to issues that span the globe, and the constraints on government policies imposed by international institutions. All of this has fostered an increasing sense of helplessness among many who feel that their lives and their economic options are being determined not by themselves, or even by their countrymen and their own governments, but by external forces over which they have no control. Residents of small countries may have experienced this long ago, but in the United States and other large countries, this is a new experience, and for many it is disagreeable.

Evidence of globalization is not hard to find, although the surprise may be that the current wave of globalization is not the first. In many ways, the world economy reached a peak of globalization just before World War I, when trade and FDI attained what were then unprecedented levels that are still quite remarkable given the technologies that were available for transportation and communication. But the current wave of globalization has far surpassed that of a century ago.

Figure 1 shows one indicator of the growth of trade over the last half century. Measured as an index of the ratio of world exports to world GDP (1990=100), the graph shows that this ratio increased fairly steadily through the early 1970s. It then stalled until the mid-1980s, when its growth resumed, and it grew especially fast in the mid-1990s. By 1998 it was more than three times what it was in 1950.[1]

A longer perspective is shown in Figure 2, which graphs merchandise exports over GDP in selected years from 1890 to 1990 for several countries and the world. The earlier peak in 1913 is evident, and for Japan and the U.K., exports remained below 1913 in 1990. This graph also shows the considerable variation, even among large countries, in the relative importance of international trade.

Increased international capital flows have been most pronounced in portfolio investment, which, like trade, displayed an earlier peak prior to World War I. Figure 3 shows foreign assets as a percent of world GDP for selected years. The pre-WWI levels were not reached again until around 1980, after which they grew threefold by 1995. We do not have exactly comparable information on FDI or the presence of MNCs in the world economy, although information reported by Crafts (2000) shows that both were also important in 1914. The real stock of FDI relative to world GDP rose by 59% from 1960 to 1995. Thus, at least in the second half of the 20th century, both international trade and international capital flows of various kinds were increasing steadily, and this is much of what has come to be called globalization.[2]

What has caused these changes? Two obvious reasons are technology and policy. Improvements in both transportation and communication have increased globalization in all markets, trends that may be accelerating today with the Internet. Policies, in contrast, have alternated direction over the years, restricting international transactions and mobility after World War I, then opening up after World War II.

Figure 4 reports average tariffs on manufactures for several major industrialized countries for selected years. Before World War I, tariffs were fairly high, becoming even higher in the 1930s. After World War II they were brought down gradually, mostly through GATT negotiations, and today they are almost negligible in most manufacturing sectors for these countries. Not reported are tariffs in less developed countries (LDCs), which remained high much longer and are still large compared to those in Figure 4. However LDC tariffs too were substantially reduced, often unilaterally, starting at various times in the 1980s. Developed-country tariff reductions have been partially offset by nontariff barriers (NTBs), especially in the 1980s,[3] but nonetheless it seems clear that much of the substantial growth of international trade was due to reduced policy barriers to trade.[4]

Is this, then, all there is to globalization – increased trade and capital flows caused by improved technology and reduced policy barriers? Not really. Other aspects of economic life have also become globalized. Governments are increasingly sensitive to policies used by other countries. NGOs look increasingly beyond borders, either because their issues are intrinsically global (the hole in the ozone layer), or because they view their causes to be of world-wide importance (human rights). Corporations increasingly operate across national borders, and have grown to sizes that dwarf some countries, achieving leverage over national governments that may free the companies from control. Again, all of these changes had counterparts in the 19th century, but that does not make their importance today any less.

Finally, the designers of the post-war institutions explicitly envisioned the need for countries to cooperate, and sometimes to sacrifice narrow national interests for the greater good. These institutions have been very successful, at least in expanding their own power and importance. The World Bank, the IMF, and now perhaps the WTO have reached the size that they can grow on their own momentum. Some find these changes gratifying; others find them threatening. And all are part of globalization.

Whom Does It Help and Whom Does It Hurt?

At its core, globalization means that international markets are becoming more integrated. Such integration has been the subject of international trade theory for two centuries, and economists have a good understanding of its effects. In this section, we review these insights from trade theory.

Static Effects of Trade

Who gains from trade? The first answer is consumers. That is, everybody in a country stands to gain from trade in their role as consumers of goods and services. For many reasons – including comparative advantage, economies of scale, increased competition, and access to a greater variety of products – a country's average consumer, with an average income, is better off with trade than without.[5] That is, the average person's income will buy a larger, more desirable bundle of goods and services with trade than without, increasing their material standard of living. This proposition, called the "gains from trade," has been shown theoretically in all sorts of economic models. With only a few exceptions – which economists generally view as unlikely to reverse the broad conclusion in practice – it applies to all countries comparing trade to not trading at all. The argument extends to further degrees of openness, as well as to other kinds of openness such as international movement of capital. Thus, the fundamental case for trade and globalization is that it raises the average person's standard of living.[6]

However, this benefit applies to the average person, with average income. Income is not equally distributed, and trade may not benefit everybody. A fundamental result of trade theory, the Stolper-Samuelson (SS) Theorem, identifies winners and losers from trade in terms of the national abundance and scarcity of factors of production, such as labor and capital, from which they derive their incomes.

Owners of abundant factors tend to gain more than average from trade, while owners of scarce factors are made unambiguously worse off.[7] More general models allow for additional sources of gain from trade and suggest that even owners of scarce factors may gain, in which case SS says only that they gain less than average. But the possibility remains that they actually lose.

So trade theory tells us that, indeed, there may be losers as well as gainers from trade and globalization. Who are the losers? In the United States, with its abundance of capital, education, and land, the scarce factor is clearly labor. Not that we have a small labor force – we do not. But we have even more of everything else. In this relative sense, we are especially scarce in those workers without a great deal of education, what we will simply call labor. Therefore, trade theory tells us that the group in the United States most likely to lose from globalization, or at best to gain less than everyone else, is labor. This is hardly a surprise. Growing opposition to globalization by organized labor shows that they are well aware of this. The surprise may be that economists, who tend to favor trade, would agree. But we do.

It follows from this, too, that trade is likely to increase income inequality in advanced countries. Because labor has lower income than those with income from other sources, and because trade lowers the relative wage, it tends to make the poor relatively poorer. Leaving aside the legitimate question of whether an increased return to some other factors, such as the return to education, may actually increase the opportunity to escape poverty by becoming skilled, we therefore expect in the short run at least that globalization will increase inequality in rich countries like the United States. Empirical studies, reviewed e.g. in Freeman (1995), confirm that increased trade accounts for a portion (although much less than half) of the increased inequality observed in the United States since 1980.

Why, then, do we claim that there are gains from trade? Because we are confident from both theory and experience that the winners gain more than the losers lose, enough so that policy could potentially compensate them, leaving everyone better off. In the long run, with some mobility across population groups and with programs to permit the whole population to share in the country's income, most people can expect to be better off with trade than without.[8]

SS also applies to LDCs, but there the scarce factor is different. Being poor, LDCs are the mirror image of the United States, with labor abundant and most other factors scarce, especially capital and education. These belong to the elite, who therefore lose from trade, according to SS. Labor in LDCs will gain. Since labor in LDCs is far poorer than labor in developed countries, globalization can be expected to reduce income inequality worldwide, even while it may increase inequality within rich countries.

Are there other gainers and losers from trade, besides the owners of abundant and scarce factors? Yes, and many of them are obvious. Due to trade, some industries expand and others contract. Many people are invested in "industry specific" capital, human and/or physical, in particular industries – skills and equipment that are useful only within an industry. These people gain or lose along with their industries, and some can find the basis for their livelihoods destroyed, a serious cost that public policy can usually only partially acknowledge. For some, these costs continue for months or even years, as they relocate, retrain, reinvest, and otherwise readjust. Others, especially those later in life, may never recover. Trade theory does not in any way dismiss these costs as unimportant or even as smaller than other gains. Economists therefore usually favor only gradual movement toward freer trade, so that these adjustment costs can be accommodated within the routine ups and downs of markets.[9]

Nonetheless owners of contracting-industry specific factors are a major source of concern in response to globalization. These include, for example, American owners and workers in textile and apparel firms, India's skilled workers in steel mills that were built as it attempted self-sufficient industrialization, and Mexico's small farmers of corn (maize) who now compete with more productive farms in the Midwest United States. These are only a few of the many groups throughout the world who have reason to be leery of globalization because of their dependence on industry-specific factors.

It is not only whole industries that expand and contract due to trade. Within an industry, particular firms also win and lose, and firms that have prospered in a protected domestic market may not be the same ones that do well in a globalized economy. Anticipating in advance the identities of winners and losers may be impossible, but once the process is underway, particular firms will try to speed it up or slow it down, depending on how well they deal with its competitive pressures.

Dynamic Effects of Trade

This discussion of gains and losses by particular firms and by specific factors is appropriate primarily to the short run, because in the longer run, people relocate, retrain, and otherwise readjust to changing circumstances. Gains and losses to abundant and scarce factors, in contrast, last longer, continuing even after factors have moved from failing firms and contracting industries into new and expanding ones. However, this is not the end of the story. Over even longer time horizons, the total of a country's factors changes with economic growth. It is reasonable to ask, then, who gains and loses from trade in the *very* long run, as sizes of countries and their rates of economic growth may change.

An easy answer to who gains and loses from trade in the very long run is: "Not us." Keynes said that in the long run we are all dead, and he was probably right. Thus whoever may be the long run gainers and losers from globalization, they will be subsequent generations, not ourselves. That makes it harder to predict how they will fare, since we know less about them than we do about ourselves. In a dynamic economy like the United States, the owners of tomorrow's capital, land, and human capital may not be the descendants of those who own these factors today. Therefore, even without economic growth, our best bet for helping future generations is to maximize total income. Globalization does exactly that. Therefore we have some confidence that "everyone" in future generations will benefit from it.

Allowing for economic growth, this conclusion becomes still more likely, although the theoretical basis for it is less certain than the aggregate gains from trade in the shorter run. Economists do not in fact have a solid theoretical grasp of how trade affects economic growth, perhaps because growth itself is less well understood than the economics of static markets. Instead, there exist a variety of models of growth, and even more ideas of how trade may interact with growth. Some predict only that trade permits a country to grow larger than it otherwise would; others suggest that trade lets countries grow faster indefinitely. And there are also models where trade may be bad for growth.

But empirical evidence is much clearer that trade and globalization are good for growth. For half a century, most countries that have minimized trade have failed to grow, while those that have stressed exports have done much better. After a few successful countries demonstrated the benefits of trade for growth – especially the "four tigers" of Hong Kong, Singapore, South Korea, and Taiwan – other countries opened their markets and grew faster as well. This process has had setbacks, but few economists today doubt that open markets are beneficial for growth, even if we do not entirely know why.

If so, the case is even stronger that, in the very long run, entire populations gain from globalization. Those who are hurt by trade in the short run may lose relative to others. But because they will have a smaller slice of a larger pie, they may well be better off absolutely. That will surely be true if trade permits countries not just to grow to larger size, but to continue growing at faster rates indefinitely. In that case, globalization and trade are beneficial for everyone who will ultimately be alive.

Effects of International Capital Flows

All of our discussion so far refers to the gainers and losers from trade. To a great extent, the gainers and losers from international capital flows are the same, since capital tends to flow in response to the same market forces as trade. There is, however, the added proviso that those who are internationally mobile tend to do better than those who are not. Dani Rodrik (1997) has stressed that, in a globalized economy where some groups are mobile and others are not, those who can move tend to benefit at the expense of others. In the last half century, capital has become increasingly mobile, while labor has not. We therefore expect some additional tendency for labor to lose, and capital to gain, from globalization.[10]

This may account in part for a widely held perception that globalization is mostly for the benefit of large corporations, as argued by Lori Wallach (2000) of the NGO Public Citizen. It is certainly true that large corporations often (but not always) prosper in the international environment, and those small corporations who also prosper become large as a result. This is partly due to their ability to shift operations around the world to wherever makes the most economic sense. If they do this well, their stockholders gain. Of course, the larger the corporation the more likely is its stock to be widely held, including in the retirement funds of workers. Therefore the gains that accrue to capital accrue in part to those workers who manage to save during their working years.

Capital mobility has another quite different implication, however, that has little to do with returns to factors of production. Financial capital often takes very short-term forms, and it is highly liquid – able to move quickly into and out of a country or a currency in response to speculative expectations. Such movements generate another class of winners and losers: those who bet correctly and incorrectly on changes in financial markets. More important, however, are other victims of short-term capital flight. When expectations turn against a country or its currency, the resulting capital outflow batters many of those within the country. Borrowers default, banks become insolvent, credit to finance exports dries up, and the damage spreads through domestic markets causing recession that hurts much of the population regardless of their apparent exposure to foreign markets. This is the story of the Asian crisis of 1997, but it had happened before, and will probably happen again. The harm here is a byproduct of globalization, but also of the prosperity that globalization has previously contributed to via capital inflows.

Other Effects of Globalization

This completes our list of those gainers and losers from globalization. But the discussion would be incomplete without mentioning several additional benefits and costs.

On the side of benefits, many say that globalization has reduced inflation. Inflation rates in many countries are low, and inflationary pressures have so far been restrained even where unemployment rates are also low. Some attribute this to a "new economy," in which technology and global markets together restrain firms from raising prices. If this continues and if it truly is a byproduct of globalization, then the lower inflation rate and the associated lower sustainable rate of unemployment benefit almost everyone.

Another possible benefit of globalization is an increased rate of technological progress and productivity growth. The slowdown in productivity growth that began in the mid-1970s appears to have reversed in the late 1990s, although it is too soon to know whether this is permanent. Here too, some argue that increased international competition has forced firms to innovate and to economize on labor, increasing productivity, and that this may be a lasting benefit of globalization. We see even less evidence to support this conclusion than the previous one, but it deserves mention.

Finally, globalization affects local cultures, causing changes that are sometimes admired, sometimes deplored. International trade, travel, and capital flows have exposed people everywhere to the products and sometimes the customs of other countries. This is evident in the United States, for example, with the variety of national cuisines now available in restaurants and supermarkets. The same is happening even more in reverse, although many are unhappy to see it. U.S. culture is spreading throughout the globe through trade, especially U.S. exports of movies, music, and television programs. Young people around the world are adopting American styles of dress, music, and behavior, to the dismay of some of their elders and of those who fear the loss of their own cultural traditions. As economists, we are reluctant to discount the choices made freely by consumers anywhere. But cultures are public goods, and fragile ones at that. Globalization may bring cultures into conflict, and new policies for protecting them may be needed.

What Should Be Done about Globalization?

We have heard it said that globalization has so much momentum that it cannot be stopped. We disagree. Unforeseen events, and even deliberate policies with unforeseen consequences, could conceivably reverse the process of globalization, just as World War I and the Great Depression did once before. There is little reason to believe that the world is now immune from the sorts of world-wide disruptive events that have wracked it twice before within the last century.[11] If such occur, much will depend on the wisdom and expertise of the world's leaders and their efforts to repair and restore the institutions of the world economy afterwards.

It is also conceivable that public policy could change direction and reverse globalization more deliberately. The institutions of the global economy – the World Bank, IMF, and WTO – would be incapacitated if the United States or Europe withdrew support, and considering recent controversies, this could happen. Without them, especially the WTO, the world could descend into a trade war or a series of competitive devaluations and tariff increases, just as in the 1930s. These were *not* irrational acts by uninformed policymakers, acts that we would not repeat today. Instead, like the uncooperative strategies in the Prisoners' Dilemma of game theory, they were rational individual responses to situations. Without some mechanism for international cooperation, the same could easily happen again.

While we believe that the benefits outweigh the costs for both trade and FDI, we are less sure of the free movement of financial capital. The disruption and hardship caused by recent financial crises could perhaps have been avoided through better policies and decisions on the part by governments and international organizations, but a case can also be made for limited restriction on international movement of short-term capital. This is not our area of expertise, and we are reluctant to take a position on it. We merely note that smart people disagree on this issue, and leave it at that.

Aside from financial capital markets, then, what policies should be pursued with regard to globalization? As we have said, we believe that globalization has been largely a good thing, with the benefits exceeding the costs. Therefore we certainly do not want to see any reversal of direction, or a return to protection. Since most of the costs of globalization are costs of adjustment, analogous costs would arise again if we moved back in the other direction. Indeed, given the progress toward global and efficient markets, continued liberalization may be less painful than what has come before. In any case, we favor continuing liberalization of both trade and direct investment.

Many of the concerns of those who oppose globalization are legitimate, however, and should not be ignored. National governments and international institutions must address their concerns, assisting those who lose most from globalization wherever they can without undermining the process. How this can best be done deserves greater study and perhaps experimentation, but programs of adjustment assistance, wage insurance, and retraining should be considered.

III. The WTO

What Is It?

The World Trade Organization, created in 1995, is the successor to, and incorporates within it, the GATT – the General Agreement on Tariffs and Trade – which was a treaty among western market economies at the end of World War II. Member countries agree to rules about when they may increase trade barriers, especially tariffs, in order to prevent them using trade policies that harm other countries. The GATT was also a forum for negotiation to reduce trade barriers. Presumably the WTO will do this as well, although it has not yet. The GATT oversaw eight rounds of multilateral trade negotiations, culminating in the Uruguay Round that created the WTO. The WTO also took on issues that GATT had not covered, including trade in services, tariffication in agriculture, and intellectual property protection.[12]

The most important change in the WTO, compared to the GATT, may be its dispute settlement mechanism (DSM). The GATT permitted countries to complain against other countries for violating its rules. Each complaint was handled by a "panel" of experts who issued a report that, if adopted unanimously by GATT members, would require the offending party to either change its behavior or be subject to sanctions. However, unanimity meant that the offending party could block a report, in effect giving every country veto power over findings against itself. The surprise was that this ever worked at all, which it did.

The WTO reversed this bias, requiring instead a unanimous decision to block a report, and it therefore made the DSM much more effective. It also made other improvements, including the right to appeal. The intent was to provide viable enforcement for WTO rules, and it appears to have worked. The DSM has been used much more often than under the GATT, both by and against a wide range of countries, as shown in Table 1. Just as important, large countries (the U.S.) have stopped going outside the GATT with their most important complaints.

Inevitably, however, the DSM has not worked to everyone's satisfaction. The WTO restricts policies that harm other countries, not only deliberately, but also inadvertently, as when policy restricts the options of another country's citizens. A contentious example was the "shrimp-turtle" case. A U.S. law protected sea turtles from death in the nets of shrimp fishermen by prohibiting imports of shrimp caught without "turtle exclusion devices" (TEDs). Since it is impossible to tell from looking at a shrimp how it was caught, the law restricted imports from certain countries. These took the case to the WTO, which decided against the United States. In effect, this decision struck down U.S. law, an intrusion into sovereignty that offended environmentalists and others. There have been other, similar examples.

The potential of the WTO to intrude in national affairs was also increased by its expanded coverage. The GATT was limited to trade in goods, even excluding certain sectors such as agriculture and textiles/apparel. The latter was covered instead by the GATT-sanctioned Multi-Fibre Arrangement (MFA), restricting developing-country exports to developed countries. The WTO changed all that, or at least it promises to. The Uruguay Round scheduled the elimination of the MFA, though the most difficult liberalization is postponed ("backloaded") ten years. First steps were also taken in agriculture, converting existing NTBs to tariffs (tariffication) so as later to negotiate them downward. And trade in services was covered in a parallel agreement to the GATT, the General Agreement on Trade in Services (GATS).

The WTO also expanded to new areas. Most prominent and effective is its TRIPS (Trade Related Intellectual Property) Agreement covering intellectual property – primarily patents, copyrights, and trademarks. In addition, the WTO includes (as the GATT had before, actually) some small ways that countries may use trade policies for environmental purposes. However, the one area – much discussed – where the WTO has *not* been extended is labor standards and rights. Despite many in developed countries who favor using trade policies for this purpose, resistance from the developing world, as well as from corporations who employ labor there, has prevented it from even being discussed.

Whom Does It Help and Whom Does It Hurt?

With its expanded role, the WTO will affect many groups. But fundamentally it is still, like the GATT, a force for increased trade, and thus for much of globalization. The WTO has not, yet, done much on international capital movements, although its agreement on financial services will lower transactions costs for movements of financial capital. But it has done much to facilitate international trade. Those who gain and lose from the WTO, then, are also those who gain and lose from globalization.

Therefore, all that we said above applies here as well, about gains and losses to abundant and scarce factors, to industry-specific factors, and to factors unable to move or retrain. Because the WTO extends to previously excluded sectors – textiles, apparel, agriculture, and services – those principles will apply especially strongly to them. For example, developed-country textile workers, who have been protected for decades, have particular reason now to be concerned, if indeed the MFA will disappear. Developing-country textile workers have corresponding reason to be hopeful.[13]

More generally, however, the WTO has an important institutional role beyond just fostering trade: to constrain countries from using trade policies that will hurt each other and themselves. Without such constraints, two things would guide countries' uses of trade policies. First, large countries would be able to use policies to gain at small countries' expense. Second, weak and misguided governments would be able to use policies to benefit themselves and their "cronies." The WTO, with its rules and its DSM for enforcement, deters both. It protects weak countries from strong countries, and also weak countries from themselves. This is true especially for poor countries. Thus, even though the WTO was mostly designed by rich countries and even corporations, its greatest beneficiaries may well be in the developing world.

Who loses from the WTO? Again, some of the losers are simply those who lose most from trade, and here we must point again to relatively unskilled labor in developed countries. It makes perfect sense that organized labor in developed countries should be skeptical of the benefits from the WTO, for theory predicts that greater trade will indeed hurt their members, at least relatively.

Aside from these effects of globalization itself, the rules of the WTO will also hurt those who would wish to break them. If there are large countries that seek to use their economic size at other countries' expense, then they will be frustrated by the WTO. Fortunately, we see little evidence in recent decades that the most powerful countries have sought to do this.

More likely losers, therefore, are those who seek to use trade policy for other legitimate purposes but run afoul of the WTO, as in the shrimp-turtle case. Those who seek to halt environmental degradation naturally wish to use trade policies to pursue their aims, since few other policies work across borders. Yet to do so risks violating the strictures of the WTO. Environmentalists have therefore sometimes been hamstrung by WTO rules, and they believe that they – or the environment – are hurt by the WTO.

It is true that the WTO makes the objectives of environmentalists harder to attain. Policies impose costs, and some are borne by other countries when one country unilaterally uses trade policies for environmental purposes. The WTO gives those costs more weight than if countries could act alone. This means that a lower level of environmental protection will result when these costs are factored in. This is as it should be, however, since global policy decisions should be based on global costs and benefits, including all aspects of all people's lives, not just the environment or one country. Environmentalists, whose role is narrower, will indeed make less progress when their interests are balanced against those of others.

Environmentalists might say, "Fine, but the WTO does not just balance other interests against the environment; it rules the environment out of court. All we want is for environmental concerns to be heard in the WTO." In fact, the WTO does include several environmental clauses, so even here the question is one of balance. How much role should environmental concerns play in justifying trade policies? Arguably, the current system has not done badly. The problem with using trade policies for environmental and other purposes is that they too easily push the cost onto others. The WTO has forced their advocates to find fairer ways to achieve those purposes. For example, the shrimp-turtle brouhaha led, more quietly, to shrimp fishermen being equipped with TEDs at developed country expense. We would say that this was the right solution all along.

There are other issues, besides the environment, whose advocates wish to use trade policies, including human rights and labor standards. For both, the United States especially has used trade policies in the past, against non-WTO members like China, and in our implementation of preferential trading arrangements. Some see the WTO as an enemy of human rights and labor standards. That conclusion is way too strong, but as with the environment, as the WTO interferes with policies that would otherwise be available to pursue these ends, the ends themselves will not be attained as fully.

In the case of human rights, the WTO does permit some use of trade policies, such as the economic sanctions that were used against Rhodesia in 1965 and against South Africa in 1985. Formally, these were permitted under GATT Article XXI, based on actions under the United Nations Charter for purposes of peace and security.[14] The WTO does not permit unilateral sanctions for human rights, however.

In the case of labor standards and labor rights, the issue is more complex, partly because it is so difficult to separate the moral from the economic, and partly because of different views of what labor standards mean economically.[15] Some labor standards, such as the prohibition of slave labor and exploitative child labor, are clearly moral issues. Others, such as a minimum wage, are economic. And still others, such as working conditions and child labor with the approval of caring parents, are somewhere in between. Where to draw the line, and who should draw it, are hard to say.[16]

Economically, most labor standards affect the cost of labor, even when not explicitly about wages. But their effects depend on how one believes that wages are determined. From the perspective of competitive markets, which guides most economists on this issue, labor standards are mostly about the remuneration of labor in poor versus rich countries, and higher labor standards in the former primarily benefit the latter, putting developing country workers out of work. Another view, however, is that all labor remuneration is at the expense of capital, so that higher labor standards merely reduce profits. In economics, this second view makes most sense if employers have market power, something that globalization is in fact likely to undermine. But not everyone believes market economics, especially non-economists, and there are plenty of subscribers to this second view among opponents of the WTO. In their view, by excluding labor standards as a basis for trade policy, the WTO helps capitalists and hurts workers, everywhere. But modern economics suggests that only developed-country workers may be hurt, while the true beneficiaries of the WTO are the developing-country workers whom labor standards are ostensibly meant to help.

The latter view, which we share, is voiced prominently by economists and by most leaders of developing countries. They perceive labor standards, when enforced by trade sanctions, as thinly disguised protection for developed-country labor. The WTO excludes labor standards as part of its broader role of protecting the weak from the strong. We agree with the position taken at the 1996 GATT Ministerial Meeting in Singapore that issues of labor standards should be handled in the International Labor Organization, although we also favor some increase in that organization's resources and effectiveness.

Other Objections to the WTO

Even among those who think the WTO has it right on environment and labor standards, however, the WTO does nonetheless have flaws. One is its lack of transparency. The proceedings of the DSM panels are secret, and the panelists get information only from governments. Some regard this mechanism as non-democratic, and they fear its capture by corporations with financial stake in the outcome. They would like interested NGOs to be able to provide input to the process, and perhaps to have the panelists themselves selected by a process that NGOs could influence.

The complaint about non-democratic procedures is ironic, since the WTO works by consensus among mostly democratic governments, whereas NGOs are by definition self-appointed special interests. More important, however, is a concern from developing countries, that opening the DSM to public scrutiny and influence would cause its capture by precisely these special interests, at developing-country expense.

Nonetheless, even defenders of the WTO are coming to see the DSM's secrecy as counterproductive. It is also inconsistent with other WTO procedures, which have always been open if anyone cared to look at them. Therefore many say the DSM should permit NGOs and others to file "friend of the court briefs." Some also argue that a more permanent body should replace the panels themselves, instead of being assembled case-by-case. If so, then greater public input to selection of that body might be natural.

Another concern has long been that a few rich countries dominate the WTO, developing countries having little role. This is true in spite of – or even because of – its formal reliance on consensus. With 140 member countries,[17] consensus is not practical, and therefore a smaller group has typically sought agreement among themselves, then come to the larger group for approval. This smaller group, named the "green room group" after the room in which they have sometimes met at WTO headquarters in Geneva, has been assembled on an ad hoc basis by the Director General and has included both developed and developing countries based on their interest in the issues being addressed.[18] However, many developing countries – especially smaller ones – have been excluded and were not formally represented, not by design because there was no design, but by default. Exactly how to change this is not clear, but it must be changed.

As already noted, a common objection to the WTO is that it overrules domestic laws. This is true, for that is its purpose. The GATT was a treaty among countries to prevent them from using certain laws and policies that would adversely affect each other. The WTO continues that purpose. However, while the original GATT dealt only with tariffs, over time the GATT/WTO has expanded to many other policies, such as environmental laws, whose main purposes are not international. Critics object that the WTO undermines domestic policies, not just tariffs. Countries might well want to reconsider membership if these new restrictions are too onerous. Had the WTO existed for 50 years without the opportunity to withdraw, this might be a big concern. However, since all members joined only six years ago, it would be surprising if many were now to pull out.

A troubling feature of the WTO for many is that countries may not restrict imports based upon the process by which they were produced. The WTO permits countries to exclude goods deemed harmful to health or the environment, for example, but only based on observable characteristics of the products themselves. In practice countries often want to exclude imports that were produced by a process that has harmed the environment, has violated labor standards or human rights, has adverse health consequences for consumers, or may be otherwise undesirable. These are often legitimate concerns, and if the process could be inferred from a product characteristic at the border, the WTO might permit their exclusion. But without that, exclusion must be based on the country where they were produced and some judgment about practices there. This runs the risk of excluding products that did not use the offending process, and also of undermining a producing country's legitimate comparative advantage.

A final concern of many WTO critics is that it is dominated by large corporations. This is true and probably inevitable, since it is large corporations that do most trade. Corporations have both the incentive and the resources to influence policies, and they do, both within countries and internationally. This means that the WTO has elements that would not be there without corporate lobbying, and some of these elements are undesirable. For example, antidumping statutes are economically nonsensical and pernicious, and yet the GATT has always permitted them, for the obvious reason that many corporations want them. More recently, in response to corporate lobbying the Uruguay Round added intellectual property rights to the WTO, in spite of strong resistance from developing countries that ultimately was overcome by the promise of market opening in textiles and apparel.[19]

The WTO, then, is not a perfect organization. It could be improved, but many of its flaws will inevitably remain, because they are there in response to political realities. Overall, it seems clear to us that the WTO serves an extremely useful purpose and that it serves it surprisingly well.

One indication that the WTO is not too far off the mark comes from its opponents. Although they share unhappiness with the WTO, some say that it does too much, others that it does too little. Environmentalists usually complain that it does too much, ruling against national efforts to improve the environment, and they want it weakened or destroyed so that national policies can proceed unhindered. Labor activists, on the other hand, complain that it does too little, not enforcing labor standards around the world. They want the WTO to take on more issues, and interfere more with national policies.

What Happened in Seattle?

All this is background for the events surrounding the WTO ministerial meeting in Seattle in December 1999. Ministerial meetings are held regularly, every two years in a different location, but the purpose of this particular meeting was well known: to agree on the parameters of a new round of negotiations. This did not happen. The meeting attracted protestors, and these demonstrated in the streets of Seattle and even prevented the opening session. The negotiators nonetheless did have extensive discussions, but they failed to reach agreement and left Seattle empty-handed.

One issue is, why? The protestors naturally took credit for derailing the new round and stopping the WTO in its tracks. However, most of those who were involved in the negotiations say that the protests had little to do with the failure.

The first problem was that the countries of the WTO had failed to agree beforehand on an agenda for these meetings. They had met at WTO headquarters in Geneva for months, trying to reach agreement, but they failed even then, long before the Seattle protests. The ministerial meeting nonetheless went ahead, but it was crippled by this failure in the preparations, which in turn was due both to bad luck and to the depth of the disagreements dividing the participants.

The bad luck was that the United States was distracted by its talks with China on terms of entry to the WTO. These negotiations had been expected to finish long before, but were instead delayed by the accidental bombing of the Chinese embassy in Belgrade. The negotiations with China were stalled, then continued, and finally concluded just shortly before the WTO ministerial. This prevented the United States from making all of the efforts that were needed to reach agreement on an agenda.

But agreement might have been elusive anyway. Large differences divided the participants, including whether even to discuss certain issues. In agriculture, the United States and LDCs sided with other agricultural exporters wanting to push ahead with negotiations. The European Union and Japan wanted nothing to do with that. The EU was however on the side of the United States on another issue: labor standards. Both wanted at least to talk about them in a new round, while LDCs, as noted here, were firmly opposed. LDCs, EU, and Japan sided together, against the United States, on anti-dumping. They wanted to reopen negotiations on this, in hopes of restricting the increasing use of these policies, but the United States refused. Finally, LDCs were unhappy with the backloading of the textile agreement and wanted to renegotiate the timetable, feeling that they had gotten very little market access in return for their acceptance of the TRIPS agreement. Here too, the United States and EU refused. On all of these issues, one of the parties did not want them even discussed.

There also were other problems encountered in Seattle. The United States, as host of the meeting, was pushing for a new round that would include many issues and proceed rapidly, perhaps causing some countries to feel they were being railroaded. Key players in the negotiations were new to their jobs, including especially Mike Moore, who had been installed as Director General of the WTO only a short time before. Finally, the desire for further multilateral liberalization may have been diminished by many countries' participation in various regional agreements, such as NAFTA, Mercosur, and the various free trade agreements of the EU.

Meanwhile, the protestors were gathered in unprecedented abundance. They included representatives of U.S. labor unions, labor rights activists, environmental groups, human rights advocates, and anti-corporate interests. Their disruption of the meeting was confined to conventional forms of protest, such as picketing, chanting, and blocking streets. However, the event and publicity also attracted a group of self-described anarchists. They had no particular interest in trade or the WTO, but were bent only on destruction, and they made news and enemies by throwing rocks and breaking windows. This drew more attention than peaceful protest ever would have, but it is not clear what effects it really had.

Toward the end of the week of meetings, with the negotiations making little progress, President Clinton arrived in Seattle and made a speech that seems to have derailed them completely. Previously, the United States and EU had both hoped to insert labor rights into the negotiations, but only in a small way. They tried to persuade the developing countries that the issue would only be discussed, not negotiated, and that there certainly would not be any use of trade sanctions in pursuit of labor rights. Whether this could have succeeded is unclear, but in any case, Clinton's speech explicitly mentioned using trade sanctions to enforce labor rights. From then on, developing country opposition hardened, even to discussion, and it became clear that no agreement on an agenda for a new round would be reached.

As we said, the protestors take credit for this failure, while the negotiators say that the protestors made little difference. We do not know who is right, and perhaps nobody does. It does seem that Clinton's speech was the final straw that prevented agreement, and he may have been influenced by the protests. On the other hand, even if he was responding to the protests, he may have decided that the meetings were going to fail anyway, and thus opted to collect political points for Al Gore from the opportunity. Or his first priority may have been permanent normal trade relations (PNTR) with China, and he did not want to anger labor further until after the election. We have no way of knowing.

It should be noted, however, that a failure of trade negotiations is hardly unprecedented. In the early 1980s, the United States also failed to initiate a new round, at another ministerial meeting. Later, with the Uruguay Round underway, negotiations collapsed several times, with no apparent hope of being restarted. Nonetheless they did, and the round eventually concluded successfully. It is therefore quite possible that what was not accomplished in Seattle will happen later, at another time and place.

What To Do?

What are the possible next steps, for those who support the WTO?[20] What can they (we) do? The most obvious option is simply to continue along the path already laid out in the Uruguay Round negotiations, which specified negotiations (the "built-in agenda") that must be pursued under that agreement. That is happening. Indeed, less informed protestors must have wondered, on February 8, 2000, when the *Wall Street Journal* headlined "WTO Will Launch Talks to Lower Trade Barriers," just how this could happen. This is *not* the new round that failed in Seattle, but only a scheduled review of barriers in agriculture and services. But it is good that countries are once again talking.

Perhaps most important for WTO supporters, however, would be to pursue any changes on which they and opponents can agree. This could increase support for the WTO. Many would favor improved transparency in the operations of WTO panels, and a greater effort on the part of the WTO and its friends to explain itself to the public. Indeed, this paper is an effort in the latter direction.

Some supporters of the WTO may also favor, or at least accept, greater participation by NGOs. If that participation is limited to the filing of friend-of-the-court briefs, which dispute settlement panels could choose to read or not as they see fit, then this might open up the process without unduly weighting it in favor of those with the most resources.[21] However, we still prefer that NGOs express their views through duly constituted national governments. If greater transparency serves better to inform the NGOs of what is being addressed in WTO discussions and DSM panels, then they should have no difficulty using governments to convey their views and the often valuable information that they can provide.

There is, however, one area where we definitely favor greater participation in the WTO. Developing countries must become more formally represented in WTO decision-making. Exactly how to do this, we do not know. Perhaps it could be a steering committee with both permanent members from the large developed countries and a rotating set of representatives from small and poor countries. It will not be easy to choose these representatives fairly. But it must be done, if the WTO is to move ahead in a world where developing countries play ever more important economic roles.

IV. Conclusion

In this conclusion, we try to distill what we have said into a list of the essentials:

On Globalization:

1. Globalization refers to the most recent expansion of global trade, together with expanding flows of real and financial capital across national borders.
2. Globalization increases average real incomes in all countries, but within countries the gains are shared unequally and some may lose.
3. Losers from globalization include owners of scarce factors, as well as those in contracting industries, if they cannot easily change their location, skills, or industry of employment.

On the WTO:

4. The WTO was formed by governments for the purpose of promoting globalization and preventing countries from doing harm with their trade policies.
5. Those who gain most from the WTO are those who gain from globalization, especially small, poor countries who would be most hurt by nationalistic trade policies.
6. The WTO limits those who would use trade policies for other goals, including environment, labor standards, and human rights, forcing them to pursue their objectives at less cost to other countries.

7. The WTO provides a dispute settlement mechanism that has been quite effective, but its operation has been less transparent than it could be.

8. The WTO operates by consensus, but its large membership makes that process unwieldy and exclusionary in practice, leaving many developing countries especially without a voice.

On Seattle:

9. The December 1999 protests at the Seattle ministerial heightened public awareness of globalization and the WTO, perhaps contributing to the failure to initiate a new trade round.

10. The more basic reason for the Seattle failure was the disagreements that divide major participants on agriculture, labor standards, anti-dumping, and market access in textiles and apparel.

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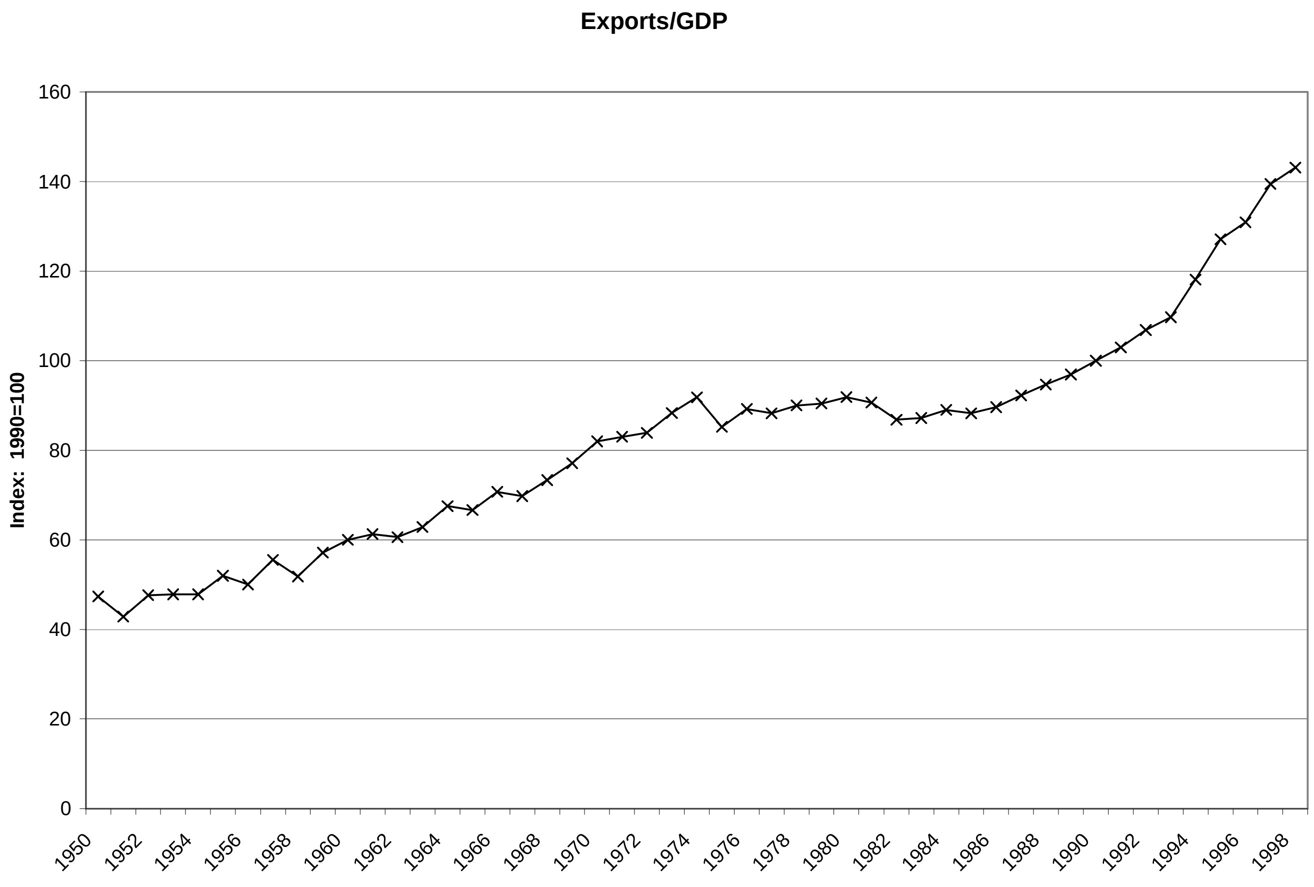
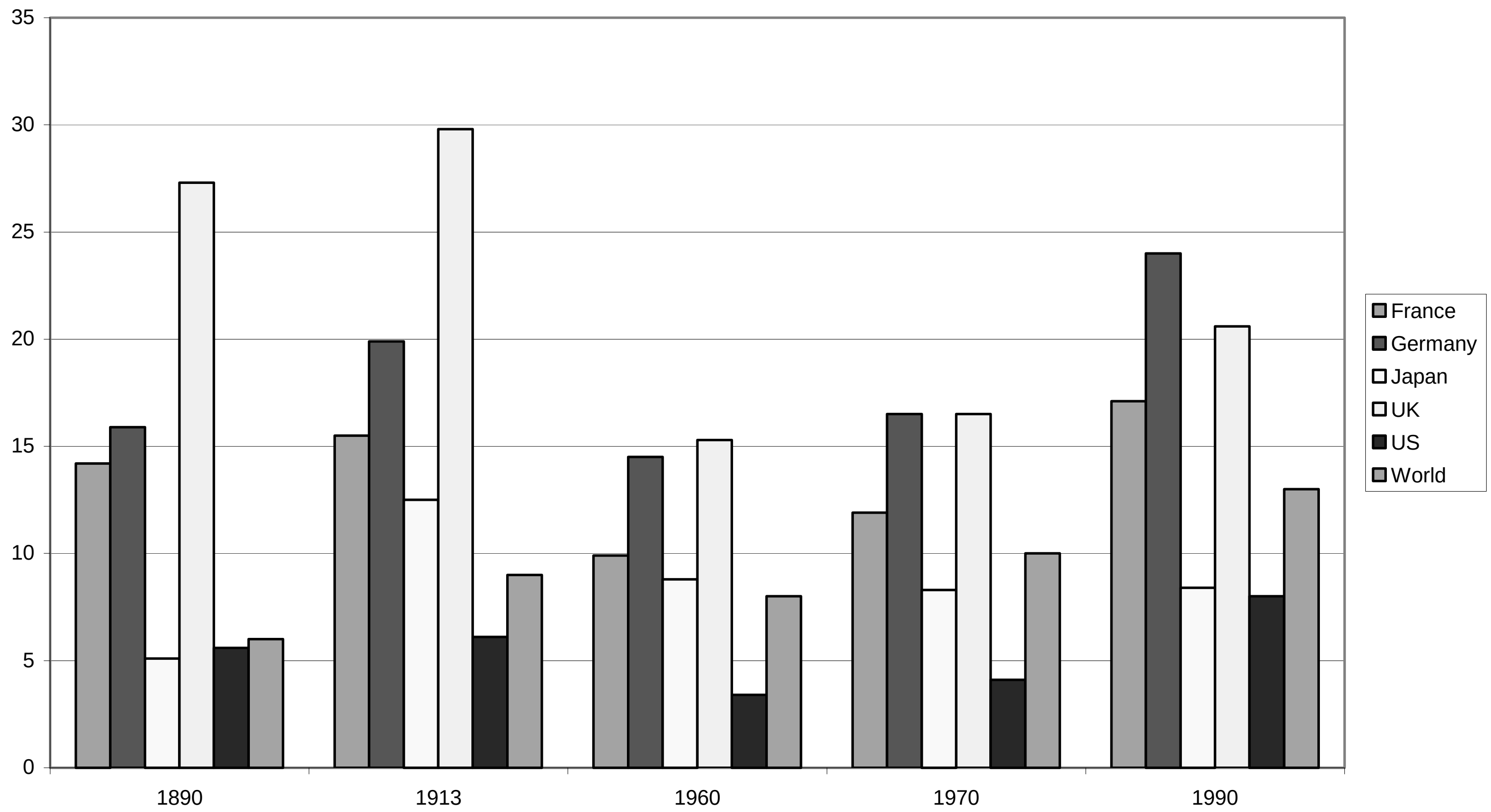
Figure 1
Index of Ratio of World Merchandise Exports to World GDP
1990=100



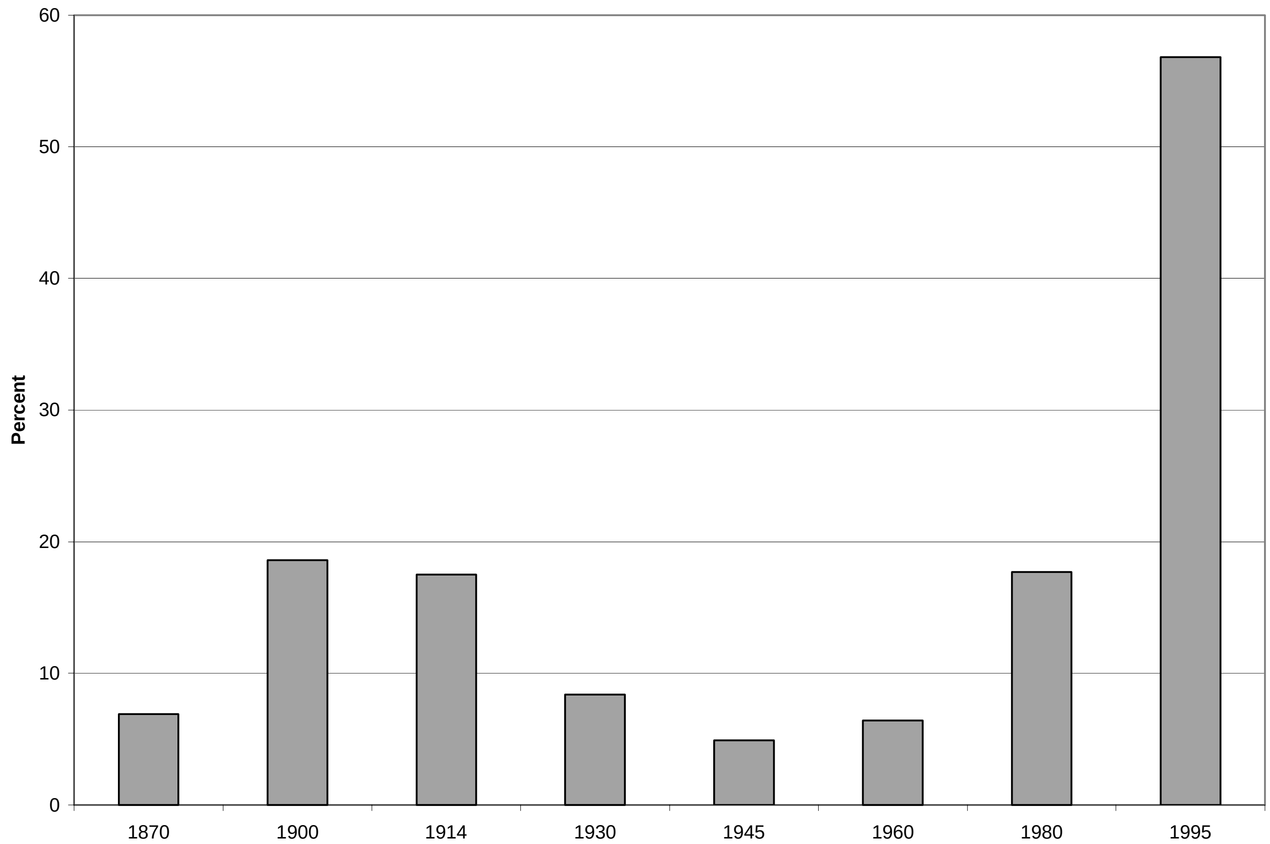
Source: WTO, International Trade Statistics, 1999

Figure 2
Ratio of Merchandise Exports to GDP for Major Countries and the World,
Selected Years 1890-1990
(Percent)



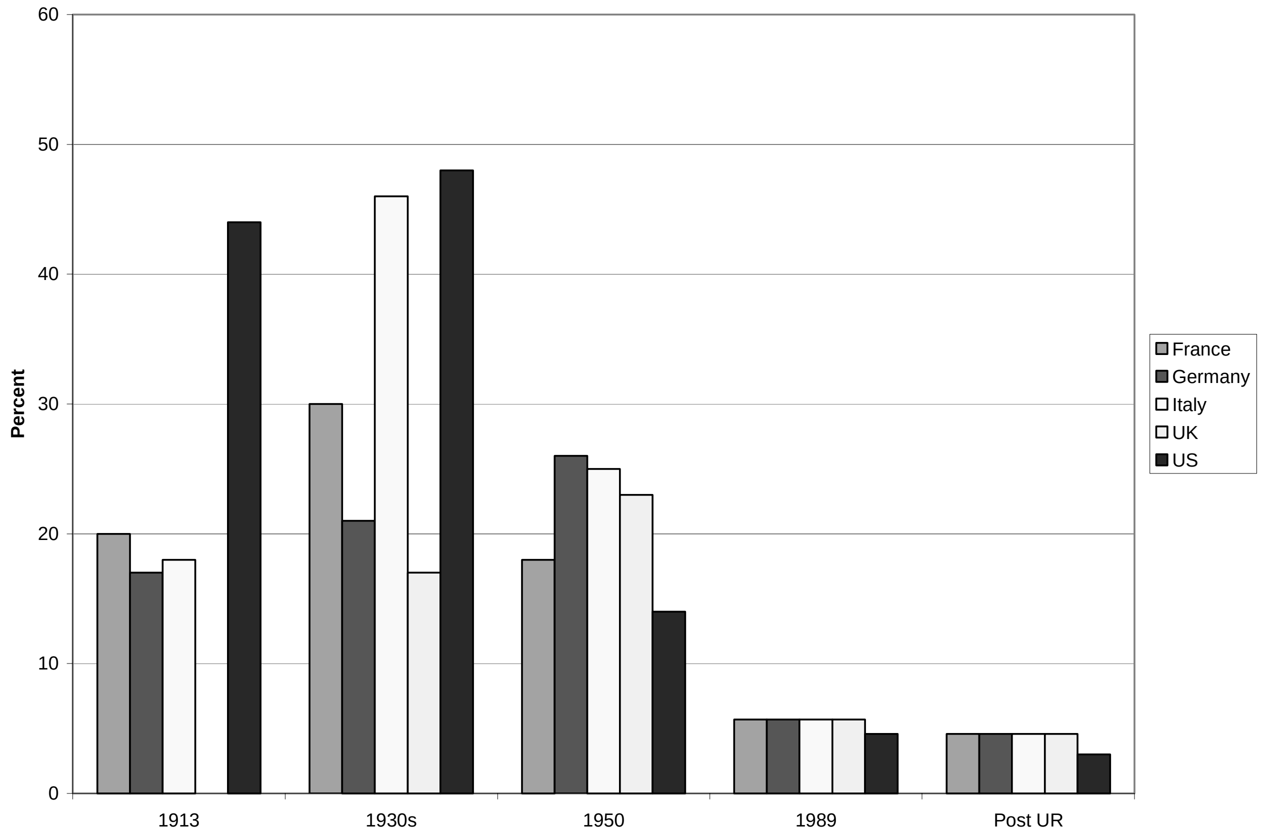
Source: Crafts (2000), Table 2.1, p. 26.

Figure 3
Ratio of Foreign Assets to World GDP
Selected Years 1870-1995
(Percent)



Source: Crafts (2000), Table 2.3, p. 27.

Figure 4
Average Tariffs on Manufactures
Selected Years 1913-Post-Uruguay Round



(Percent)

Source: Crafts (2000), Table 2.4, p. 28.

TABLE 1
WTO Disputes: Consultation Requests
January 1, 1995 to March 23, 2000

	Respondents					
Complaints by	United States	Japan	European Com.[a]	Oth. Ind. Countries	Dev./ Emerging	Total[b]
United States	–	5	25	7	24	61
Japan	4	–	–	–	3	7
European Communities	16	6	–	5	25	52
Other Industrialized Countries	5	1	5	3	12	26
Developing/Emerging Economies	17	–	17	1	25	60
Total[b]	43	11	47	16	89	206

Notes:
[a]Includes complaints against the European Communities (EC) as well as individual EC member countries.
[b]Totals reflect individual cases involving more than one country requesting consultation with respondent.

Source: World Trade Organization, "Overview of the State-of-play of WTO Disputes," http://www.wto.org./wto/dispute/bulletin.htm, 23 March 2000.

Notes

[*] We have benefited greatly from conversations with the economic and legal scholars who participated in a meeting at the Georgetown University Law Center on January 28, 2000. We also had useful comments from our students, from participants at a conference in Delphi, Greece, May 2000, where this was presented, and from an anonymous referee.

[1] There has also been a significant growth of services trade, as documented in the WTO, *International Trade Statistics*.

[2] There has *not* been a comparable increase in international labor mobility, which also reached a peak just before WWI.

[3] See Deardorff (1991). Note, however, that most NTBs in developed countries are scheduled to be eliminated by 2005.

[4] An exception, however, is agriculture, which is still subject to relatively high tariffs and other restraints.

[5] This statement is literally correct only if the word "average" refers to the simple arithmetic mean of incomes – that is, total income divided by total population. Given the very skewed distribution of income, this does *not* necessarily mean that the majority of consumers are better off, since in principle the rich could enjoy a disproportionate share of the gains. However, in practice the vast majority of consumers are likely to gain from trade, the losers being only the small minority whose incomes fall disproportionately due to direct competition from imports.

[6] These conclusions are, strictly speaking, theoretically valid only for countries that are too small to influence world prices with changes in their trade. For large countries, the "optimal tariff" is positive, allowing them to benefit somewhat at the world's expense. While this argument might apply to a country the size of the United States, we believe that U.S. levels of protection in sectors where it is highest are well above this "optimal" level, and in any case this argument for protection bears scant resemblance to what opponents of globalization have in mind.

[7] See Stolper and Samuelson (1941).

[8] Also in the long run, economic well being depends most on how rapidly countries grow. Here the role of trade is less well understood, but in recent decades countries have grown more rapidly with trade than without. See below.

[9] In Brown, Deardorff and Stern (1992), for example, we estimated the employment reallocation effects of the NAFTA for the United States, and found them to be much smaller than the normal turnover within U.S. industries in one year.

[10]Capital gains most if it starts in a capital abundant country and can earn more by going abroad, but this is just an example of factor abundance at work. The point here is different. Mobile capital, even in capital scarce countries, stands to gain from the potential to move, and this is an advantage that immobile labor lacks. This is most important in imperfectly competitive factor markets where the division of profits and rents depends on the bargaining power of the participants. Mobile capital, by threatening to move abroad, can reach a more favorable contract with immobile labor.

[11] Actually, there is one reason for hope, and it is globalization itself. Those who designed the postwar international institutions at Bretton Woods in the 1940s were not just seeking economic prosperity for the world. They hoped that trade and other forms of economic integration would make wars less likely in the future. Of course, the globalization at the beginning of the century had failed to serve that purpose.

[12] There are many sources of information about the GATT and WTO. See, for example, Deardorff (1997).

[13] For owners of textile firms it is more complicated. Developed-country firms may move production abroad. Some developing-country firms have prospered, using export licenses under the MFA to make extraordinary profits.

[14] See Jackson and Davey (1986, p. 917).

[15] The line between human rights and labor standards is not always clear. The right to organize and a safe workplace are both on most lists of labor standards, but they might also be regarded as human rights.

[16] For more on labor standards see Brown, Deardorff, and Stern (1996, 2001).

[17] As of 30 November, 2000, according to the WTO web site in May 2001.

[18] Our information comes from personal communication with Rufus Yerxa, who participated in these meetings on behalf of the United States during the Uruguay Round. He lists almost twenty countries as having

been present in the green room, including a handful of developing countries such as Brazil, India, and Nigeria.

[19] And despite arguments that they had no more business in the WTO than labor rights. See Deardorff (1990).

[20] For those who oppose it, the choices are working to cause its demise or working to change it. The first might best be accomplished by getting the United States to withdraw, perhaps by putting pressure on Congress. The second might ultimately happen in response to continued protests, although it would help if the protesters could agree on what they want.

[21] A recent Appellate Body decision has permitted such input to the DSM.