United States Government Accountability Office

GAO

Report to the Chairman, Committee on Finance, U.S. Senate, and to the Chairman, Committee on Ways and Means, House of Representatives

May 2005

WORLD TRADE ORGANIZATION

Global Trade Talks Back on Track, but Considerable Work Needed to Fulfill Ambitious Objectives

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Accountability * Integrity * Reliability

GAO-05-538

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GAO Accountability·Integrity·Reliability

Highlights

Highlights of GAO-05-538, a report to the Chairmen, Senate Committee on Finance and House Committee on Ways and Means

Why GAO Did This Study

The outcome of ongoing World Trade Organization (WTO) negotiations is vital to the U.S. economy, because trade with WTO members accounts for about one-fifth of the U.S. gross domestic product. The current round of trade negotiations—called the Doha Round—was supposed to end by January 2005 with agreement on the key issues of agriculture, industrial market access, services, and to strengthen the trading system's contribution to economic development. Failure to reach any agreement at the last WTO ministerial meeting in Cancun, Mexico, in September 2003, put the talks behind schedule and threatened the outcome; however, talks resumed in 2004, and a new ministerial conference will convene in Hong Kong in December 2005. In light of these events, and with the impending renewal decision on U.S. Trade Promotion Authority, which streamlines the process by which Congress approves trade agreements, GAO was asked to assess (1) the overall status of the Doha Round negotiations, (2) progress on key negotiating issues, and (3) factors affecting progress toward concluding the negotiations.

www.gao.gov/cgi-bin/getrpt?GAO-05-538.

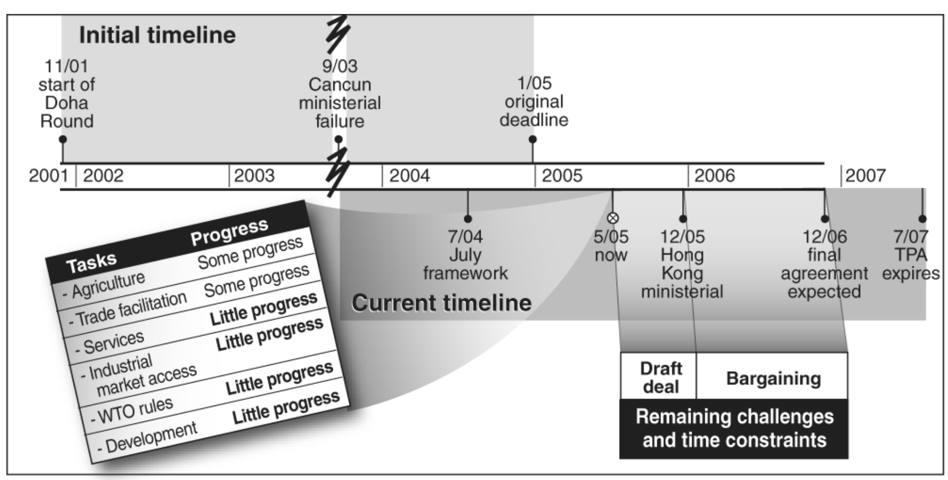
To view the full product, including the scope and methodology, click on the link above. For more information, contact Loren Yager at (202) 512-4347 or yagerl@gao.gov.

What GAO Found

During 2004, Doha Round negotiations got back on track as trade ministers signed a framework agreement known as the "July package." By committing to eliminate agricultural export subsidies, the agreement's main achievement was to recognize the importance of agriculture in the round and thus reopen talks on other issues. Since this breakthrough, negotiations are picking up momentum, as WTO members are working toward deadlines for more detailed agreements at the December 2005 Hong Kong ministerial conference. Yet despite the improved negotiating atmosphere, the talks are behind schedule, and considerable work remains on the numerous issues that must constitute a final agreement.

Progress has been uneven on the six negotiating issues identified as central to the Hong Kong meeting—agriculture, trade facilitation (customs reforms), industrial market access, services, WTO rules, and development issues. The United States has particular reform interests in the first four of these issues. Progress has occurred on two of them: in agriculture, based on agreements in the July framework, and trade facilitation, for which talks have finally been started. However, little progress has been made on industrial market access and services, two other issues of interest to the United States.

Several factors could affect progress in the critical period leading up to the December 2005 Hong Kong ministerial. Achieving consensus among the WTO's 148 members is a challenging task, and diverse economic incentives and competing visions add complexity to the negotiations. Cooperation by the United States, the European Union, and some of the developing countries is also seen as key to a successful conclusion before U.S. Trade Promotion Authority expires in mid- 2007, an implicit deadline for the talks.



Source: GAO analysis of WTO data.

Contents

GAO
Accountability * Integrity * Reliability

United States Government Accountability Office
Washington, D.C. 20548

May 31, 2005

The Honorable Charles Grassley
Chairman
Committee on Finance
United States Senate

The Honorable William H. Thomas
Chairman
Committee on Ways and Means
House of Representatives

U.S. trade with members of the World Trade Organization (WTO) totaled $2.1 trillion in 2004, accounting for almost one-fifth of U.S. gross domestic product. As such, the United States has a considerable stake in WTO negotiations launched in November 2001 that aim to liberalize trade by lowering tariffs and other distortions to global trade in agriculture, industrial goods, and services and to strengthen the trading system's contribution to economic development. Officially known as the Doha Development Agenda, the talks are being conducted under the auspices of the WTO and are the latest in a series of negotiating "rounds" among its members, which now number 148 nations and customs territories. Past GAO reports have highlighted the ambitious list of 19 substantive issues being addressed in what is now known as the Doha Round and the challenges WTO members have faced in making progress. Notably, the failure of the September 2003 meeting of trade ministers at Cancun, Mexico, set back the talks and made meeting the original January 2005 deadline for conclusion impossible. The President recently requested a 2-year extension of Trade Promotion Authority (TPA) from Congress, which streamlines congressional approval of trade agreements, for purposes of pursuing a final Doha Round agreement, among others. TPA legislation allows for such an extension unless a disapproval resolution is passed by either House of Congress by June 30, 2005. The U.S. Congress will also consider the 5-year WTO membership review, as called for in section 125 of the Uruguay Round Agreements Act.[1]

[1]Section 125 of the Uruguay Round Agreements Act requires the U.S. Trade Representative to report once every 5 years on the effects of the WTO agreement on the interests of the United States and the value of continued U.S. participation in the WTO. It sets forth a procedure whereby congressional approval of U.S. participation in the WTO could be withdrawn.

Given the importance to the United States of the WTO Doha Round and Congress's present TPA renewal decision, you asked GAO to provide a status report on the WTO negotiations. In this report, the latest in a series, we assess (1) the overall status of the WTO Doha Round negotiations; (2) developments on key negotiating issues since the previous (January 2004) GAO report; and (3) factors affecting progress in the negotiations.

To address these objectives, we met with and obtained documents from a wide variety of WTO, U.S., and foreign government officials, as well as academic experts and private sector groups (including business associations, law firms, and civil society groups), both in Washington, D.C., and Geneva, Switzerland. We also reviewed international tariff and trade data from the WTO and the United Nations. We determined that these data were sufficiently reliable for the purposes of our analysis. Appendix I provides a full description of the scope and methodology of our work. We conducted our work from March 2004 through March 2005 in accordance with generally accepted government auditing standards.

Results in Brief

Overall, the Doha Round is behind schedule, but the global trade talks have regained their footing and achieved some forward momentum since the failed Cancun ministerial. Leadership by both developed and developing nations, an improved process, hard work, and a willingness to compromise resulted in a July 2004 framework agreement widely credited with putting the Doha Round back on track. The negotiating participants we spoke with are generally pleased that a July 2004 framework agreement and its breakthrough in agriculture reform has succeeded in demonstrating broader commitment to success and effectively breaking the deadlock in the negotiations. Agriculture remains the top issue for many participants, and dissatisfaction with progress on agriculture has held up movement on the other 18 issues on the negotiating agenda. Negotiators report that the July framework has enabled technical negotiations to proceed in a much improved atmosphere, despite political transitions in some countries during the fall of 2004. Nevertheless, those with whom we spoke universally stressed that considerable work remains to be done if the Doha Round's promise is to be realized—particularly because simultaneous agreement on all issues is required for agreement. Moreover, progress thus far in 2005 has proved slower than hoped, causing WTO Director-General Supachai Panitchpadki to sound a warning over prospects for success in Hong Kong.

For its part, the United States has made it clear that issues besides agriculture are important to satisfy its balance of interests. It is seeking evidence of others' commitment to liberalize barriers to industrial goods and services by the pivotal December 2005 Hong Kong ministerial, whose goal is to set the stage so final bargaining can occur in 2006. Such progress is also vital to attaining U.S. Trade Promotion Authority objectives—and realizing U.S. economic gains—for the Doha Round.

Progress has been uneven among the six negotiating issues identified as key to the Hong Kong ministerial—agriculture, trade facilitation, industrial (nonagricultural) market access, services, development issues, and WTO rules. Two issues the United States has advocated have progressed. Discussions on agriculture are the most advanced, with the July 2004 framework capturing the important new commitment to eliminate all export subsidies at an agreed-upon date. The formal launching of talks on trade facilitation—the simplification and streamlining of customs procedures--also is progress on an issue increasingly seen as a "win-win" proposition for developed and developing countries alike. Little progress has been made on two other issues of interest to the United States. First, on industrial market access, the primary achievement has been to establish an agenda for discussion, though disagreement persists on the two main methods being considered for achieving substantial liberalization. Second, the current number and quality of offers on opening access to national services markets are still inadequate, according to participants. The remaining two issues are being pressed by other WTO members and also have not progressed very far. Debate over the July framework showed WTO members are still divided over how to best approach development issues, but more ready to consider practical accommodations to address concrete problems. Meanwhile, negotiations on various trade "rules" have intensified, with the United States and other members who are users of trade remedy laws facing calls for considerable change to their antidumping and countervailing duty regimes—measures used to counter unfairly priced and subsidized imports.

Several interrelated factors could affect progress in the critical months culminating in the Hong Kong ministerial. Achieving agreement among the WTO's large membership has long been recognized as complicated, given its consensus-based decision making structure. The task before WTO negotiators is particularly difficult, partly due to differences in the economic benefits and costs countries expect from trade liberalization. For example, some developing countries that currently benefit from preferential access to developed country markets are resisting ambitious reduction of multilateral trade barriers out of fear that it will erode their margins of preference and reduce their exports. Coalitions have been instrumental in consolidating views among like-minded members, but the active participation by developing countries that sometimes have competing visions to developed countries has added to the complexity of achieving consensus. Progress at the WTO still depends on strong leadership by—and good relations between—the United States and the European Union, but political transitions have preoccupied them into early 2005. Analysts agree that action on high-profile WTO dispute settlement cases such as cotton and sugar could prove important to ongoing agriculture negotiations. Moreover, proponents say the avid pursuit of trade negotiations outside the WTO is spurring on WTO progress, but others warn it is detracting attention and resources from the Doha Round. Several negotiators indicated that if extended for 2 years by June 1, 2005, the final expiration of TPA in mid-2007 is serving as the implicit deadline for the Doha Round, and effectively means it must conclude by December 2006. Finally, preparations for the Hong Kong ministerial have begun, but are still incomplete.

We conclude by noting that despite limited progress to date and considerable challenges ahead, some of the trade experts we consulted are confident that an ambitious, balanced outcome is still attainable—if 2005 results in sufficient progress. Others warn that hard decisions are necessary and time is short if an outcome that lives up to Doha's promises is to be achieved. We received comments on a draft of this report from the Office of the U.S. Trade Representative and the Departments of Agriculture, Commerce, and State indicating that these agencies generally agreed with our findings.

Background

The World Trade Organization (WTO) was established as a result of the Uruguay Round on January 1, 1995, as the successor to the General Agreement on Tariffs and Trade (GATT). Based in Geneva, Switzerland, the WTO administers agreed-upon rules for international trade, provides a mechanism for settling disputes, and serves as a forum for conducting trade negotiations. There are currently 148 WTO members, up from 90 GATT members when the Uruguay Round was launched in 1986 and from 128 members in 1995.

The highest decision-making authority in the WTO is the ministerial conference, which consists of trade ministers from all WTO members and occurs every 2 years.[2] The outcome of ministerial conferences is a ministerial declaration that guides future work. The WTO General Council, which consists of representatives from all WTO members, is empowered to make decisions between ministerial conferences. Decisions in the WTO are made by consensus—or absence of dissent—among all members rather than a simple majority.

At the fourth ministerial conference in Doha, Qatar, in November 2001, WTO members reached consensus to launch a comprehensive negotiating round, the Doha Development Agenda or Doha Round.[3] The Doha Round is the ninth round of trade liberalizing negotiations since the trading system's founding in 1947. These rounds result in legally binding international obligations on members both in terms of the trade barriers they are allowed to maintain, such as tariffs (import taxes), and the trade rules (disciplines) they are to abide by. Failure to comply is subject to binding dispute settlement and possible trade retaliation. In the Doha ministerial declaration, WTO members set a number of overall objectives for the round, such as the need to ensure that developing countries, particularly the least-developed, secure growth of world trade commensurate with their needs for economic development (see fig. 1 for a list of the overall Doha objectives). The declaration sets forth a work program that covers 19 negotiating areas, including agriculture, services, and market access for nonagricultural goods (also known as industrial market access).[4] Within each of those areas, WTO members set specific goals.[5] WTO members also established a Trade Negotiations Committee, chaired by the WTO Director General, to oversee the round's progress. Because the Doha Round is a

[2]According to WTO rules, ministerial conferences are to be held at least once every 2 years.

[3]For additional information on the fourth ministerial conference and the Doha Development Agenda, see GAO, *World Trade Organization: Early Decisions Are Vital to Progress in Ongoing Negotiations*, GAO-02-879 (Washington, D.C.: Sept. 4, 2002).

[4]The 19 negotiating areas are implementation-related issues and concerns; agriculture; services; market access for nonagricultural products; trade related aspects of intellectual property rights; relationship between trade and investment; interaction between trade and competition policy; transparency of government procurement; trade facilitation; WTO rules; dispute settlement understanding; trade and environment; electronic commerce; small economies; trade, debt, and finance; trade and transfer of technology; technical cooperation and capacity building; least-developed countries; and special and differential treatment.

[5]A detailed discussion of the goals for each area is provided in the appendixes of this report.

package, or “single undertaking” in WTO parlance, simultaneous agreement on all issues is required to finalize an agreement.

In negotiating the Doha Round on behalf of the United States, the Office of the United States Trade Representative (USTR) is also guided by certain goals, notably the goals outlined by the Trade Promotion Authority (TPA) granted by Congress in 2002. TPA’s goals for USTR negotiators include overall and principal objectives and promotion of certain priorities. In addition to TPA, USTR has its own goals for the Doha Round outlined in a required official notification to Congress in November 2002.[6] (See fig. 1 for a description of the TPA and USTR goals.) In general, USTR states that it plans to use the Doha Round negotiations to strengthen the multilateral trading system, improve the operation of the WTO, and liberalize international markets. USTR places special emphasis on creating new export opportunities for the United States in agriculture, manufacturing, and services. USTR must explain how any resulting agreement makes progress towards TPA goals when submitting it for consideration for congressional approval under TPA’s expedited approval procedures. TPA is set to expire in mid-2005, but provides a procedure for the President to request a one-time extension of the authority to July 1, 2007. The President recently requested such an extension, which is automatic unless Congress disapproves it by June 30, 2005.

[6]Such notification is required by law, under the Bipartisan Trade Promotion Authority Act of 2002 (P.L. 107-210). The issue areas USTR specifies goals for are trade in agricultural goods, trade in industrial and other goods, trade in services, trade in intellectual property rights, electronic commerce, trade facilitation, trade and investment, government procurement, competition policy, transparency/regulatory reform, labor (including child labor), regional trade agreements, trade and the environment, fisheries subsidies, border taxes, trade remedy laws and disciplines, and dispute settlement.

Table 1: Overall Goals for the Doha Round Negotiations from the Doha Declaration, U.S. Trade Promotion Authority Legislation, and USTR

Doha Declaration Goals

- To maintain the process of reform and liberalization of trade policies, thus ensuring that the system plays its full part in promoting recovery, growth, and development.
- To ensure developing countries, and especially the least-developed among them, secure a share in the growth of world trade commensurate with the needs of their economic development.
- To address marginalization of least-developed countries in international trade and to improve their effective participation in the multilateral trading system.
- To stress commitment to the WTO as the unique forum for global trade rulemaking and liberalization, while also recognizing that regional trade agreements can play an important role in promoting the liberalization and expansion of trade and in fostering development.
- To continue to work with the Bretton Woods institutions for greater coherence in global economic policymaking.
- To reaffirm commitment to the objective of sustainable development.
- To reaffirm the right of members under the General Agreement on Trade in Services to regulate, and to introduce new regulations on, the supply of services.
- To reaffirm commitment to internationally recognized core labor standards.
- To attach great importance to concluding accession proceedings as quickly as possible, particularly for least developed countries.
- To ensure internal transparency and the effective participation of all members.

TPA Goals

- To obtain more open, equitable, and reciprocal market access.
- To obtain the reduction or elimination of barriers and distortions that are directly related to trade and that decrease market opportunities that otherwise distort U.S. trade.
- To further strengthen the system of international trading disciplines and procedures, including dispute settlement.
- To foster economic growth, raise living standards, and promote full employment in the United States and to enhance the global economy.
- To ensure that trade and environmental policies are mutually supportive and to seek to protect and preserve the environment and enhance the international means of doing so, while optimizing the use of the world's resources.
- To promote respect for worker's rights and the rights of children consistent with core labor standards of the International Labor Organization.
- To seek provisions in trade agreements under which parties to those agreements strive to ensure that they do not weaken or reduce the protections afforded in domestic environmental or labor laws as an encouragement for trade.
- To ensure that trade agreements afford small businesses equal access to international markets, equitable trade benefits, and expanded export market opportunities, and provide for the reduction or elimination of trade barriers that disproportionately impact small businesses.
- To promote the universal ratification and full compliance with the International Labor Organization Convention Concerning the Prohibition and Immediate Action for the Elimination of the Worst Forms of Child Labor.

USTR Doha Round Goals

- To open markets around the globe for American workers, farmers, and companies, with special emphasis on creating new export opportunities in agriculture, manufacturing, and services.
- To bring home a set of world trade agreements that enhances economic growth and prosperity in the United States and its trading partners (especially in the developing world, most notably in Africa) by reducing and eliminating barriers to trade.
- To strengthen the multilateral trading system and improve the operation of the WTO.

Sources: WTO, TPA, and USTR documents.

Note: Goals for each specific negotiating area or issue were also set.

The Doha declaration also set several goals for the following ministerial conference. However, at the ministerial conference held in Cancun, Mexico, from September 10-14, 2003, WTO ministers were unable to achieve these goals or to bridge wide, substantive differences on individual negotiating issues. They concluded the unsuccessful conference with WTO members sharply divided along North-South (developed-developing country) lines and agreed only to continue consultations and convene a meeting of the General Council by mid-December 2003 to take steps to move the negotiations forward. As we noted in our January 2004 report,[7] the Doha Round of WTO negotiations had missed virtually all of the established milestones for progress during its first two years. The breakdown at Cancun threatened to derail the talks completely. The December 2003 General Council meeting did not result in any agreements, except to resume talks in early 2004. As a result, WTO negotiators missed the original deadline of January 1, 2005, for concluding a Doha Round agreement. Thus, at the time our last report was issued, in January 2004, the Doha Round's prospects were uncertain.

Doha Round Behind Schedule but July Framework Injected New Momentum into Trade Talks after Failed Cancun Ministerial

Despite the Doha Round starting 2004 on an uncertain note, political leadership, intensified dialogue, and a series of conciliatory gestures resulted in adoption by WTO members of a framework agreement on key negotiating issues called "the July framework" or "package." The framework is credited with putting global trade talks back on track, and participants report that they have finally begun to make progress. Recent high-level meetings have sought to focus and accelerate work that leads up to a December 2005 ministerial conference in Hong Kong. The Hong Kong meeting is now hoped to result in decisions that will help determine how ambitious the Doha Round will be in terms of cuts in subsidies, tariffs, and other barriers. But even if negotiators reach the goal of setting the stage for finalizing a Doha Round agreement in 2006, WTO negotiations are about 2 years behind their original target date.

[7] GAO, *World Trade Organization: Cancun Ministerial Fails to Move Global Trade Negotiations Forward; Next Steps Uncertain*, GAO-04-250 (Washington, D.C.: Jan. 15, 2004).

Shows of Leadership and More Interactive Process Spur Progress

Contrary to post-Cancun gloom, 2004 witnessed a resumption of Doha negotiations. Active leadership by the United States and the European Union (EU) proved essential to progress, as did a more interactive process and hard bargaining. Former U.S. Trade Representative Robert Zoellick is widely credited with taking the initiative to resume talks with a January 2004 letter to fellow trade ministers urging them to keep 2004 from being a lost year for the WTO and suggesting various ways to make the agenda more manageable. He followed up on the letter with extensive foreign travel to meet with other WTO nations and rally support for resuming talks. WTO Director-General Supachi also traveled extensively as part of an active outreach effort to WTO member country officials.

WTO members reactivated Doha negotiating groups in February 2004 with new chairs intent on ensuring more fruitful member-to-member discussions. Summing up the status after his visits with foreign officials, Ambassador Zoellick concluded that a breakthrough on agriculture was "absolutely the key" to progress. WTO members undertook intensive efforts to reach a breakthrough on agriculture both in Geneva and at high-level meetings among key nations. Observers credited the EU Trade Commissioner Lamy's offer in May to eliminate export subsidies with providing a tangible incentive to reach agreement on agriculture. Several conciliatory initiatives were also taken to allay specific developing country concerns. For example, a workshop held in Benin emphasized the importance of cotton reform to growth and poverty reduction in Africa. To alleviate poorer countries' concerns over adjustment costs that were holding back overall trade liberalization, the EU suggested the WTO's poorest members in Africa and elsewhere should be offered the "Round for Free"—that is, they would benefit from others' concessions without having to offer much if anything in return. The offer sparked a debate over this differentiation by making it clear that the EU felt the Doha Round offered, and expected, more of other developing countries.

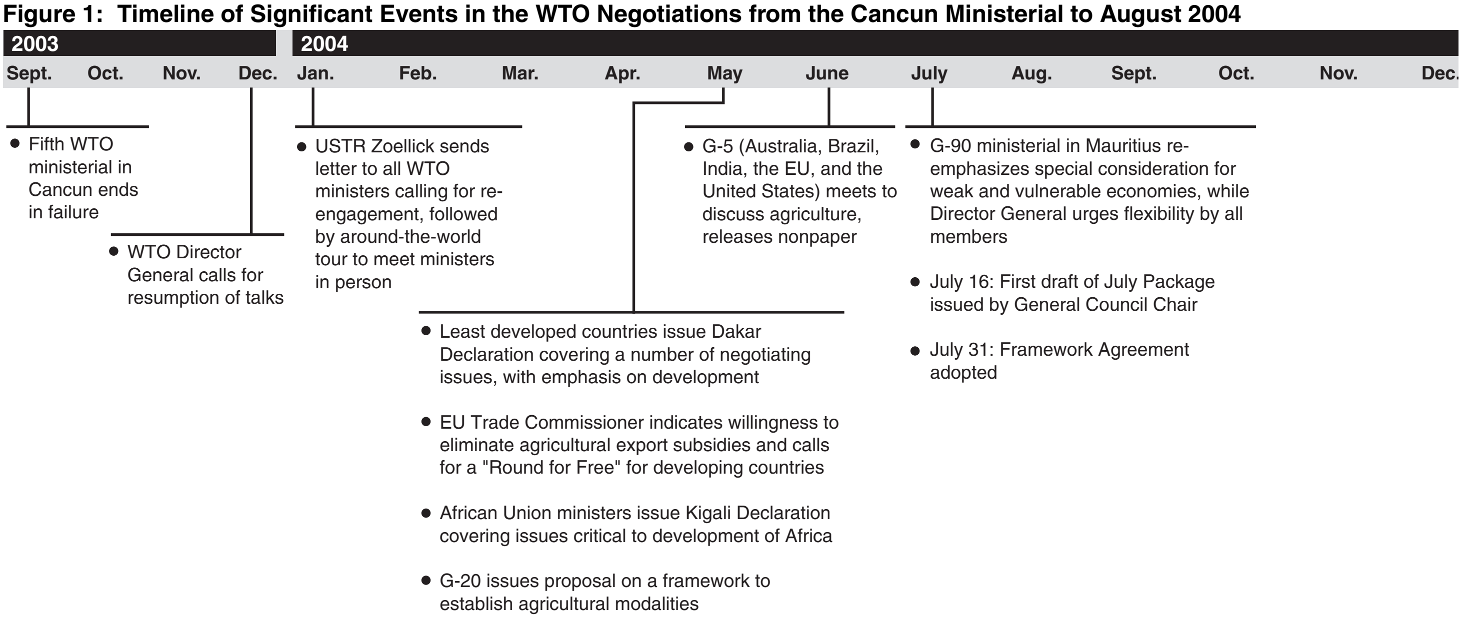
Developing countries also took on leadership roles and actions that contributed to progress. After Cancun, there was skepticism in some quarters as to whether the newly-created coalitions of developing countries would be able to maintain cohesion and play constructive roles. However, according to other participants, throughout 2004, these groups articulated their positions clearly and negotiated effectively with other groups, including the industrialized countries. For example, the group of populous developing countries with agricultural interests known as the Group of 20 (G-20) issued a late May paper setting forth principles to govern tariff cuts to help bridge wide differences in agricultural market access. Malaysia played a key role in shaping the novel terms for trade facilitation negotiations.

The WTO negotiating process also became more effective, contributing to progress. In our last report, we noted that the WTO's large number of members made formal gatherings increasingly ineffective and more suitable for speech-making or restating well-known-positions than for advancing the negotiations. Moreover, members often focused their efforts toward influencing the negotiating group chairmen, rather than other members. In early 2004, a series of mini-ministerials and other smaller, informal group meetings were used to foster direct interaction between members and became the real venues for moving the negotiations forward. Negotiating groups on specific issues also adopted informal meetings that featured more direct member-to-member dialogue rather than the prior chair-driven process.

Yet, leadership and process improvements alone were not sufficient to attain agreement. Hard work and willingness to compromise were also required. The wide remaining gaps on agriculture and unrealized demands on other issues were apparent at a late June 2004 meeting of the WTO Trade Negotiations Committee. WTO Director General Supachai Panitchpadki urged members then, and at a ministerial among African nations shortly thereafter in Mauritius, to seize the opportunity before them and show the flexibility required to seal a deal. With the July 16 release of a draft text, 2 weeks of day-and-night negotiating—often in intensive small group settings—were begun. An ad hoc group called the Five Interested Parties (or Group of Five)—composed of five key players in agriculture[8]—was critically important in bridging developed/developing country differences and shaping agreement (even though some members, such as the Group of 10 net agricultural importers, complained about being left out of these deliberations). Finally, on July 31, 2004, WTO members reached a deal on a framework agreement and adopted it formally at a WTO General Council meeting.

[8]The group included Australia, Brazil, the European Union, India, and the United States.

Figure 1: Timeline of Significant Events in the WTO Negotiations from the Cancun Ministerial to August 2004



Source: GAO, based on WTO, USTR, and other information.

The main features of the July framework agreement were: establishing key principles for each aspect of global agricultural trade reform, launching negotiations to clarify and improve WTO rules on customs procedures (trade facilitation), identifying the key elements of negotiations to improve industrial (nonagricultural) market access, and stressing the importance of liberalizing access to services markets and addressing outstanding development concerns.[9] It also set a notional December 2005 date for the next WTO ministerial in Hong Kong but did not set a new deadline for concluding the Doha Round. A veteran U.S. negotiator suggested they had pleasantly “surprised themselves” in reaching agreement at the WTO on a long-sought framework. The framework was widely praised by its key architects and many of their stakeholders, though it drew skepticism from some corners.

[9]The full framework (World Trade Organization, “Doha Work Program: Decision Adopted by the General Council on 1 August 2004,” WT/L/579, Aug. 2, 2004) is available at www.wto.org.

July Framework Unlocks Negotiations and Improves Negotiating Atmosphere

The July 2004 framework is widely credited with putting the Doha Round "back on track" and renewing political commitment to its ultimate success. Up until then, it had proved impossible to make meaningful progress on any of the other 18 issues of the round because key members linked movement on those issues to satisfactory progress on agriculture. Several participants went so far as to suggest that the July 2004 framework meant WTO members had prevented failure in the Doha Round and the WTO from becoming obsolete as a forum for liberalizing trade. A number of officials and experts we met with maintain that the package represents important progress and provided a sound basis for productive technical work on all issues during an anticipated political hiatus in the fall of 2004, when the European Commission changed and the United States held elections.

Considerable Work Remains on All Issues

While GAO's examination does reveal some progress on all fronts either in the July framework or afterwards, participants and experts widely agree that considerable work remains on all issues if the Doha Round is to be concluded successfully as a package deal. Notably, experts agree that translating political commitment into concrete cuts in agricultural subsidies and tariffs involves grueling negotiations over myriad technical details. Without such commitment, loopholes and exemptions could undermine hoped-for liberalization. Moreover, agriculture is recognized as having achieved greater progress than other issues, such as industrial market access and services, which are essential for attaining an acceptable balance of issue interests among the WTO's 148 members. While cautioning that each issue will advance at its own rate and urging others not to insist on lock-step progress, U.S. negotiators have made it clear they must see evidence of others' commitment to liberalize barriers to industrial goods and services by the WTO ministerial now officially slated for December 13-18, 2005, in Hong Kong so that member-to-member negotiations can begin in earnest. Such progress is also vital to attaining U.S. TPA objectives—and realizing U.S. economic gains—for the Doha Round.

Next 6 Months Will Determine How Ambitious the Doha Round Will Be

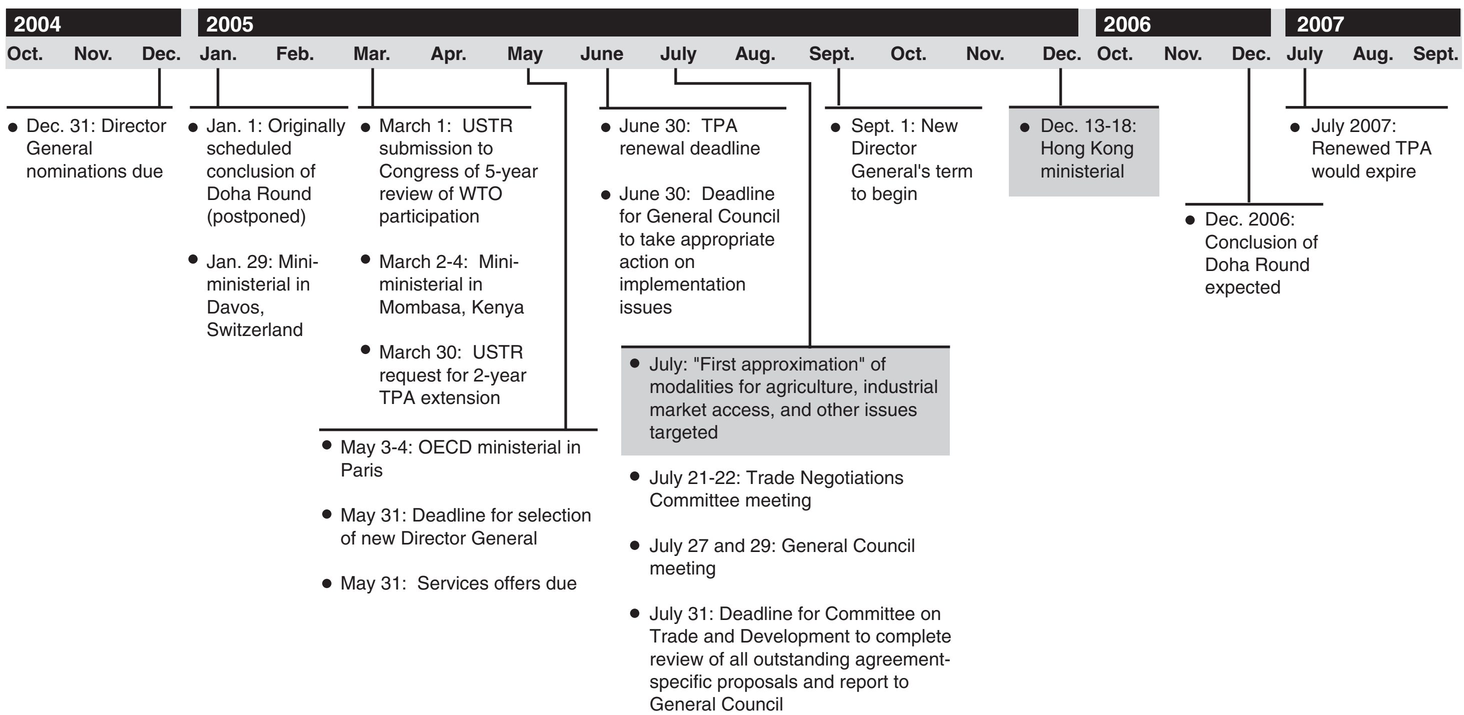
With tough battles on the details of agriculture reform ahead and the need for progress on other issues, the coming 6 months are crucial. U.S. negotiators are hopeful that groups will concentrate on working through the issues and ensure they are sufficiently advanced to obtain needed decisions by the December 2005 Hong Kong ministerial. If so, and if the Hong Kong ministerial results in the needed decisions, there is at least a reasonable prospect for the talks to conclude by the end of 2006 with meaningful results.

Early 2005 high-level meetings have sought to focus negotiations ahead of the December 2005 Hong Kong ministerial. At the late January 2005 mini-ministerial in Davos, Switzerland, and the subsequent mid-February Trade Negotiations Committee meeting, WTO members generally agreed to focus on six issues in Hong Kong. These six issues are: (1) agriculture, (2) industrial or nonagricultural market access (NAMA), (3) services, (4) trade facilitation, (5) "rules" such as subsidies and antidumping, and (6) development. They also generally agreed that the Hong Kong ministerial's goal is to set the stage for final negotiations in 2006.

Although there is not yet agreement about what this entails, U.S. negotiators report that it is widely accepted that by the time of the Hong Kong ministerial WTO negotiators should seek to finalize "modalities" on agriculture and NAMA—that is, numerical targets, formulas, industrial sectors for potential sectoral agreements, and technical guidelines for countries' commitments on cutting tariffs and subsidies. By the Hong Kong ministerial, negotiators should also have made progress in services, market access, and rules discussions and narrowed the focus, and possibly have begun to outline or draft texts on trade facilitation and development issues.

These deliverables will be critical in determining how ambitious the Doha Round will be in terms of cuts in tariffs, subsidies, and other barriers to trade, and what the overall balance will be across various issues. Finalizing modalities is also an important interim step before concrete negotiations can occur among WTO members. WTO members had hoped that by mid-July 2005 they would be able to get a sense of how well their balance of issue interests are being met through such means as producing a "first approximation" of the relevant texts or conducting stocktaking meetings on negotiating progress. However, at a late April 2005 TNC meeting WTO Director-General Supachai expressed concern about meeting these goals, noting that across the board progress has fallen short of what is required. He urged greater unity of purpose and warned that without better progress, WTO members could be facing major problems for Hong Kong. At an early May 2005 meeting of the Organization for Economic Cooperation and Development (OECD) in Paris, ministers called for a heightened sense of urgency in the negotiations and expedited preparations for the Hong Kong conference. After the Paris meeting, trade officials from certain WTO members reached an informal agreement on a technical issue—on the method for converting specific tariffs to ad valorem[10] tariffs—that was considered significant because it had been blocking progress in the agriculture negotiations for months.

Figure 2: Key Milestones in the WTO Negotiations in 2005 and Forward



Source: GAO, based on WTO, USTR, and other information.

WTO Negotiations Are About 2 Years Behind Their Original Target Date

Even with the July framework and a successful Hong Kong ministerial, slow overall progress and the Cancun setback means the Doha Round now is unlikely to conclude before December 2006, 2 years after the originally established deadline of January 2005. However, past rounds have taken

[10]"Ad valorem" signifies any charge, tax, or duty that is applied as a percentage of value. An ad valorem tariff rate is a trade tax calculated as a percentage of the value of the product being traded.

longer than originally planned, and the last two rounds—which involved fewer countries—each took 6 or more years to complete.

Experts offer mixed views as to whether this lag is cause for concern. A number of experts we spoke with stressed that the real question is not how long the round is taking, but how ambitious—in terms of liberalization and reform—the Doha Round's result will be. Some were fairly pessimistic. For example, one USTR and WTO Secretariat veteran termed the progress to date not only pitiful but worrying. Another expert said he did not believe the round was on track for achieving its ambitious liberalization and development objectives and expressed concern because the hardest issues still have not been tackled. As a result, this expert felt that the round would only conclude by December 2006 if work accelerates and political engagement increases. However, other experts said it is too early to give up on the round's success. One expert stressed that ups and downs—such as build-ups before deadlines and let downs after missing milestones—are typical in trade negotiations. Another expert noted that failures can often be vital to achieving worthwhile agreements and suggested Cancun was such an event. Both he and another expert indicated that there is still time for the Doha Round to conclude with meaningful results in all key negotiating issues. However, they said there is no more time to spare if a balanced, ambitious package is to be attained because even past rounds have required at least a year and a half of very hard bargaining to conclude. That time is upon us, if one works backwards from the July 1, 2007, expiration of any renewed U.S. Trade Promotion Authority.

Negotiators Have Made Uneven Progress in Key Issue Areas

Negotiating progress has varied markedly in the six issues designated as key work areas at the upcoming Hong Kong ministerial—(1) agriculture, (2) trade facilitation, (3) industrial (nonagricultural) market access, (4) services, (5) development issues, and (6) rules. Some advances have been clear in two issues advocated by the United States, agriculture and trade facilitation, although negotiations in the latter have just begun. As detailed in appendixes III and IV, very limited progress has occurred so far in two other issues being advocated by the United States—industrial market access and services. Progress has also been limited on two other issues being advocated by other WTO members—development-related issues and rules. Reform of WTO rules remains an area of controversy, with the United States and other users of the trade remedy laws pitted against many other countries over whether to maintain and even strengthen current rules.

Progress Made in All Three Pillars of Agricultural Reform, but Difficult Debate Lies Ahead

As detailed in appendix II, negotiators pressed hard in 2004 to make some progress on all three pillars for agricultural reform: (1) export competition, (2) domestic supports and (3) market access. The centerpiece of WTO member countries' efforts was the July 2004 framework agreement to remove all export subsidies at a future date. This commitment had long been sought by the United States and other nations, but involved a trade-off: the agreement to negotiate disciplines in other agricultural export competition programs, including U.S. export credit and food aid programs, and state trading enterprises. The framework also set ceilings on certain trade-distorting domestic supports (subsidies), though negotiators will need to further define and set comprehensive reduction schedules for such trade-distorting domestic supports. The framework also establishes the principle that countries with higher trade-distorting domestic supports and tariffs reduce them comparatively more.

Export competition, domestic supports, and market access comprise the "three pillars" within WTO agricultural negotiations.

- Export competition refers to a variety of programs designed to promote a country's exports, including export subsidies contingent on export performance, export credit programs, and state trading enterprises.
- Domestic supports, often called "subsidies," are payments made to farmers who raise prices or guarantee income. They include such measures as government buying at a guaranteed price, commodity loan programs, and direct payments to farmers.
- Market access refers to lowering tariff and non-tariff barriers to trade, such as tariff rate quotas.

Market access, the third area of reform, proved the most difficult to negotiate. As further explained in appendix II, the July framework established a principle of tiered and harmonized reductions in tariffs, but did not resolve the differences on how this would be accomplished. Negotiators still need to agree on numerous outstanding details if WTO members are to achieve modalities at the December 2005 Hong Kong ministerial. Technical work on issues including tariff rate quota administration,[11] export credit repayment terms, and converting tariffs into ad valorem equivalents has begun. Yet, the months-long stalemate on the last issue frustrated progress until May 2005. Moreover, according to many experts, the big battles that will determine how ambitious the Doha round will be— over whether and how trade-distorting domestic support categories will be redefined, setting domestic support and tariff reduction formulas, and defining the sensitive and special products that can be insulated from tariff cuts—remain to be fought.

Launched after Years of Discussion, Trade Facilitation Negotiations in Early Stages

WTO members finally agreed in the July framework to formally launch negotiations on trade facilitation (customs reforms). Trade facilitation, together with three other issues—investment, government procurement, and competition policy—had been under consideration and intense debate by WTO members for the past 7 years (since the Singapore ministerial).

[11]Tariff rate quotas are a tariff whereby lower tariffs are specified for a specific quantity and higher tariffs are specified for quantities that exceed the quota.

Trade facilitation is an issue that the United States is very interested in bringing into the trading system in order to establish the transparent and swift customs procedures that are vital to realizing the benefits of market access concessions. The July framework contained agreement by explicit consensus to begin negotiations on trade facilitation and contained an annex specifying the goals, scope, and other understandings associated with their launch.[12] Notably, WTO members agreed that "the extent and timing of entering into commitments [on trade facilitation] shall be related to the implementation capacities of developing and least-developed [WTO] (m)embers. . . ." WTO members also decided to halt work toward negotiations on the remaining three "Singapore issues" of investment, government procurement, and competition policy for the remainder of the Doha Round. Since the July framework, WTO members created a negotiating group and selected a chair. The group has met several times, and various countries, including the United States, have tabled proposals. According to a U.S. trade official, two potentially difficult issues are dispute settlement and technical assistance to help developing countries defray implementation costs. While WTO members did not set specific goals on trade facilitation for Hong Kong, the United States is hopeful that negotiators can make meaningful progress in evaluating proposals. Some experts we spoke with said that progress on this issue is increasingly seen as a "win-win" proposition for developed and developing countries alike.

Little Progress in Narrowing of Differences on Industrial Market Access

As detailed in appendix III, thus far WTO members have made little progress in negotiations aimed at securing improved industrial market access, a key U.S. objective in the Doha Round. The July framework for industrial market access established an agenda for discussion and, since July, negotiators have addressed some technical issues. However, disagreement persists over the two main methods being considered for liberalization of trade in industrial goods: the tariff reduction formula and sectoral initiatives that would further reduce tariffs in agreed-upon sectors. Such disagreement is reflected in the lack of consensus over the tariff reduction guidance in the July framework. As of late April 2005, disagreement continued over the type of tariff reduction formula to use, the extent of exceptions to the formula that would be available to developing countries, and whether or not sectoral agreements should be included and

[12]See paragraph 1g. and Annex D of World Trade Organization Document WT/L/529, August 2, 2004.

on what terms. Nevertheless, achieving a meaningful agreement in industrial market access will be essential for the United States.

Services Talks Still Lagging

Services liberalization is also a key U.S. objective in which progress is lagging, as discussed further in appendix IV. Initially thought to be a lynchpin of the Doha Round, services talks have taken a back seat relative to other issues. Although several economists and trade experts argue that both developed and developing countries would greatly benefit from services trade liberalization, certain developing countries perceive this goal as a developed country priority. Nevertheless, the inclusion of services in the July framework, on an equal footing with agriculture and industrial market access, represented a victory of sorts and resulted from efforts on the part of both developed and developing country members. Since the July framework, talks on the domestic regulation of services have shown signs of progress. Technical negotiations on market access are also underway but have yet to translate into many new or improved offers in the lead up to May 31, 2005, the deadline set by the July framework. As a result, WTO members and officials remain disappointed with the number and quality of offers. For example, many developing countries have a keen interest in liberalizing the temporary movement of service professionals, but developed countries have so far shown few signs of movement towards more responsive offers.

WTO Members Still Divided Over How to Approach Development Issues

On development, WTO members are grappling with developing country concerns in the areas of special and differential treatment (S&DT) and implementation of their past WTO commitments in light of the July framework's calls for decisions by July 2005. Conceptual divisions between developed and developing countries, and among developing countries, remain unresolved. They involve such basic issues as whether participating in trade liberalization and abiding by the agreed-upon trade rules is good or bad for development and whether S&DT is an across-the-board right for all developing countries, or an ad hoc privilege available only on a case-by-case basis to meet justified needs, particularly of the WTO's poorest members. The chair has had only limited success to date in getting members to move to a practical, problem-solving stage.[13] However, as negotiations on agriculture and other market access areas move forward, specific S&DT language is being included. Certain negotiators told us that future progress on S&DT seems increasing likely to come out of technical negotiations within specific negotiating committees, more so than the Committee on Trade and Development, which examines it as a systemic issue.

Negotiations on Antidumping Rules Intensifying, with United States on Defensive

Review and possible reform of WTO "rules" for trade remedies such as antidumping against unfairly priced imports is prominent and controversial in the Doha agenda, though not in the July framework. Other WTO members, notably a coalition of 15 developed and developing nations known as Friends of Antidumping Negotiations, have advanced numerous proposals for extensive reform of existing trade remedy rules. Some of the proposed reforms target U.S. practices that have also been challenged under WTO dispute settlement procedures. In 2004, WTO members participated in an active schedule of meetings to discuss these proposals in depth. Proponents are pushing to intensify negotiations with a view to having rules be a major component of a Hong Kong package. According to U.S. government officials, the United States remains committed to preserving the effectiveness of trade remedies but wants increased transparency abroad.

[13]To achieve more fruitful dialogue, the Chairman proposed that the group adopt a new approach for discussing the outstanding proposals. First, they would agree to keep certain principles in mind--such as the objective of securing effective market access for products of export interest to developing countries, the need to give developing countries flexibility when implementing WTO commitments in certain situations, and the desirability of a rules-based trading system. Second, they would discuss proposals with a view towards either modifying them or coming up with another alternative for addressing the underlying issue or concern. Third, they would also consider cross-cutting issues such as capacity-building and coherence in policymaking between the WTO and other multilateral agencies. However, partly due to concerns by some of the more advanced developing countries that this could open the door to differentiation among developing countries, which they strongly oppose, this approach has yet to be operationalized. See, for example, WTO, Report by the Chairman of the Special Session of the Committee on Trade and Development, Mr. Faizel Ismail, to the Trade Negotiations Committee, WTO/TN/CTD/11, Feb. 14, 2005.

Several Factors Pose Challenges to Successful Negotiations in Hong Kong

Seven interrelated factors may influence the Doha Round's progress in resolving substantive differences in the lead-up to the Hong Kong ministerial. First, achieving internal consensus on a balanced package for trade liberalization and successfully negotiating a result that is acceptable to 148 members is an enormously complicated task. Second, formation of coalitions may facilitate consensus building, but developing countries show no signs of taking a less assertive role in pressing their sometimes-competing vision for the WTO's Doha Development Agenda. Third, U.S. and EU cooperation remains pivotal, but leadership transitions may change relationships. Fourth, analysts agree that action on high-profile WTO dispute settlement cases such as trade remedies and cotton could prove important to ongoing negotiations. Fifth, trade negotiations pursued outside the WTO are widely seen as affecting the Doha Round, though opinion differs on how. Sixth, there are timing considerations, with the mid-2007 expiration of any renewed U.S. Trade Promotion Authority acting as an implicit deadline. Finally, preparation strategy has proved critical to past WTO ministerial success, but there is mixed news on preparations for the Hong Kong ministerial.

Negotiators Face a Complex Task

The complexity of the task itself could make it hard for Doha negotiators to achieve consensus. Several experts and negotiating participants told us that the scope of work remaining is considerable and that the current round is more complex than past rounds because the number of countries actually participating is larger and the issues are, in some sense, unfinished work from prior negotiations. The fact that agriculture had not been addressed for most of the trading system's first half century was cited frequently as evidence of its thorny nature. The last (Uruguay) round succeeded in the complex challenge of adding agriculture, services, and intellectual property rights to the trading system for the first time. The Doha Round is ambitious because it aims to cut subsidies and trade barriers from the Uruguay Round's high levels. In industrial goods, the Doha goal of having all members conform to specific methods for liberalizing tariffs on all products differs from past practice of relying primarily on member-to-member bargaining to secure tariff cuts. (Past practice did result in substantial liberalization, but left in place high barriers on some goods and in some countries.)

The diversity of economic costs and benefits also makes the task complex. Studies emphasize that both developed and developing countries are positioned to benefit from the Doha Round, but individual countries face varying economic incentives that could affect their willingness to compromise on issues at the Hong Kong ministerial. The Doha talks have been fueled by the premise that international trade can positively benefit a country's overall growth and development. As discussed more fully in appendix V, a number of expert studies have emerged in response to the negotiations that estimate potential worldwide economic gains exceeding $100 billion under an ambitious liberalization scenario. However, the distribution of economic gains may vary within and between countries, creating perceived winners and losers. For example, several studies estimate economic losses from agricultural liberalization for regions that are large net importers of food, such as North Africa and the Middle East, because the removal of developed country subsidies may increase world food prices. Other experts point out that for countries receiving preferential trade access the estimated economic benefits from worldwide trade liberalization may not reflect export losses from erosion of those preferences. Potential losses in tariff revenue may also be a concern to certain developing countries that heavily rely on trade taxes for government financing. In April 2004, to assist developing countries with potential adjustment costs to trade liberalization, the IMF introduced a new lending program called the Trade Integration Mechanism (TIM).

Maturing of Country Coalitions May Facilitate Progress, but Differences in Visions between Developing and Developed Countries Persist

Coalitions of WTO members have been a factor in both leading and preventing movement forward in the Doha negotiations. At Cancun, the large number of participants proved unwieldy and the unexpected emergence of developing country coalitions challenged traditional ways of negotiating. Since then, country coalitions have matured and now advance common priorities of many types. See appendix VI for a depiction of some major groups of countries and their negotiating interests. Developing countries in particular have become more active and influential, according to various participants. A number of ad hoc groups have arisen around other issues. For example, the Colorado Group has led discussion on trade facilitation issues; a variety of "friends" groups have formed to advocate positions in the services negotiations; and the Friends of Antidumping Negotiations group has pressed for changes in the antidumping agreement. This mode of operations has been particularly valuable to developing country members, which sometimes cannot afford to maintain enough staff in Geneva to attend all negotiating sessions that interest them. By reaching an agreement on negotiating proposals within groups, coalitions also help to overcome the difficulty of creating consensus in an organization as large as the WTO. By the same token, they may strengthen opposition to proposals that some members might not otherwise care about. Country coalitions also have other drawbacks, according to several participants—they cannot be relied on exclusively as interlocuters because country interests vary and not every country is included; internal communication is critical, but sometimes breaks down; and coalitions' efforts to forge common positions may leave little room for negotiating maneuver.

Developing countries are not monolithic in their interests, but there is still some evidence that developing and developed countries have competing visions of Doha Development Round's promise and that satisfying developing country's expectations may be difficult–factors we identified as challenges in prior reports. While developed countries tend to stress the development benefits projected to accrue from agriculture reform and trade liberalization, developing country coalitions, in various formations, have continued to emphasize the need for special and differential treatment. The largest group of developing countries, the Group of 90 G-90), has advanced specific special and differential treatment proposals, protection against erosion of trade preferences, and trade facilitation approaches that address implementation costs and capacity building issues. However, satisfying these demands–without prejudicing the interests of other developing countries—has proven difficult. In addition, four least-developed African cotton-producing countries successfully lobbied in July 2004 for a special focus on cotton within agricultural negotiations, but have expressed dissatisfaction with progress attained since then and called for decisive action by Hong Kong.

Leadership Critical, but U.S.-EU Political Transitions May Change Relationships and New WTO Director-General Is Being Selected

Despite more active and positive participation by developing countries, 2004 also demonstrated that leadership and cooperation by the United States and the EU remains essential. A special relationship between U.S. and EU leaders contributed to the Doha ministerial's success and to the July 2004 package. But the U.S.-EU trade principals have changed since then. Two very important participants in the negotiations, who played pivotal roles in launching the round in 2001 and reviving the Doha negotiations in 2004 after Cancun, U.S. Trade Representative Robert Zoellick, and the EU's Trade Commissioner, Pascal Lamy, are both out of those offices. The President named a new USTR in mid-March who assumed office on April 29, 2005. In the interim, continued direction by the Acting USTR kept the United States engaged in negotiations. However, the relationship that develops among new U.S.-EU leaders could influence Hong Kong's success. Their will to lead is also vital. Over the coming months, the United States will face important tests of its trade leadership, such as potentially divisive domestic debates over the Central American

Free Trade Agreement (CAFTA), competition from China, TPA renewal, and continued U.S. WTO membership. The EU, meanwhile, has made some statements that suggest it “gave most” in 2004 and thus is expecting others to reciprocate with ambitious offers for services and industrial market access offers.

The WTO has been in the midst of selecting a replacement for the position of Director-General (DG). Three WTO committee chairs are personally conducting the vetting process whereby those candidates with the least support from the members are expected to withdraw voluntarily. The last DG selection became so contentious along North-South lines that the job ultimately had to be shared by dividing the DG’s six-year term between two candidates – Mike Moore of New Zealand and the current DG, Supachai Panitchpakdi of Thailand. To avoid a similar situation, WTO members agreed to a selection process and timetable. Mr. Supachai’s term ends on August 31, 2005; by May 31, WTO members aim to select a new Director General who will assume the DG’s position in September, just three months before the Hong Kong ministerial. A smooth transition is necessary to ensure members can concentrate on the difficult negotiations needed to achieve results at Hong Kong. (It appears that a new DG has been selected – France’s Pascal Lamy - and that the process worked well avoiding a contentious north/south divide. Specifically, on May 13, 2005, the General Council Chair informed WTO delegations that Mr. Lamy had received the broadest support from the WTO members and that therefore she would recommend that WTO members appoint Mr. Lamy as the next Director General of the WTO starting September 1, 2005. On May 26, 2005, WTO General Council officially named Mr. Lamy, the next Director General. Welcoming the move, current WTO Director General Supachai pledged to “make every effort to move the Doha Development Agenda negotiations as far as possible to ensure that we are well positioned for our Hong Kong ministerial conference in December.”)

Ongoing Disputes Could Affect Negotiating Dynamics

WTO disputes often have little day-to-day impact on negotiations, but several ongoing disputes may affect the negotiating atmosphere leading to Hong Kong. In recent months, Brazil won two high-profile cases against the United States and the European Union. Both rulings are expected to influence the Doha agriculture negotiations. In March 2005, the WTO Appellate Body upheld a panel finding against U.S. cotton subsidies, stating that certain types of current U.S. domestic supports result in significant price suppression in world markets. The United States has informed the WTO that it intends to come into compliance and is now consulting with

Congress and stakeholders about possible reforms. The European Union has vowed to reform its sugar sector in the wake of an adverse WTO ruling, but is facing challenges to its proposals to reform its banana regime to conform with another adverse ruling. The United States is also facing calls to bring its trade remedy laws and actions into conformity with adverse WTO rulings. With the EU and Canada both imposing millions of dollars in retaliation starting in May because the U.S. has not repealed the Continued Dumping Subsidy Offset Act (also known as the Byrd Amendment), there is a risk of a negative spillover into the Doha negotiations. In part to avoid a similar situation, the United States and the EU have been trying to resolve their dispute over aircraft subsidies.

Free Trade Negotiations Outside of the WTO Affecting Progress

Although WTO members and experts have divergent views on the effects of the numerous free trade negotiations that take place outside of the WTO, they widely agree that the negotiation of preferential trade agreements (PTA)[14] have an impact on multilateral trade talks such as the Doha Round.[15] The Bush administration has actively pursued PTAs as part of its trade liberalization strategy, and more generally, these extra-WTO agreements have flourished worldwide since the mid-1990s. Proponents of PTAs claim that they offer opportunities for achieving deeper and faster liberalization than is possible in the WTO by allowing members to negotiate with subgroups of likeminded countries. Once in place, they argue, PTAs can demonstrate the benefits of freer trade to nonmembers, thereby encouraging greater multilateral liberalization. In contrast, opponents claim that the rising number of PTAs increases the administrative and legal complexity of international trade and adds to the difficulty of building an open, rules-based trading system. After weighing many of the arguments in its report on the future of the WTO, a Consultative Board to the Director General recently stated that there is "real reason to doubt that the pursuit of multiple PTAs will enhance, rather than undermine, the attractiveness of multilateral trade liberalization—at least in the short and medium term."[16]

[14]Preferential trade agreements encompass several types of trade agreements, such as free trade agreements that two or more countries negotiate outside of the WTO framework. These include free trade agreements, customs unions, common markets, and economic unions.

[15]Economists agree that PTAs either create or divert trade, depending on circumstances.

[16]Consultative Board to the Director General. *The Future of the WTO: Addressing Institutional Challenges in the New Millennium*, World Trade Organization, 2004.

Among other objections, the Board expressed concern that such agreements are diverting skilled and experienced negotiating resources and reducing enthusiasm for the Doha Round.

Timing Constraints

Timing considerations are also relevant. WTO negotiators are keenly aware that the United States will consider revamping comprehensive farm legislation slated to expire in 2007 and want to make sure it includes WTO-agreed reforms. Moreover, the duration of U.S. Trade Promotion Authority is, in effect, operating as an implicit deadline for concluding the Doha Round, according to numerous participants and experts. If Congress renews TPA in mid-2005, the Doha Round agreement would be eligible for approval under TPA provided it was signed by the President by June 30, 2007. However, the President must fulfill a number of procedural requirements and meet certain time frames established by TPA.[17] Thus, the WTO Doha negotiations would need to conclude by the end of December 2006 to meet TPA's statutory requirements.[18] If the Doha Round agreement required no changes to trade remedy laws, the effective deadline could change to the end of March 2007.

[17]Specifically, TPA includes the following requirements:

- *at least 180 days* before signing a trade agreement, the President must report to revenue committees (House Ways and Means and Senate Finance) on agreement provisions that might require amendments to U.S. trade remedy laws
- *at least 90-day* notice to Congress required before signing a trade agreement
- *no later than 30 days* after President notifies Congress of intent to enter into agreement, private sector advisory committees must submit reports on trade agreements to Congress, the President, and USTR. However, this imposes no requirements on the President.
- *at least 90 days* before entering into agreement, the President must provide the ITC with details of the agreement and request an assessment
- USTR must consult closely with revenue committees, the Congressional Oversight Group, and other congressional committees with jurisdiction over affected subject areas.

[18]This assessment is based strictly on these TPA procedural requirements. It does not take into account other potential requirements.

Ministerial Preparations Under way, but Still Incomplete

A preparation strategy has proved to be critical to WTO ministerial success (Doha) and failure (Cancun and Seattle) in the past, but there is mixed news on preparations for Hong Kong. Ministerials are important because unlike political summits or annual meetings of other international organizations, actual negotiations occur and decisions are made to enable future work. Indeed, ministerials are the only occasion when trade ministers of all WTO members gather to provide high-level political direction. As noted above, the December 2005 Hong Kong ministerial is pivotal so that final bargaining on cuts in subsidies and tariffs can occur and a Doha package can be finalized by the end of 2006.

On the positive side, although Ministers at Hong Kong will face a complex and full agenda, WTO members are trying to narrow differences and clarify options prior to the ministerial. Moreover, there is general agreement on which issues will be discussed and on concrete deliverables desired. In late January and mid-February 2005, WTO members agreed that they would aim to make concrete progress by July on a Hong Kong package. In March, 2005 WTO members agreed on a work plan.

On the negative side, April 2005 meetings and our issue-by-issue analysis suggest that wide substantive differences persist and progress in bridging them is lagging, but WTO ministerials have inherent limits and drawbacks in resolving them. First, ministerials can get out of hand if too many unresolved issues are presented or if politically charged issues dominate. Second, the glare of the public spotlight can make compromise difficult. WTO ministerials are large, public events that can involve high-profile confrontations over politically sensitive issues (e.g., labor at Seattle, Trade Related Aspects of Intellectual Property Rights (TRIPS) and Public Health at Doha, cotton at Cancun). The atmosphere surrounding the July 2004 framework was markedly different, in part because WTO negotiators operated outside public view. Third, there has been no change in the process for conducting ministerials, which is, by all accounts, unclear and sometimes chaotic.[19] Past experiences at Cancun and Seattle have shown the risk associated with this situation.

[19]For example, appointed facilitators often are asked by the host country to bridge differences over issues, but delays in naming facilitators and the fact that they are not as familiar with the issues under debate as the negotiating group chairs can cause delays and confusion.

Concluding Remarks

Taking into consideration that two of the three last WTO ministerials ended in failure, we have noted some positive developments in the current WTO negotiating environment compared to that just before Cancun. For instance, the July framework represented progress, and since the July 2004 Framework, there has been significant activity and positive engagement by all member countries, including developing countries. Members are very aware of the tight deadlines and work remaining prior to the Hong Kong ministerial. If they are successful in meeting their goals for interim progress, the risk of arriving in Hong Kong with an overly full agenda will be reduced.

However, as we pointed out in the report, the ministerial faces a number of potential challenges—and some risk of falling short of its ambitious goals without a greater sense of purpose, according to WTO Director-Supachai's latest assessment. Furthermore, issue progress requires compromise, but substantive movement toward convergence is still not evident in most areas. Agriculture remains central to the round. Despite some progress, developed country commitments to undertake painful agricultural reform are at least partly contingent on movement on market access. Yet, technical talks on market access are bogged down, and meetings have only recently broken the impasse. Moreover, even with recent proposals, there is scant evidence that key countries are willing to make commitments to liberalize access to their markets for industrial goods and services. But cutting barriers from today's high levels will be the source of any projected gains from the Doha round to rich and poor countries alike--and deemed vital to achieving balanced results. Deadlines for deciding development issues loom in July 2005, but discussions on outstanding proposals have yet to become fruitful. The United States, meanwhile, is facing tests of its trade leadership at home and calls by other WTO nations for urgent action on cotton, as well as greater receptivity to difficult demands in services and antidumping.

With an effective deadline of December 2006, the question is whether the rest of 2005 will see sufficient progress to enable final agreement on a package that offers gains to all WTO members. Some experts remain optimistic that the Doha Round can deliver its promised benefits. Others say tough decisions are necessary for progress and warn time is short given the substantial work remaining.

Agency Comments and Our Evaluation

We requested comments on a draft of this report from the U.S. Trade Representative, the Secretary of Agriculture, the Secretary of Commerce, and the Secretary of State, or their designees. The Assistant U.S. Trade Representative for WTO and Multilateral Affairs and other USTR staff indicated general agreement with the report, but provided us with several technical comments, which we incorporated as appropriate. The Department of Agriculture's Foreign Agriculture Service agreed with our report's factual findings and analysis, but provided several technical comments, including data on non-ad valorem tariffs, which we incorporated as appropriate. The Department of State's Director of Multilateral Trade, Bureau of Economic and Business Affairs, indicated agreement with GAO's findings and analysis, and provided a technical comment, which we incorporated. The Department of Commerce provided written comments, indicating that "GAO analysts have focused on the essential pieces of the negotiating puzzle" and "accurately portrayed the broad state of progress and existing negotiating tensions in the key areas" (see app. IV). In addition, the Deputy Assistant Secretary for Agreements Compliance and other Commerce staff provided us with oral technical comments on the draft, which we incorporated as appropriate.

We are sending copies of this report to interested congressional committees, the U.S. Trade Representative, the Secretary of Agriculture, the Secretary of Commerce, and the Secretary of State. We will also make copies available to others upon request. In addition, the report will be available at no charge on the GAO website at http://www.gao.gov.

If you or your staff have any questions about this report, please contact me at (202) 512-4347. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made major contributions to this report are listed in appendix VII.

Loren Yager
Director, Interational Affairs and Trade

Objectives, Scope, and Methodology

The Chairman of the Senate Committee on Finance and the Chairman of the House Committee on Ways and Means asked us to assess (1) overall progress in the WTO Doha Round of negotiations, (2) progress in specific negotiating areas, and (3) factors affecting progress.

We followed the same overall methodology to complete all three of our objectives. We obtained, reviewed, and analyzed documents from a variety of sources. From the WTO, we analyzed the *2001 Doha Ministerial Declaration*, the *Doha Work Programme Draft General Council Decision of 31 July 2004*, known as the "July framework," as well as numerous negotiating proposals from WTO member countries and other documents. From U.S. government agencies and foreign government officials, we obtained background information and documentation regarding negotiating proposals and positions. We also obtained information on day-to-day developments from reputable trade publications.

We met with officials from key U.S. government agencies, including the Department of Agriculture, the Department of Commerce, the Office of the U.S. Trade Representative, the State Department, and the Department of the Treasury, to obtain perspectives on progress in the negotiations overall and individual issue areas and factors affecting negotiations. The State Department arranged meetings with various of its country desk officers to provide us with perspectives on key WTO participating member nations. We also met with trade representatives from developed and developing countries located in Washington, D.C., including Australia, Brazil, Canada, Chile, Costa Rica, the European Union, Guyana, Japan, Malaysia, New Zealand, Norway, Singapore, South Korea, and Switzerland. Further, we met with private-sector representatives from specific business sectors, including the American Sugar Alliance, the National Association of Wheat Growers, National Corn Growers Association, the Coalition of Services Industries, the National Association of Manufacturers, and the Zero Tariff Coalition. We met with nongovernmental organizations (NGO), including Oxfam America and the Carnegie Endowment; and trade experts from institutions including the United Nations Conference on Trade and Development (UNCTAD); Georgetown University; the Cato Institute; the Institute for International Economics, the American Enterprise Institute; the World Bank; Columbia University; the University of Toronto; the Manufacturers Alliance; and the Institute for International Business, Economics, and Law, the University of Adelaide, Australia; White and Case; and C&M International.

To illustrate tariff profiles for examples of developed and developing countries, we reviewed international tariff and trade data from the World Bank's World Integrated Trade Solution (WITS) database, which contains member-supplied data from the WTO and the United Nations. Though these organizations are limited in their ability to verify official country data, we concluded that the data is sufficiently reliable for the purposes of our analysis based on accuracy checks regularly performed on the database and its' wide usage in the negotiations.

Prior to the July 2004 mini-ministerial, with the assistance of USTR and the State Department, we traveled to WTO headquarters in Geneva to obtain foreign government official, private sector, and nongovernmental organizational views on progress. We followed this initial visit to Geneva with another trip in late June and early July 2004, to meet with U.S. and WTO officials and observe the Trade Negotiations Committee negotiations; a visit in September 2004, to obtain official reactions to the July framework; and a mid-April 2005 update. The series of visits to Geneva resulted in interviews with WTO member country officials from developed and developing countries including Australia, Brazil, the European Union, India, Jamaica, Japan, and Singapore. We also met with WTO officials, including the agriculture, industrial (nonagricultural) market access, services, development, and trade facilitation negotiating group chairs. In total, we conducted more than 130 interviews with negotiators and trade experts.

We performed our work from March 2004 through April 2005 in accordance with generally accepted government auditing standards.

Agriculture

Given the importance of agriculture in the Doha Round negotiations, coalitions of countries regrouped in 2004 and focused on making progress on the three pillars in agricultural reform of export subsidies, domestic supports, and market access. The most notable achievement thus far has been agreement in the July 2004 framework to remove all export subsidies at some future date. The framework also set ceilings on certain trade-distorting domestic support categories. However, disagreement persists over how to define such categories and set reduction schedules, as well as how to improve market access through a tariff reduction formula and the definition of sensitive and special products that can be insulated from tariff cuts.

Export Competition

The May 9, 2004, EU letter from Pascal Lamy and Franz Fischler to WTO member countries offered to eliminate all export subsides[1] -- with no products excluded – if suitable agreements were reached on market access and domestic support. This offer was warmly welcomed by member countries; for decades, the United States and other countries have advocated completely eliminating export subsidies.

Lamy and Fischler conditioned their offer on what they termed "full parallelism," meaning the commitment to eliminate all export subsidies is linked to establishing new disciplines in other export competition programs, including U.S. export credit and food aid programs, as well as export state trading enterprises. The move reinvigorated negotiations, country officials and we agreed, because the European Union had previously offered only the substantial reduction and elimination of export subsidies for certain products, not total elimination.

The EU's offer, valued at about US $9 billion, meant other countries with substantial export competition programs, such as the United States, would need to agree to undertake disciplines on them.[2] The July framework envisions new disciplines on export credits, food aid, and state trading enterprises.

[1]Export subsidies are subsidies contingent on export performance. For example, they include cost reduction measures, such as subsidies to lower the cost of marketing goods for export, and internal transport subsidies that apply to exports only.

[2]According to its 2001 notification to the WTO, the EU spent about $2.3 billion of the approximately $9 billion it is allowed to spend on export subsidies.

- The framework is likely to force the substantial restructuring of U.S. export credit programs, trade officials say, and our analysis supports this conclusion. For example, the July framework language stipulates that export credit programs may not have financing repayment periods of longer than 180 days. The main U.S. export credit programs, General Sales Manager (GSM)-102 and GSM-103, have repayment periods from 6 months to 3 years and up to 10 years, respectively.[3]

- All food aid programs are subject to scrutiny and could be subject to new disciplines, with certain U.S. programs the focus of international attention, country officials and trade experts told us. The European Union and many African nations advocate that food aid be made only in grant form. They also want to make sure food aid is not a mechanism for surplus disposal when commodity prices are low and commodity stocks are high, because this can trigger commercial displacement. This agreement would have implications for the United States' Title I P.L. 480 food aid program , which provides for long-term, low interest loans to developing countries for their purchase of U.S. agricultural commodities, and the Section 416b food aid program, which authorizes USDA to donate surplus agricultural commodities overseas. As a result, the U.S. successfully sought changes in a July 16 draft text for the framework agreement, which had called for disciplines to "ensure that food aid is not used as a mechanism for *surplus disposal* and to prevent commercial displacement" [italics added]. However, the framework text agreed upon in late July makes no such mention of surplus disposal. Instead, it indicates that there will be future discussions on "providing food aid exclusively in fully grant form."

- Finally, the framework calls for disciplines to remove the export subsidy components of state trading enterprises, including the government financing of and underwriting losses of such programs. U.S. goals for the negotiations reflect long-held concerns about the exercising of monopoly power on imports and exports through these institutions. As a result, Canada and Australia are likely to face tighter disciplines on their wheat state trading enterprises, trade officials and experts told us.

[3]The 2002 Farm Bill authorized $5.5 billion in annual farm exports for GSM-102 and GSM-103 programs. The legislation authorized an additional $1 billion for emerging markets through 2007.

Domestic Supports

Many developing and developed countries are seeking substantial reductions in developed country trade-distorting domestic support[4] programs because these programs can reduce world prices and displace otherwise competitive producers from world markets. The European Union and the United States in 2001 together accounted for the majority of global spending in trade-distorting domestic supports. The U.S. has publicly stated it would significantly reduce its trade-distorting domestic support spending if other WTO member nations agree to ambitious outcomes in other areas, such as market access.

In July, WTO members agreed that the eventual Doha Round agreement would contain a strong element of harmonization in reductions of trade-distorting domestic support programs by developed countries, with those countries with larger subsidy programs cutting more. This dovetails with U.S. aims in the domestic supports pillar, since the European Union still outspends the United States. The framework sets ceilings on certain kinds of trade-distorting domestic supports and calls for the capping and future reduction of others. The July framework also called for a substantial reduction in the overall level of trade-distorting support from bound levels.

To examine how these broad guidelines could affect existing European Union and the United States programs, we have reviewed the various categories of domestic supports, which the WTO classifies into "boxes:" amber, blue, green, and *de minimis* supports. Figure 3 describes the categories of WTO-recognized domestic support programs.

[4]Domestic supports (often called "'subsidies") are payments made to farmers that raise prices or guarantee income. They include such measures as government purchases at guaranteed prices, commodity loan programs, and direct payments to farmers.

Figure 3: Types of Domestic Supports—WTO Definitions

Types of Domestic Supports-WTO Definitions

- The WTO classifies agricultural domestic support into main categories identified by traffic-light color-coded "boxes" that range from most to least trade-distorting: **Red,** e.g. spending not permitted in these types of supports; **amber,** domestic supports that are production- and trade-distorting, the total value of which was capped and then reduced; **blue,** production-limiting subsidies that have marginal trade-distorting effects; and **green,** non- or minimally-trade distorting, and thus permitted.
- ***De* minimis** is a category that captures other domestic supports, including market price support measures, direct production subsidies, or input subsidies. There is no requirement to reduce de minimis trade-distorting domestic support for any year in which the aggregate value of the product-specific support does not exceed 5 percent of the total value of production of the agricultural product in question. In addition, non-product specific de minimis support which is less than 5 percent of the value of total agricultural production is also exempt from reduction.
- **Trade-distorting support** is comprised of a country's expenditures in Amber Box, Blue Box, and de minimis supports. In other words, it does not include Green Box measures.

Source: GAO.

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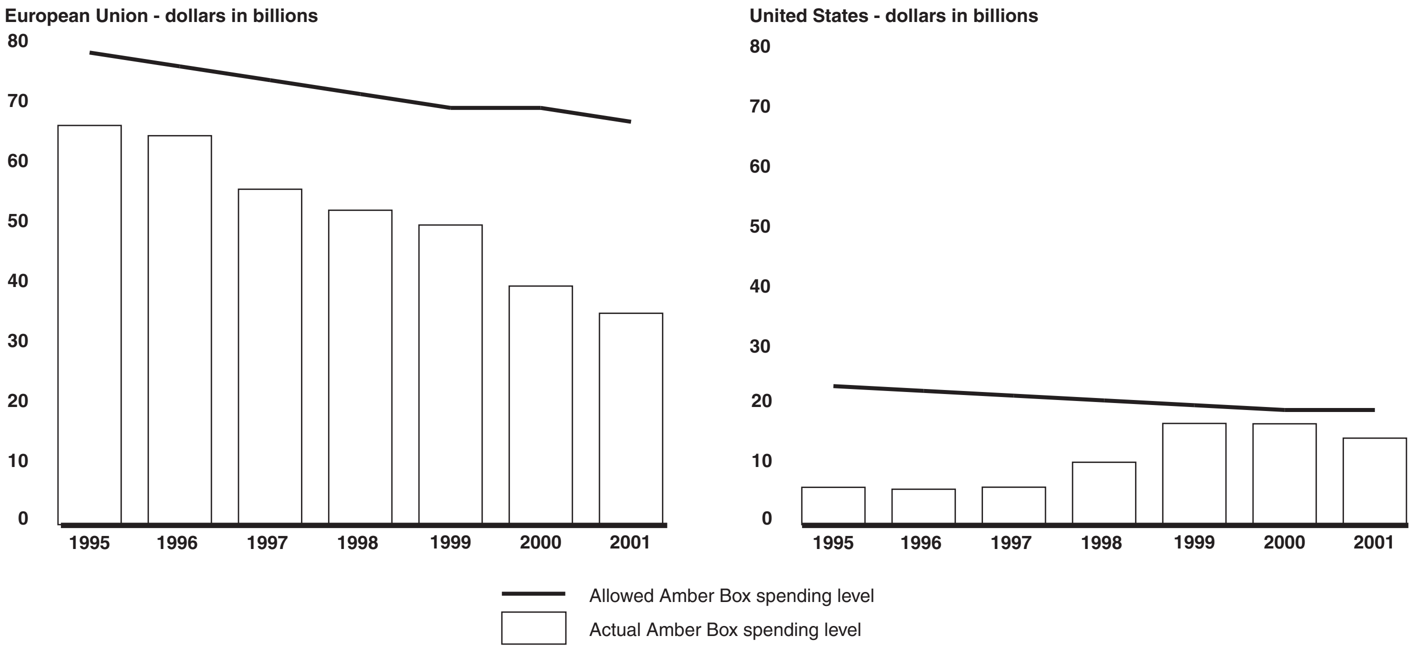
Trade-distorting support is comprised of a country’s expenditures in Amber Box, Blue Box, and de minimis supports. In other words, it does not include Green Box measures.

For Amber Box supports, the most trade-distorting category, the July framework calls for final bound thresholds[5] to be reduced substantially, using a tiered approach whereby members with more substantial support programs will be placed in higher tiers and forced to cut more. As illustrated in figure 4 below, this provision will narrow the difference between the levels the United States and European Union are authorized to spend versus the amount they actually spend.

Figure 4: Recent Amber Box Spending Patterns for the European Union and United States, as Measured by Aggregate Measure of Support



Source: GAO, based on USDA and GAO analysis of USDA and EU data.

In absolute terms, the European Union spends substantially more in Amber Box programs than the United States and accounts for more than half of the total amount notified by the 30 WTO members that use such domestic supports. The U.S. is permitted to spend less than one-third of what the EU is permitted. In recent years the European Union spent just over half of

[5]Bound thresholds refer to the permitted levels of spending.

what it is permitted to spend on these trade-distorting domestic supports, and its actual spending has declined.

By contrast, trade experts and officials told us that other countries are concerned about U.S. domestic subsidy programs due to the United States' trend of increased spending. The United States has supplied official WTO notifications through 2001 that indicate its Amber Box program spending was within established WTO limits, but its actual spending in Amber Box supports grew from $6.2 billion in 1995 to $15.6 billion in 2001, the most recent year data are available.

Furthermore, as we reported in our January 2004 report, the 2002 Farm Bill[6] could increase U.S. agricultural support spending and shift its composition. Specifically, the 2002 Farm Bill created a new category of domestic support programs, dubbed "countercyclical payments," which are income support payments to farmers when the market price for a covered commodity falls below a legislatively-set target price. As a result, the United States has pushed in the WTO Doha Round for a redefinition of the WTO Blue Box, in which it currently does not spend – so that as long as the Blue Box exists it has greater flexibility to allow access for other programs that are less trade- distorting to count against its current, unused ceiling for this category of domestic supports.

The July framework language regarding the Blue Box was favorable to the United States, trade officials and experts told us. It redefines the Blue Box to allow direct payments that do not require production limitations[7] if based on certain criteria.[8] This has met with sharp resistance from the G-20 and other WTO members that seek significant reductions in all forms of trade-distorting domestic supports. These members are concerned that by allowing the United States to place its countercyclical payments in the redefined Blue Box, the United States will not be forced to reduce its trade-distorting domestic support programs and could in fact increase its total sum of trade-distorting domestic support. As recently as March 2005, the G-20 called for further disciplines on price-linked supports in the

[6]The Farm Security and Rural Investment Act of 2002 (P.L. 107-171, May 13, 2002).

[7]In contrast to the existing definition, which specifies that Blue Box measures must be production-limiting.

[8]Criteria provisionally include fixed production conditions, such as acreages, yields, and historical production levels.

provisionally redefined Blue Box to allow the compensations for some, but not all, of the difference between market and target prices, among other proposals.

The July framework calls for a cap on the Blue Box of 5 percent of the production value, with historical spending patterns to be determined as a base. This could affect the European Union, trade officials and experts told us, which in 2001 spent 23.7 billion euros in Blue Box supports, or 9.6 percent of its total agricultural production.

To ensure ambitious cuts in domestic support, the July framework also calls for a substantial reduction in overall trade-distorting support, specifically the sum of Amber Box spending as measured by "Final Bound Total AMS," Blue Box payments, and de minimis programs—with a 20 percent cut to be made in that total in the first year of implementation.[9] However, the specific extent of reductions was left to future negotiations.

Finally, on non- or minimally trade-distorting "Green Box" domestic supports, the framework called for a review, but not a capping or cut of these supports. The G-20 has charged that certain current Green Box direct payments to producers contradict the Green Box criteria of being non- or minimally trade-distorting. The United States and the European Union have resisted caps and cuts, but agreed to examine concerns about abuse. The United States spent about $51 billion in these types of supports, according to its 2001 notification to the WTO, the most recent year that data are available.

Market Access

Market access remains the most difficult pillar of the negotiations, country officials and experts told us. Major agricultural exporters including Canada, Australia, and Brazil want to expand their overseas markets. The United States is the world's largest exporter of agricultural products, is a highly competitive producer of many products, and has significant offensive interests in this area. The United States has conditioned domestic support cuts on gains in market access. However, many developing countries have resisted liberalization, arguing they do not have the means

[9]The United States spent about $7 billion in de minimis payments while the European Union spent less than Euros 1 billion on these supports in 2001, the most recent year data are available.

to subsidize exports or domestic production, and that tariffs are their only source of leverage and protection in the agricultural negotiations.

Though the July 2004 framework states that a numerical formula will be used to cut tariffs from current bound rates, countries differ strongly over the type of formula they prefer. The methodology for converting specific tariffs into *ad valorem* equivalents[10], upon which the tariff reduction formula would be applied, also frustrated progress in the market access negotiations for months. Such differences are based on the widely divergent tariff profiles among WTO members. Specifically, several studies by the Organization for Economic Cooperation and Development and the World Bank find that for agricultural goods, developed countries tend to have lower average bound and applied tariffs.[11] However, developed countries have a greater percentage of specific (non-ad valorem) tariffs and tariff peaks.[12] The products where developed countries have specific tariffs tend to be those with high levels of protection and the products where they have tariff peaks tend to be those of export interest to developing countries. In contrast, developing countries have uniformly higher bound tariffs, though currently applied tariff rates tend to be far lower than bound tariff rates and specific tariffs are rare. To illustrate these different tariff profiles, table 1 provides agricultural goods weighted average tariff rates for a selected set of countries and products. Due to member differences over the methodology for calculating ad valorem equivalents, the data excludes specific tariffs.

[10]A specific tariff is a trade tax levied as a monetary amount per unit of import. An ad valorem tariff is a trade tax calculated as a percentage of the value of the product being traded. To convert a specific tariff into an ad valorem equivalent, an import price for the product is needed. In the market access negotiations, some members advocated using the world input price. The EU advocated using the import price recorded by each country. In May, 2005, members eventually agreed on a combination of both prices.

[11]Bound tariffs are the rates WTO member nations are permitted to charge and can raise only under strictly prescribed circumstances.

[12]Tariff peaks are tariffs that exceed a selected reference level.

Table 2: Trade Weighted Average Ad Valorem Agricultural Tariff Rates for Selected Countries and Products. (Tariffs in percent)[a]

	US	EU	Japan	India	Indonesia	Kenya	Venezuela
Average bound tariff	2.5	3.0	6.8	126.2	54.2	100.0	73.6
Average applied tariff	3.0	5.2	7.1	53.8	4.7	22.3	16.2
Maximum applied tariff	350.0	74.9	50.0	182.0	170.0	100.0	20.0
Share of applied domestic peaks [b]	6%	14%	30%	11%	5%	1%	0%
Share of applied international peaks [b]	4%	11%	28%	89%	6%	59%	49%
Agricultural imports as a share of total imports	4%	7%	10%	7%	12%	13%	13%
Dairy Products[c]							
Average applied tariff	10.9	10.8	27.3	30.9	5.0	25.0	19.6
Share of international peaks	11%	2%	55%	100%	0%	100%	91%
Yogurt – HTS Code 040310	17.3	n/a	27.5	30.0	5.0	25.0	20.0
Edible Fruits and Nuts[c]							
Average applied tariff	0.1	9.5	8.5	40.6	5.0	27.7	15.0
Share of international peaks	1%	7%	16%	94%	0%	62%	0%
Bananas – HTS Code 080300	0.0	16.0	10.2	30.0	5.0	25.0	15.0
Tobacco[c]							
Average applied tariff	70.6	25.4	0.1	30.0	0.3	20.8	15.4
Share of international peaks	11%	16%	27%	100%	0%	100%	56%
Smoking Tobacco – HTS Code 240310	257.0	74.9	16.6	30.0	11.7	30.0	20.0
Year of Data	2003	2004	2003	2002	2002	2001	2002

Source: WITS World Bank Integrated Database.

[a]Notes on data: Due to member differences over estimating ad valorem equivalents, the data excludes specific tariffs. Since specific tariffs tend to apply to products with higher protection levels, this exclusion may bias the data downward in certain circumstances.

[b]Domestic peaks are tariffs that exceed three times the average tariff for a country. International peaks are tariffs that exceed 15 percent.

[c]Tariff rates for dairy products are those for chapter 4 in the U.S. Harmonized Tariff Schedule (HTS). Tariff rates for edible fruits and nut products are those for HTS chapter 8. Tariff rates for tobacco products are those for HTS chapter 24.

In line with these general patterns, the table shows that developed country members such as the United States, the European Union, and Japan have relatively low average bound and applied ad valorem tariff rates that range from around 2 percent to 7 percent. However, by excluding specific tariff rates, the table does not show the full extent to which these countries protect their agricultural sectors. According to the World Bank, the European Union, for example, has specific tariff rates on 44 percent of its agricultural product lines. A 2001 study by the U.S. Department of Agriculture employed a certain methodology for converting ad valorem equivalents and estimated that the non-trade weighted average tariff rate for agricultural goods in the United States, the EU, and Japan was 12 percent, 30 percent, and 58 percent respectively.[13] Additionally, for the example products of dairy, fruits and nuts, and tobacco, the United States, the European Union, and Japan have relatively high tariffs and a large share of international peaks.[14] The United States' average tariffs in the tobacco sector are extremely high, at around 71 percent.

Developing countries such as India, Indonesia, Kenya, and Venezuela have much higher average bound tariffs, ranging from 54 percent in Indonesia to 126 percent in India. However, in each of these cases, there are substantial gaps between the bound and applied tariff rates.

The contrast between developed and developing country tariff profiles has fueled a sharp debate on what formula to use to conduct tariff reduction, country officials and trade experts told us. Some developed countries, including the United States, have advocated for a harmonizing formula called a Swiss formula, that would reduce high tariffs by a larger percentage than low tariffs. Developing countries and, particularly net-exporters such as Brazil with high bound tariffs want more flexibility than the Swiss formula would offer. As an alternative, they advocate a banded approach, which divides tariffs into a series of bands and applies an average tariff reduction within each band. The banded approach would apply larger reductions to higher tariff bands—thereby addressing developed country tariff peaks – but would be less harmonizing than a Swiss formula. A formula that combines elements of both Swiss formula reductions and linear reductions is a blended approach.[15]

[13]See Economic Research Service, *Profiles of Tariffs in Global Agricultural Markets*, Washington: US Department of Agriculture, 2001. This paper chose to use the world input unit value as a proxy for the input price based on data from the Agricultural Market Access Database – which largely draws on data from the WTO and United Nations. This methodology differs, however, from that agreed upon in the WTO negotiations.

[14]The average U.S. tariff on edible fruit and nut products is an exception, at only 0.1 percent.

[15]The blended formula would apply an average tariff cut to a certain percentage of tariff lines, the Swiss formula cuts to another percentage of tariff lines, and provide duty-free access to the remainder.

Figure 5: Tariff Reduction Formulas Considered for Improving Agricultural Market Access

Tariff Reduction Formulas Considered for Improving Agricultural Market Access

Linear formula: a formula where all tariff rates will be reduced by the same percentage. The general mathematical specification is:	$t_1 = c*t_0$ where t1 is the final tariff rate, to is the initial tariff rate, and c is a constant parameter.
Swiss formula - a nonlinear formula that is harmonizing because it subjects higher tariff rates to larger tariff cuts. The general mathematical specification is:	$t_1 = (a*t_0)/(a+t_0)$ where t1 is the new tariff, t0 is the initial tariff, and a is the coefficient to be negotiated.

- Blended approach: an approach where tariffs cuts would be applied by three methods. Some tariffs would be made duty-free, some tariffs would be reduced by an average linear cut with a minimum reduction per product (the Uruguay Round approach), and some tariffs would be reduced by a Swiss formula.
- Banded approach: an approach where tariffs would be divided into bands and reduced by an average linear cut within each band. Higher tariff bands would be reduced by a larger percentage than lower tariff bands.

Source: GAO.

The United States was among a handful of nations that in June 2004 penned and circulated a draft market access white paper attempting to strike a compromise. The paper called for a different type of a tiered formula approach, where within each band a certain percentage of bound tariffs would be cut by a Swiss (harmonizing) formula and a certain percentage of bound tariffs would be cut by a linear percentage. A certain number of tariff lines would be exempt from either a Swiss or linear cut. Instead, liberalization would be handled through tariff rate quota increases. This in effect allows member countries to shield themselves from substantial reduction commitments for certain products by self-designating them as "sensitive products."

Continued disagreement on the tariff reduction formula is significant because variations in the type of formula could result in widely different results. Recent studies indicate that for developed countries, the banded approach reduces applied tariff rates in some instances more than the blended approach. These studies further indicate that the blended approach could have a greater impact in reducing bound rates in developing countries due to the homogeneity of their bound rates at relatively high levels. However, irrespective of the type of tariff reduction formula chosen, the degree of liberalization will strongly be affected by the degree of ambition within the formula, as determined by the coefficients, and by the exceptions to the formula through sensitive product designation.

Negotiators had hoped to agree on the formula to cut tariffs in July 2004 but were unable to do so. Instead, they agreed that (1) the future formula will be a single approach for developed and developing countries; (2) the future formula will be tiered, with progressive reductions achieved through deeper cuts in higher tariffs; and (3) all WTO members will have some flexibilities in applying cuts to sensitive products that will be used in the future. Under the framework, increased market access on sensitive products will be achieved through expanded tariff quota rates and tariff reductions.

Sensitive products and special products—whereby developing countries are allowed to declare additional products exempt from standard reductions under certain criteria, such as rural development or food security needs—are likely to be among the most contentious battles going forward, trade officials and experts told us. The G-20 and other negotiating groups have stressed that the exceptions for sensitive products – whereby countries are permitted to declare certain key commodities as sensitive and exempt them from standard tariff reduction schedules—is at odds with the liberalizing mission of the Doha Round. Sensitive product exceptions could be used to protect developed country tariff peaks, these countries say, and greatly undermine the ambitious nature of any agreement.

Industrial Market Access

Negotiators report that during the period between Cancun and the July framework, members avoided discussing differences in industrial market access (nonagricultural market access or NAMA) so that they could focus on the agricultural negotiations. As a result, while the negotiating atmosphere has improved, the July framework represents a lack of movement on key issues in the industrial market negotiations relative to Cancun. In fact, the framework consists simply of the text that was circulated in Cancun with the addition of a paragraph stating that agreement on substantive elements of the text had not yet been reached. While negotiators are using the framework as an agenda for discussion, the framework lacks both consensus and specificity on the two main methods being considered for liberalization of trade in industrial goods—a tariff reduction formula and sectoral initiatives—as well as the flexibilities that developing countries will be offered in applying these methods. As of the spring 2005, consensus on these substantive issues had not yet been reached.

The Tariff Reduction Formula

WTO members remain divided over the tariff reduction formula and its application. The July framework suggests a nonlinear formula, to be applied line by line to bound tariff rates, with the aim of reducing or eliminating tariff peaks and tariff escalation.[1] Despite the framework's disclaimer that agreement on the formula had not been reached, negotiators we spoke with indicated that members have generally accepted the idea of a nonlinear formula. Nonetheless, there remain strong differences over countries' preferences for the type of nonlinear formula chosen and the formula coefficients. The July framework also suggests a variety of ways in which special and differential treatment could be provided. Negotiators we spoke with suggest that members agree that least developed countries (LDCs), as well as countries with a low percentage of bound tariffs, can be exempted from reducing their tariffs through a formula, but the degree to which other developing countries can exempt products from the formula and qualify for longer implementation periods remains controversial.

[1]A nonlinear formula would apply different percentage reductions to tariff rates at different levels. A tariff peak is a tariff that exceeds a selected reference level. Tariff escalation is a practice that countries often use, whereby they increase tariffs in relation to the degree of processing found in a product.

Figure 6: Potential Special and Differential Treatment Provisions Discussed in the July Framework on NAMA

Potential Special and Differential Treatment Provisions Discussed in the July Framework on NAMA

The July Framework provides for three general avenues for which special and differential treatment for developing countries could be pursued:

- Developing countries with less than a certain percentage of their tariff lines that are bound could fully bind their tariffs at an average level rather than participate in tariff reductions through a formula. The current text suggests that countries with less than 35 percent of tariff lines that are bound could qualify. Least-developed countries would also be expected to increase their level of bindings but would be exempt from the tariff reduction formula and sectoral initiatives.
- Developing countries that are subject to a tariff reduction formula could (a) apply less than formula cuts to some percentage of tariff lines as long as the cuts made are at least half of the formula cuts and (b) keep some percentage of tariff lines unbound. For both exceptions, the selected tariff lines could not exceed a certain share of the total value of a country's imports. The current text suggests that the percentage of tariff lines for less than formula cuts could be 10 percent, and the percentage of tariff lines to keep unbound could be 5 percent.
- Longer implementation periods would be provided, though unspecified, for developing country commitments.

Source: GAO.

Country preferences for the formula and application of special and differential treatment provisions continue to reflect those advocated prior to Cancun and are largely based on the varying tariff profiles among WTO members. Similar to conditions in agriculture, tariff profiles for non-agricultural goods suggest that (1) developed countries have bound almost all of their tariffs at relatively low levels, though certain products are characterized by tariff peaks; (2) products where developed countries have high tariffs tend to be among those of export interest to developing countries such as textiles and apparel or leather and footwear; and (3) developing countries, in many but not all cases, have limited tariff bindings and relatively high bound tariffs, though currently applied tariff rates tend to be far lower than bound tariff rates.

Developed country members that have relatively low tariffs want significant tariff liberalization in order to access new markets in developing countries that have relatively high tariffs.[2] The United States, for example,

[2]Some developing country members that are seeking access to new markets, such as Costa Rica, Pakistan, and several Central and Eastern European countries, also advocate an ambitious approach in NAMA. Some of these countries belong to the informal coalition called the “Friends of Ambition.”

is strongly pressing for an industrial market access agreement that would effectively lower tariffs in key developing countries for which an estimated 71 percent of foreign duties on U.S. manufactured exports are assessed, according to the National Association of Manufacturers. To achieve this result, the United States, the EU, and other developed country members, as well as some developing country members that have autonomously liberalized in the past, continue to support a Swiss-type formula – a harmonizing nonlinear formula that would reduce high tariffs by a larger percentage than low tariffs. Such a formula would also address tariff peaks and escalation. [SIDEBAR] To account for special and differential treatment, the United States has proposed that developing countries could apply a different coefficient within the Swiss formula than developed countries, implying more moderate liberalization. The EU and Norway have proposed a “credit-based approach” where the flexibility in the formula coefficient for developing countries would be determined uniquely for each country based on credits for commitment to apply the formula without exception or participation in sector agreements, for example.

Figure 7: Various Formula Specifications for Tariff Reductions Considered with the NAMA Negotiations

Various Formula Specifications for Tariff Reductions Considered with the NAMA Negotiations

Prior to the Cancun ministerial, the WTO received 17 proposals for different tariff reduction formulas. Key concepts are defined below.

Nonlinear formula: a formula that would apply different percentage reductions to tariff rates at different levels.

Swiss formula: a nonlinear formula that is harmonizing because it subjects higher tariff rates to larger tariff cuts. The general mathematical specification is:	$t_1 = (a*t_o)/(a+t_0)$ where t1 is the new tariff, t0 is the initial tariff, and a is the coefficient to be negotiated.
Girard formula: a nonlinear formula proposed by the former Chair of the NAMA negotiating group that differentiates among countries according to their current overall average bound tariff rates. Countries with higher average bound tariffs would reduce their bound tariffs at a lesser rate than countries with lower average bound tariffs. The general mathematical specification is:	$t_1 = (B*t_a*t_o)/(B*t_a+t_0)$ where t1 is the new tariff, t0 is the initial tariff, ta is the average initial tariff and B is the coefficient to be negotiated.

Source: GAO.

In contrast, some developing countries emphasize that due to their higher average tariff rates, harmonizing formulas that reduce higher tariffs more than lower tariffs would result in greater percentage cuts for developing countries than developed countries—a result that they argue contradicts the principle of special and differential treatment. As such, they continue to support a Girard type formula—a non linear formula proposed by the former Chair of the industrial market access negotiating group that is based on each country's average tariff rate and allows countries with higher initial tariffs to reduce those tariffs at a lesser rate than countries with lower initial tariffs.[3] They also support a more extensive application of special and differential treatment exceptions such that developing countries can maintain the flexibility to pursue industrial policies to promote growth of new industries and protect themselves against some of the adjustment costs of ambitious liberalization commitments.

Continued disagreement on the tariff reduction formula is significant because variations in the type of nonlinear formula chosen, the formula coefficients, treatment of unbound tariffs, and exceptions to the formula could result in widely different results. For example, both the World Bank and UNCTAD have analyzed the Swiss and Girard non-linear formulas by using hypothetical coefficients and have found that:

- Swiss formula reductions tend to be larger than Girard formula reductions, particularly for the high tariff rates found in developing countries.
- While effective at reducing developed country tariff peaks, the Girard formula may also entail greater tariff cuts than the Swiss formula for developing countries that have lower average tariffs resulting from autonomous liberalization.
- The wide wedge between bound and applied tariff rates in developing countries limits the amount of trade liberalization achieved through any formula.

Nonetheless, echoing our analysis of market access negotiations in agriculture, the actual degree of liberalization that is achieved through these formulas or any other formula will strongly be affected by the degree of ambition within the formula, as determined by the coefficients, and by

[3]The Girard formula, when proposed, was to be accompanied by seven sectoral agreements. Recently, India, Brazil, and Argentina tabled a new proposal that is based on the Girard type formula but does not mention sector agreements.

exceptions to the standard tariff reduction schedules that will be offered through special and differential treatment.

Sectoral Initiatives

WTO members also remain divided over sectoral initiatives. The July framework states that sectoral agreements should supplement the tariff reduction formula with an aim to eliminate or harmonize tariffs in key sectors of interest to developing countries.[4] The United States and other members have proposed the notion that participation should be based on a principle of "critical mass," meaning that countries that account for the majority of trade in a sector should participate such that mutual gains are obtained without problems of free-ridership from nonparticipants.[5] However, we were told that key developed and developing country members disagree strongly over whether sector agreements should be included in an industrial market access agreement.

The United States has specific objectives for industrial market access as set out by its Trade Promotion Authority legislation: to focus on improving market access for U.S. exports and to increase global participation in sectoral agreements that reduce or eliminate barriers in key sectors, such as textiles and apparels and civil aircraft. Developed country members such as the United States, New Zealand, and Japan strongly support the inclusion of sector agreements because they can result in greater liberalization outcomes than even ambitious formula cuts. Specifically, they argue that only cuts that bring bound rates below currently applied rates would actually liberalize trade. Such members have conducted education and outreach with developing countries regarding potential requirements and flexibilities for sectoral agreements, as well as the likely economic benefits they could receive from ambitious trade liberalization. Nonetheless, certain developing countries, such as Brazil, do not support this method of liberalization and remain concerned about potentially

[4]While the framework itself did not specify which sectors should be included, earlier drafts provided by the industrial market access Chairman lists among others, electronics; fish and fish products; footwear; leather goods; motor vehicle parts and components; stones, gems, and precious metals; and textiles and clothing. Sector representatives in the U.S. are also interested in other sectors, such as chemicals, wood and paper products, and processed foods.

[5]The notion of critical mass was first used with the Information Technology Agreement (ITA) where, according to one trade expert, countries accounting for 90 percent of trade in that sector were participants.

mandatory participation. They argue that sector agreements could create an overly ambitious pace of reform.

Services

Accounting for 78 percent of private sector GDP[1] and 80 percent private sector employment in the United States, services constitute a core priority for U.S. negotiators. Initially thought to be a lynchpin of the Doha Round, services talks have taken a backseat position relative to other issues. Nevertheless, the inclusion of services in the July 2004 text on an equal footing with the key market access pillars of agriculture and industrial market access resulted from efforts by both developed and developing country members and industry coalitions. Although some developing countries are reticent about services negotiations, generally perceiving them as a developed country interest, many developing countries have a particular interest in obtaining commitments under mode 4, which governs the temporary movement of service-delivery professionals. Notwithstanding these points of contention, since July, talks on the domestic regulation of services have shown signs of progress, as have technical negotiations on market access. However, these have yet to translate into improved offers. An opportunity for significant services liberalization could be foregone if negotiations do not intensify.

Services negotiations aim to reduce barriers to international trade by improving the General Agreement on Trade in Services (GATS) which (1) ensures the increased transparency and predictability of international trade rules and domestic regulations governing services industries (rulemaking); and (2) promotes progressive liberalization of services markets through bilateral negotiations (market access[2]).[3] The Doha Declaration states that members shall submit initial services offers by March 31, 2003, a deadline that many members missed. Following the Cancun ministerial, and in the run up to the July framework, services negotiations made slow progress. Rule-making talks were stalled, and although the 2003 deadline had long past, pending market access offers outnumbered those submitted. Observers said there lacked a "critical mass" of offers for market access talks to make substantial progress. Those offers that were tabled were

[1]U.S. Department of Commerce, Bureau of Economic Analysis, *Survey of Current Business*, June 2004.

[2]"Rulemaking" is conventionally used to refer to GATS rules and disciplines on domestic regulation. "Market access" is commonly used to refer to commitments on both market access and national treatment.

[3]Market access is typically negotiated bilaterally, following the so-called request-offer approach, whereby members request specific commitments from one another in a series of bilateral negotiations, and respond by presenting an offer to all WTO members.

characterized as being of poor quali1ty. Movement had become contingent upon advances in other areas, particularly agriculture.

July Framework Sets New Deadlines

Nevertheless, the final version of the July framework placed services on an equal footing with agriculture, industrial market access, and the other areas considered essential to a final Doha Round package. Initially, services were absent from the text. However, a specific section and annex on this sector were added after several developed and developing countries, as well as industry coalitions from the U.S., the EU, Australia, India, Hong Kong, China, Japan, Brazil, and Canada argued for their inclusion. Specifically, the July framework reasserts the importance of achieving services liberalization and urges members to intensify their efforts to conclude the negotiations on rulemaking. With a view to providing market access to all members, the text calls upon members to submit high-quality offers, particularly in the sectors and modes of supply of export interest to developing countries. It specifically names mode 4 as being among these, and sets May 2005 as the deadline for members to table new offers.

Progress Since July

After they agreed to the July framework, members held several multilateral and bilateral meetings and discussed rules, domestic regulation, and market access with renewed momentum. Technical talks were ongoing on all fronts. On the rule-making side, members initiated new discussions[4] on emergency safeguards,[5] subsidies and government procurement, but none of these issues came close to resolution. Certain East Asian developing countries continued to advocate creation of an emergency safeguard mechanism for services, reflecting concerns over their experience with the 1997 financial crisis. However, many WTO members reportedly see an emergency safeguard for services as being technically unfeasible and/or, in the case of the United States and most other developed countries, undesirable. Discussions on domestic regulation were more promising.

[4]GATS contains several negotiating mandates in rule-making areas which members felt unable to consider in detail within the time frame of the Uruguay Round. These negotiations are conducted in two Working Parties, one on Domestic Regulation and one on GATS Rules. The latter Working Party is charged with negotiations on emergency safeguards, government procurement, and subsidies.

[5]Emergency safeguards are measures that would allow for the temporary suspension of market access, national treatment, and/or any additional commitments that members may have assumed in individual sectors.

Several proposals triggered constructive debates on regulatory disciplines and transparency.[6]

On the market access side, talks were said to be progressing on a technical level. After July 2004, a few more developing countries tabled initial offers, bringing their number up to 52,[7] and bilateral talks seemed to have regained momentum. One gauge of movement was embodied by the intensification of informal meetings held by so-called Friends groups, which assemble subsets of member countries around issue-specific concerns such as financial services, energy services or mode 4. However, WTO officials said that sufficiently detailed negotiations on specific services sectors had still yet to begin. Moreover, a general concern with the current offers is that they do not fully bind, let alone deepen, the level of liberalization that members have already, de facto, achieved outside of the WTO. Another potential problem is that these offers do not systematically schedule commitments in every service sector. Some have signaled notable absences and weaknesses in financial, insurance, communication, audio-visual, and professional services—sectors of interest to the United States—but also maritime services and others of interest to different members. In response, a number of countries are pushing for the universal adoption of minimum requirements, or "benchmarks," in given industries such as financial services. Approximately 40 developing countries have not submitted initial services offers at all—not counting LDCs. According to one WTO official, their failure to table services offers does not strictly reflect a lack of means, though in some cases it may. WTO officials felt that the outcome of intensified bilateral and informal talks would only become clear after May 2005, the deadline for tabling new and revised services offers.

Forward movement in the months leading up to the Hong Kong ministerial and beyond will depend on members overcoming four challenges. First, several officials we spoke with stated that insufficient technical capacity could prevent a number of developing countries from tabling initial or revised services offers before the Hong Kong ministerial. Second, resolving the contentious, mainly North-South disagreement over the extent of liberalization under mode 4 may be crucial to achieving progress in market access. The temporary movement of service-delivering professionals is a

[6]Issues at the heart of these talks include technical disagreements on licensing and qualification standards.

[7]Counting the 25 current EU members as one.

politically sensitive issue for many developed countries, and their offers under mode 4[8] are generally unsatisfactory to most developing countries with ambitions in this area, such as India. Despite their demands, the U.S. government has clearly expressed its reticence to grant other members more extensive market access under mode 4 than is reflected in its existing commitments. According to U.S. negotiators, certain commitments under this mode could involve modifying domestic immigration law, and certain countries are simply not prepared to make this move within the WTO framework.[9] Given the priority placed on obtaining mode 4 concessions, this discord may become increasingly problematic.

A third factor that could affect progress in services negotiations is the question of balance. Malaysia, Thailand, and the Philippines allegedly want a concession on emergency safeguards before fully engaging in market access bargaining. Brazil has tied its willingness to press forward in services talks to obtaining satisfaction in agriculture. Continuing to tie progress in services talks relative to other areas could be problematic, as the request-offer approach to negotiating services liberalization is inherently and comparatively slow. Moreover, the greater complexity of identifying and dismantling often opaque barriers to trade in services slows the speed of services talks. The head of the WTO Secretariat's services division thinks that members will take 18 months to reach a meaningful agreement once they start negotiating on a more detailed level than they are currently. Finally, there is wide agreement that negotiators need to summon more political and technical resources from their capitals to conclude a meaningful services agreement. More than in other areas of trade, barriers to trade in services often occur behind borders, such that dismantling these measures requires involvement on the part of national

[8]Mode 4 is an issue in both market access and domestic regulation negotiations.

[9]In a World Bank study, Chaudhuri, Matoo and Self (2004) specify that with respect to mode 4, the GATS covers two categories of measures: "those affecting 'service suppliers' of a Member' of the GATS (i.e., self-employed suppliers who obtain their remuneration directly from customers) and those affecting the natural persons of a member who are 'employed by a service supplier of a Member, in respect of the supply of a service.' The Annex also states that the GATS does not apply to measures affecting individuals seeking access to the labor market of a member country, or to measures regarding citizenship, residence, or employment on a permanent basis. . . As Winters (2003) points out, unlike with the mass migration of less skilled workers, fears about cultural identity, problems of assimilation, and the drain on the public purse are not really relevant to mode 4. Host country concerns often pertain to national security, the difficulty in enforcing temporariness, and the impact on the labor market." The two authors note that what lacks clarity in GATS includes the definition of "temporary movement," and the types of contracts it covers.

ministries, subfederal level regulators, and various authorities not normally involved in trade policy. This poses a problem for many small developing countries.

Economic Incentives for Doha Negotiations

The Doha trade negotiations aim to increase international trade in order to improve member countries' economic growth and development. Economists have used trade models to generate numerous studies that estimate potential economic gains from trade liberalization for developed and developing countries alike. These estimates vary significantly, depending upon the extent of trade liberalization assumed and other key characteristics of the models. Several studies find that estimated worldwide economic gains accrue to both developed and developing countries. However, the distribution of economic gains may vary within and between countries, creating perceived winners and losers. As such, the individual economic incentives that countries face may differ, thereby affecting each country's negotiating goals within Doha.

Doha Round Liberalization Is Expected to Yield Benefits and Costs

A primary rationale driving the Doha liberalization agenda is the belief that international trade can positively benefit a country's overall growth and development. Potential benefits occur as international trade increases competition and specialization, provides greater access to technology, and expands export markets. Over time, a more liberal trading regime may reduce costs on both imported manufacturing inputs and exported final products that create incentives for foreign producers to invest in new production – benefits typically referred to as dynamic gains from trade.

While the role of international trade in fostering growth and development has become more widely accepted, economists have also argued that trade liberalization can involve significant adjustment costs.[1] Adjustment costs may include unemployment in sectors that are not internationally competitive or costs of fiscal reform as governments heavily dependent on trade taxes shift toward income or production taxes. Additionally, international trade may yield an uneven distribution of economic gains, creating temporary winners and losers between countries as well as within them. As each country participates in the Doha negotiations, it is working to achieve a balanced package of commitments that will be politically acceptable to its various domestic constituencies.

[1]Some economists have highlighted that developing countries may also face some specific challenges with trade liberalization such as greater instability due to volatile export markets and an increased reliance on international debt to finance trade deficits. See appendix IV in GAO-05-150 for further discussion.

Nevertheless, without considering distributional issues, several studies predict that both developed and developing countries stand to benefit economically from multilateral liberalization. Developed countries are positioned to receive gains from trade liberalization since they are large traders and currently face relatively high tariffs for exports into developing countries, particularly for industrialized goods. Developing countries stand to receive gains from trade liberalization due to the fact that developed countries often have pockets of high average tariffs on products that developing countries tend to export. High developed country tariffs tend to apply to agricultural and processed agricultural goods as well as to light manufactures such as textiles and clothing. When weighted by the amount of trade occurring under them, these tariffs translate into significant trade barriers for developing countries. Developing countries also stand to gain significantly from liberalization by other developing countries. The share of developing countries' agricultural exports going to other developing countries rose from 28 percent in the 1980s to 37 percent in 2001. However, in many cases, barriers imposed by developing countries on goods from other developing countries are even higher than those they face from developed countries, impeding potential South-South trade between developing countries.

Economists Use Trade Models to Estimate Economic Gains

Economists often estimate the benefits and costs of easing trade restrictions by examining a recent period and estimating how trade and economic welfare would have been different under a scenario where certain trade restrictions were eased. Concurrent with the WTO and other trade negotiations, numerous trade models have been used to simulate liberalization of trade policies and calculate the likely range of effects on variables such as exports and imports, tariff revenues, production, prices, and income. Many of these studies use a computable general equilibrium (CGE) model called the Global Trade Analysis Project (GTAP) model. GTAP is a global general equilibrium model that describes the relationship between all sectors within an economy and all economies worldwide. In its general form, GTAP is a static model, which means that it simulates how economies will respond only to the trade policy change being examined. Results generated from GTAP should be interpreted as order-of-magnitude results rather than single point best estimates because the assumptions regarding how responsive economic variables are to policy changes drive the results.

Extensions of GTAP and other CGE models have been made to take into account how economies will grow over time. These dynamic versions of

GTAP may include information on growth rates of capital, investment, and productivity. Additionally, while the general form of GTAP includes an assumption of perfect competition and constant returns to scale, extensions of GTAP have incorporated characteristics readily observed in manufacturing, such as imperfect competition and increasing returns to scale.[2] In these cases, trade liberalization can lead to greater specialization and increased economic gains over time. However, information on how firms respond to market changes in the long run is inherently more difficult to measure with certainty and, as such, results yielded from these models should be viewed with this limitation in mind.

Estimated Economic Gains from Trade Liberalization Vary

Table 2 provides a listing of various estimates of the economic gains from trade liberalization under selected trade liberalization scenarios. The table is not comprehensive but is intended to illustrate the wide range of results estimated through trade models – economic benefits ranging from $22 billion to $574 billion worldwide. Results vary depending upon the type of model (static vs. dynamic), key assumptions in the model (perfect competition or imperfect competition), and the ambition of the liberalization scenario.

[2]Increasing returns to scale refers to production conditions where the cost per unit of production falls as the level of production rises. When production for exports expands, the decrease in unit costs will create greater economic benefits. Imperfect competition is correlated with increasing returns to scale because firms whose production is characterized by this condition are able to capture some monopoly powers.

Table 3: Models Estimating the Economic Benefits from Tariff Reduction in the WTO Doha Round

Model	Tariff reduction scenario	Sectors included	Estimated annual economic benefit ($US billions)[a]
Static models that assume perfect competition			
Anderson et al	100% linear cut	Agriculture Manufacturing	$254
Cernat et al	50% linear cut	Agriculture Manufacturing	$40
De Cordoba and Vanzetti	50% linear cut for industrialized countries; 33% linear cut for developing countries; capped maximum rate, sector initiatives; 5% of lines excluded for developing countries	Agriculture Manufacturing Services	$123
	Swiss formula cut at 6.8% for industrialized countries and 25% for developing countries; 5% of lines excluded for developing countries		$108
Hertel and Martin	33% linear cut	Manufacturing	$107
IMF and World Bank	100% linear cut	Agriculture Textiles	$194
Laird et al	50% linear cut for industrialized countries; 33% linear cut for developing countries	Manufacturing	$22
	Swiss formula cut with certain zero tariff initiatives in chosen sectors		$33
OECD	50% linear cut; decline in trade costs equal to 1% of trade; tariff cuts apply if rate falls below applied level	Agriculture Manufacturing Services	$117
	Swiss formula cut with coefficient of 5; decline in trade costs equal to 1% of trade; tariff cuts apply if rate falls below applied level		$159
	100% linear cut; decline in trade costs equal to 1% of trade		$174
Shakur et al	36% linear tariff cut; reduction of agricultural subsidies	Agriculture Manufacturing	$38
	100% linear tariff cut; elimination of agricultural subsidies		$82
World Bank (1)	Tariff targets of 5% (10%) and 1% (5%) for agriculture and manufacturing respectively for industrialized (developing) countries; capped maximum rates; elimination of subsidies	Agriculture Manufacturing	$291[b]
Static models that assume imperfect competition			
Brown et al	33% linear cut	Agriculture Manufacturing Services	$574
Francois et al	Swiss cut with maximum tariff of 25%; 50% reduction in agriculture subsidies and services barriers; decline in trade costs equal to 1.5% of trade	Agriculture Manufacturing Services	$206
	100% linear cut in tariffs, agriculture subsidies and services barriers; decline in trade costs equal to 1.5% of trade		$367
Dynamic models that assume perfect competition			
World Bank (2)	100% linear cut; removal of subsidies	Agriculture Manufacturing	$385[b]

(Continued From Previous Page)

Model	Tariff reduction scenario	Sectors included	Estimated annual economic benefit ($US billions)[a]
Dynamic models that assume imperfect competition			
Nagarajan	50% linear cut; decline in trade costs equal to 1% of trade.	Agriculture Manufacturing Services	$385

[a]Models rely on base year data from various years, including 1995 and 1997.

[b]Results are for the year 2015.

Sources:

Anderson et al., "The Cost of Rich (and Poor) Country Protection to Developing Countries." *Journal of African Economies*, vol. 10, no. 3 (2001): 227-257.

Cernat et al., *Back to Basics: Market Access Issues in the Doha Agenda*, Geneva: UNCTAD, 2002.

De Cordoba, S.F., and Vanzetti, D., "Now What? Searching for a Solution to the WTO Industrial Tariff Negotiations", Geneva: UNCTAD, 2005.

Hertel, T.W., and Martin, W., "Second-Best Linkages and the Gains from Global Reform of Manufactures Trade." *Review of International Economics*, vol. 9, no. 2 (2001): 215-232.

IMF and World Bank, "Market Access for Developing Country Exports – Selected Issues", Washington, IMF: 2002.

Laird et al, "Market Access Proposals for Non-Agricultural Products", Geneva: UNCTAD (2004)

OECD, *The Doha Development Agenda: Welfare gains from Further Multilateral Trade Liberalization with Respect to Tariffs*, Paris: OECD, 2003.

Shakur et al, "How Comprehensive will be the Doha Round? Experiments with Agricultural and Non-agricultural Reforms." New Zealand: Massey University Discussion Paper 02.11, 2002.

World Bank (1), *Global Economic Prospects: Realizing the Development Promise of the Doha Agenda*, Washington: World Bank, 2003.

Brown et al, "Computational Analysis of Multilateral Trade Liberalization in the Uruguay Round and Doha Development Round." Ann Arbor: University of Michigan Discussion Paper No. 489, 2002.

Francois et al, *Economic Benefits of the Doha Round for the Netherlands*, the Hague: Agricultural Economics Research Institute, 2003.

World Bank (2), *Global Agricultural Trade and Developing Countries*, Washington: World Bank, 2004.

Nagarajan, N, *The Millennium Round: An Economic Appraisal* , Brussels: CECA Economic Papers, No. 139, 1999.

For example, the level of tariff cuts and sectors included for liberalization determine the ambition of the liberalization scenario and are one important factor accounting for variation in the results in table 2. Anderson et al. estimate gains of $254 billion with a full removal of tariffs on agricultural and industrial goods, while Cernat estimates gains of $40 billion with a 50 percent reduction. An OECD model on liberalization in agriculture, manufacturing, and services shows that as tariff reductions are increased from a 50 percent linear tariff cut to a more ambitious Swiss formula tariff cut, to a 100 percent tariff cut, economic gains rise from $117 billion to $159 billion to $174 billion, respectively. Several studies suggest that liberalization of agriculture will provide significant benefits to developing countries, despite the small size of agriculture in global output. Models by Anderson et al. and the World Bank estimate that roughly two-thirds of global economic gains from the liberalization of agricultural and industrial goods come from agricultural liberalization. The study by Brown et al., however, estimates that the largest economic benefits, $414 billion, come from liberalization of services and that there is an actual global net loss of income from agricultural liberalization of $3 billion.[3]

Several studies in table 2 also find that the distribution of economic benefits between developed and developing countries may be relatively even (ranging from 40 percent to 60 percent for each). Such benefits as a share of GDP, however, would be much larger for developing countries. For example, according to estimates by the World Bank, liberalization of both agricultural and industrial tariffs would provide $385 billion in economic benefits that would be equally divided between developed and developing countries. However, relative to their income levels, developing countries would gain 1.5 percent of GDP compared to 0.5 percent of GDP for developed countries. Several studies emphasize that the majority of gains for developed countries derive from lowered tariffs by other developed countries – a finding that is true for developing countries as well.

In addition to caveats previously discussed, three limitations of trade models should be acknowledged:

- *Difficulty in measuring current levels of protection*. Many trade model estimates are based on analysis of current levels of trade protection that are difficult to measure due to the presence of nontariff barriers, non-ad valorem tariffs, and gaps between bound tariffs and applied tariffs. In some cases, data on tariffs may not be current enough to include information relating to preferential tariff rates or country accessions to the WTO. As a result, economic benefit estimates yielded from these data may be overstated because they account for tariff reductions that have already taken place. Economic benefit estimates may also be overstated if the analysis is focused on reductions in bound tariffs rather than reductions in applied tariffs – wrongly assuming that any reduction in the bound rate would translate into an equal reduction in the applied rate.

[3]This result is partially due to the assumption of constant returns to scale for agriculture but increasing returns to scale for nonagriculture.

- *Costs of adjustment.* Many trade model estimates do not take into account adjustment costs to trade liberalization, such as a rise in unemployment or consumer prices during a transition period to the new trade policies. The more ambitious the liberalization scenario, the greater the long-term economic gain—as well as the short-term economic costs—are likely to be. Development institutions such as the World Bank, IMF, and United Nations have placed recognition on these costs, though there is presently limited understanding of the extent of such costs.

- *Structural features of some economies.* Many trade model estimates use general assumptions regarding industry characteristics, which may not account for positive effects due to industrial policies. Some economists have noted that under certain conditions there are potential benefits in using tariffs to support growth in new industries.

Trade Liberalization May Create Both Winners and Losers

While many studies estimate that trade liberalization is likely to result in economic benefits worldwide, there is likely to be differentiation in economic gains between and within individual countries. In the short run when adjustment costs are present, liberalization is likely to create winners and losers. For example:

- *Net food exporters vs. net food importers.* Regions that are significant agricultural exporters are expected to gain significantly from the agricultural liberalization measures being negotiated in Doha. However, the estimated gains are smaller and sometimes negative in regions that are large net importers of food because the potential removal of developed country subsidies may increase world food prices. The IMF estimates that major net exporters of food in Latin America and sub-Saharan Africa could gain between 0.3 percent and 0.6 percent of GDP from agricultural liberalization, while major net food importers in North Africa and the Middle East could lose 0.3 percent of GDP. Other large net food importing countries include South Korea, Russia, and Venezuela.

- *Countries that do not receive trade preferences vs. those that do.* Certain developing countries are offered nonreciprocal trade preferences into developed country markets. Under multilateral trade liberalization, those preferences may be eroded as overall tariff rates are reduced. As such, countries that do not receive trade preferences may gain a competitive advantage over developing countries that currently participate in preference programs. Potential economic costs associated with erosion of preferential access are difficult to determine, however, given the mixed empirical evidence on program benefits.[4] The IMF notes that erosion of sugar and banana preferences could be a concern. Mauritius, for example, benefits substantially from preferential access for its sugar exports, and Caribbean nations benefit from preferential access for banana exports.

- *Traders vs. non-traders in tariff revenue dependent countries.* For countries that are dependent on tariff revenues to finance government operations, the tax burden on importers who pay those tariffs may be relatively high compared with the burden on consumers or domestic industries that pay consumption or production taxes. As tariffs are reduced through trade liberalization, tariff revenues may also be reduced if there is not a sufficient increase in the quantity of imports in response to lower tariff rates. In such cases, the burden of financing government operations may shift away from traders and toward non-traders within an economy. For African least-developed countries that, on average, rely on tariffs for 34 percent of government revenue, the potential distributional consequences from lower trade taxes is likely to be an important adjustment cost to trade liberalization.

[4]Several studies note that benefits have been limited due to already low developed country tariffs and poor program utilization rates. Empirical examination of the more recent targeted programs, such as the United States' African Growth and Opportunity Act (AGOA) or the European Union's Everything but Arms (EBA) initiative, suggests that the economic impact has been greater.

Trade Negotiating Interests and Affiliations of Leading Merchandise Exporters

			Exports by Sector (%)		
Top 50 merchandise exporters in 2003 (in rank order of dollars exported)	EU[a]	G-90[b]	Agriculture	Industrial goods	Services
Germany	X		5	81	15
United States			7	64	29
Japan			1	85	14
China			5	84	11
France	X		9	70	21
United Kingdom	X		4	64	32
Netherlands	X		16	66	19
Italy	X		6	75	19
Canada			11	76	13
Belgium	X		8	71	21
Hong Kong			2	80	18
South Korea			2	83	15
Mexico			5	88	7
Spain	X		11	54	34
Taiwan			n/a	n/a	n/a
Singapore			2	79	19
Russian Federation			6	82	11
Sweden	X		6	71	23
Switzerland			2	73	25
Malaysia			8	78	14
Austria	X		5	64	31
Ireland	X		6	70	24
Saudi Arabia			1	93	7
Thailand			14	68	18
Brazil			27	59	14
Australia			21	58	22
Norway			5	71	23
Denmark	X		15	52	32
United Arab Emirates			n/a	n/a	n/a
Indonesia			14	75	10

Areas of Negotiation										
Agriculture				Industrial Goods		Services	Trade Facilitation		Rules	
Cairns Group[c]	G-20[d]	G-10[e]	G-33[f]	Friends of Ambition[g]	Tariffs over 10%[h]	Have tabled offers[i]	Core Group[j]	Colorado Group[k]	FANs[l]	Have initiated over 75 antidumping investigations since 1995
				X*		X*		X*		X*
				X		X		X		X
		X		X		X		X	X	
	X		X			X				X
				X*		X*		X*		X*
				X*		X*		X*		X*
				X*		X*		X*		X*
				X*		X*		X*		X*
X				X		X		X		X
				X*		X*		X*		X*
				X		X		X	X	
		X	X	X		X		X	X	X
	X				X	X			X	X
				X*		X*		X*		X*
		X				X			X	
				X		X		X	X	
				X*		X*		X*		X*
		X		X		X		X	X	
X						X	X			
				X*		X*		X*		X*
				X*		X*		X*		X*
X	X				X	X			X	
X	X				X	X			X	X
X				X		X		X		X
		X		X		X		X	X	
				X*		X*		X*		X*
X	X		X			X	X			

(Continued From Previous Page)

			Exports by Sector (%)		
Top 50 merchandise exporters in 2003 (in rank order of dollars exported)	EU[a]	G-90[b]	Agriculture	Industrial goods	Services
India			9	57	34
Poland	X		7	73	20
Finland	X		7	80	13
Czech Republic	X		5	80	16
Turkey	C[(m)]		8	62	30
Hungary	X		7	75	19
Philippines			5	87	8
South Africa		X	8	79	14
Iran			3	92	5
Israel			4	69	27
Portugal	X		7	65	28
Argentina			43	47	10
Algeria			n/a	n/a	n/a
Venezuela			2	95	4
Ukraine			12	68	21
Slovak Republic	X		5	80	16
Chile			29	52	19
Nigeria		X	n/a	n/a	n/a
Vietnam			24	61	15
Kuwait			n/a	n/a	n/a

Areas of Negotiation										
Agriculture				Industrial Goods		Services	Trade Facilitation		Rules	
Cairns Group[c]	G-20[d]	G-10[e]	G-33[f]	Friends of Ambition[g]	Tariffs over 10%[h]	Have tabled offers[i]	Core Group[j]	Colorado Group[k]	FANs[l]	Have initiated over 75 antidumping investigations since 1995
	X		X		X	X	X			X
				X*		X*		X*		X*
				X*		X*		X*		X*
				X*		X*		X*		X*
			X			X			X	X
				X*		X*		X*		X*
X	X		X				X			
X	X									X
					X					
		X				X			X	
				X*		X*		X*		X*
X	X				X	X				X
					X					
	X		X		X		X			
				X*	X	X*		X*		X*
X	X			X		X		X	X	
	X		X		X		X			
					X					

Source: GAO analysis of WTO documents and data, World Bank export data, and other information

Notes:

Non-WTO members are shaded.

X* indicates that the country participated in the group or the action as a member of the European Union.

[a] Other members of the European Union are Cyprus, Estonia, Greece, Latvia, Lithuania, Luxembourg, Malta, and Slovenia. Turkey is a candidate for membership, as are Bulgaria, Croatia, and Romania.

[b]The G-90 is a large umbrella group including the least developed countries and other countries from Africa, the Caribbean, and the Pacific.

[c]Other members of the Cairns Group are Bolivia, Colombia, Costa Rica, Guatemala, New Zealand, Paraguay, and Uruguay.

[d]Other members of the G-20 are Bolivia, Cuba, Egypt, Pakistan, Paraguay, Tanzania, and Zimbabwe.

[e]Other members of the G-10 are Bulgaria, Iceland, Liechtenstein, and Mauritius.

[f]Other members of the G-33 are Antigua and Barbuda, Barbados, Belize, Benin, Botswana, Congo, Cote D'Ivoire, Cuba, Dominican Republic, Grenada, Guyana, Haiti, Honduras, Jamaica, Kenya,

Mauritius, Madagascar, Mongolia, Mozambique, Nicaragua, Pakistan, Panama, Peru, Senegal, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Sri Lanka, Suriname, Tanzania,Trinidad and Tobago, Uganda, Zambia, and Zimbabwe.

[g]Other members of the Friends of Ambition are Costa Rica and New Zealand.

[h]Tariffs examined were most favored nation rates for the latest year available from the WTO. European Union member country rates were aggregated.

[i]Other WTO members that had tabled services offers, as of March 29, 2005, are Bahrain, Barbados, Bolivia, Bulgaria, Colombia, Costa Rica, Dominican Republic, Egypt, El Salvador, Fiji, Gabon, Grenada,Guatemala, Guyana, Honduras, Iceland, Jordan, Kenya, Liechtenstein, Macao, Mauritius, New Zealand, Panama, Paraguay, Peru, Senegal, St. Kitts and Nevis, Sri Lanka, Suriname, and Uruguay, as well as other countries that are members of the European Union.

[j]Other members of the Core Group are Bangladesh, Botswana, Egypt, Cuba, Jamaica, Kenya, Mauritius, Tanzania, Trinidad and Tobago, Uganda, Zambia, and Zimbabwe.

[k]Other members of the Colorado Group are Colombia, Costa Rica, Morocco, New Zealand, and Paraguay.

[l]Other members of the Friends of Antidumping Negotiations (FANs) are Colombia and Costa Rica.

[m]C indicates that Turkey is a candidate for membership in the European Union.

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In addition to the individuals named above, Michelle Munn, Kendall Schaefer, Emilie Cassou, Ann Baker, Mark Keenan, Jose Martinez-Fabre, Jonathan Rose, Jamie McDonald, and Ernie Jackson made key contributions to this report.

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