

# **Reform at the Top: What's Next for the WTO? A Second Life? A Socio-political Analysis**

**Daniel Drache**

WORKING PAPER SERIES

Centre for the Study of Law and Governance  
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**Daniel Drache** is Emeritus Professor of Political Science at York University Senior Research Fellow Robarts Centre of Canadian Studies, York University. He has written and published extensively in books, articles and conference presentations on global governance, the WTO crisis, North American integration and the new geography of web 2.0 activism and social networking with its disorderly voices, contradictory interests and virulent claims of global counter publics. His articles, reports and research papers are available at [www.yorku.ca/drache](http://www.yorku.ca/drache). He has been a research associate at the European University Institute, Florence; a professor invité at CEPREMAP-CNRS, Paris; a visiting scholar at Macquarrie University and a guest lecturer at UNAM, Mexico. In 2009 he is invited to India as the Shastri Indo-Canada Distinguished Visiting Professor and lectured at ten Indian academic institutions. In June he was invited by five Argentinian Universities to lecture and give seminars on globalization after neo-liberalism. In 2010 he was the Ford Foundation Visiting Professor the Centre for the Study of Law and Governance, JNU, New Delhi. Polity Press has published his latest book, *Defiant Publics: The Unprecedented Reach of the Global Citizen* in September 2008. In November 2008 Wilfred Laurier UP published his edited volume, *Big Picture Realities: Canada and Mexico at the Crossroads*. His latest work with Les Jacobs is entitled *New Policy Spaces for a Dismal Economic Era: Trade and Human Rights*, forthcoming 2013.

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**INTRODUCTION**

A fundamental change is taking place in the global economy, and the standoff in the Doha Round has raised many questions about the World Trade Organization's (WTO's) troubled architecture (Khor, 2009). So far, the quest for renewed policy coherence in the rules-based multilateral system has produced stalemate rather than reform. The analysis that follows explores the proposition that with its narrowly cast rules, the organization charged with a mandate of global trade governance has not been able to evolve into an institution of the twenty-first century.<sup>1</sup> If anything, the gap between aspirations for reform and the stalled Doha Round has grown larger. Without the metaphoric 'knife at its throat' to shock it to its senses, the WTO will continue in the short term to be trapped by its existing architecture. The second life of the WTO will be dramatically different from the present configuration. It will have a smaller remit, be prone to mini-multilateralism and will have

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<sup>1</sup> I use the term 'global south' somewhat loosely as both geographic metaphor and historical fact to describe a very diverse group of countries, at sharply different stages of development, who see themselves as a bloc of countries with different interests than the global north—the advanced economies of the globe.

to learn to live with a proliferation of regional trade agreements. How did we arrive at this point of no return?

This paper sets out to answer this question and looks at the following ideas: first, it examines the way globalization has dramatically evolved as the golden era of export-led growth unwinds and challenges the way the WTO conducts its negotiations. In the aftermath of the global financial crisis, the WTO's member countries have not waited for the organization to rethink the state-market problematic. Countries around the world have demonstrated that they are ready to use any means available to protect their industries from the devastating consequences of a contracting world economy. New empirical evidence from Simon Evenett (2007) also demonstrates that the welfare gains from the Doha Round are paltry or negative for many countries from the global south. Second it examines the internal barriers of its legal and institutional culture standing in the way of the WTO finding a new direction. The paper demonstrates the importance for the WTO of institutional problem solving; particularly when designing a development strategy with a focus that includes public health and education that requires an unconventional response. It also explains that the unprecedented judicial power of the WTO only partly resides in its Appellate arm. The real power lies in the legalization of best-practice expectations for governments as part of the Single Undertaking. The consequence is that there has been little room for a culture of adaptive legal exceptionalism to emerge. The final section examines what is next for this member-driven organization. How should it redefine its mission? Where to, now? Four possible outcome scenarios for the future of the WTO are examined. All have very dissimilar implications for a modern trade policy and global governance. In the interminable Doha Round, trade negotiators find themselves boxed in by these new dynamics. They can no longer simply focus on the technocratic details of striking a deal aware that they will ultimately have to sell the final package to doubting publics.

## THE WORLD TRADING SYSTEM IN TURMOIL

So far, the WTO has failed to learn by doing, and take significant steps to reform its work style and decision-making processes. Strong member advocacy to alter the institutional status quo has been very weak. There is no visible member support for either a bottom-up or top-down redesign of the WTO's institutional structures that would push it in a public interest direction. To this point the WTO's legal culture has been unable to experiment with new policy initiatives or introduce a flexible trade agenda because of what Steger calls 'the GATT bias for template solutions.' It follows an agenda of single best practice, strict rule interpretation, a smaller role for the state in economic management, and above all, market access enhancement, all goals that were largely the product of the neoliberal Washington Consensus. By comparison both the International Monetary Fund (IMF) and the World Bank (WB) have tactically distanced themselves for the time being from the neoliberal policies of the recent past; recognizing the necessity for global financial reform and the re-regulation of global financial markets (see accompanying table below). In Philip Cerny's words, 'the processes of restructuration have moved the organizations from a homogenous and tightly woven model to one of increased adaptation' (2009).<sup>2</sup>

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<sup>2</sup> Each autumn the WTO organizes a major conference on topical themes such as trade and the environment, gender and even reform of its trade architecture. Despite all the papers and panel, as one ambassador noted, 'it's all talk and nothing ever comes of it.' Up to the present, there is little evidence that the WTO is planning for a post-neoliberal order that, among other things, will require a long-term perspective on a reformed trading order. Its website is not at the centre of an engaged policy debate when compared to the ICTSD (International Centre for Trade and Sustainable Development) and the South Centre (An Intergovernmental Policy Think Tank about Developing Countries) in Geneva and The Brookings Institution in Washington, DC—all are knee-deep in a policy world of sustained analytical thought.

**Table 1 The New Idea Universe**

<i>Restructuration and Structural Coherence</i>	
<i>WTO Normative Practice</i>	<i>World Bank Rebalancing Remit</i>
Single best practice	New role for the state
Strict rule interpretation	Policy experimentation e.g. capital controls
Smaller role for the state	Rebalancing social agenda and markets
Broadening market access	Problem solving, risk assessment, institution-building
Legal monitoring and enforcement	Incremental adaptation and ad hoc response to the crisis

Source: Drache 2010

For many observers, the WTO’s ‘bloated trade agenda,’ in Diana Tussie’s acerbic words, and the legal straight jacket of single undertaking (its outmoded one-size-fits-all legal framework) are reasons enough to require major surgery (Tussie, 2009). In particular, three imbalances stand out for much comment from a socio-economic point of view. The WTO has a strong, effective, and binding dispute resolution system ‘coupled with weak, ineffective political decision-making procedures’ (Steger 2008, 707). Secondly, its practices are grounded in a deep distrust of domestic politics and the belief that without the legal constraints of the WTO, protectionism would be rampant (Pauwelyn, 2008, 560). Thirdly, globalization today requires ‘strategic non-trade flanking policies’—policies around human rights, environmental sustainability, and industrial practice that will safeguard local development and domestic policy space (Pauwelyn, 2009). Paradoxically, while WTO members support human rights conventions and take measures to correct market failures, these critical public policy areas lay outside of the WTO’s institutional remit.

## **The Keynesian Correction**

To correct these structural deficits, trade politics for the 21<sup>st</sup> century require a very different global governance institution—one capable of handling complex and challenging issues (Roadnight and Higgott, 2008). In the aftermath of the global financial crisis, the WTO's member countries have not waited for the organization to rethink the state-market problematic. Countries around the world have demonstrated that they are ready to use any means available to protect their industries from the devastating consequences of a contracting world economy. Governments are gaining valuable experience managing structural change, and the state is no longer missing in action in either the global south or north. It is in full throttle with a newfound presence in leading jurisdictions. It is useful, for comparative purposes, to see how far the dynamics of state-market relations have changed since the currently stalled Doha Round was launched a decade ago. The need to map new state practices and take account of new policy communities as well as the need for far-reaching institutional stabilization and re-regulation has shifted the focus of trade politics from deepening market access to getting the institutional response right (Rodrik, 2007). It important to look at some of these developments very briefly.

Many of the new state policies that WTO member states have adopted since 2008 seem to be strongly Keynesian in inspiration. These include: state aids to take workers off the unemployment lines (wage subsidies in Germany, France and Netherlands); massive bailouts of near failed banks and investment firms (Eurozone and United States); deficit spending and macro stimulus packages to restore consumer demand and battered industries (Eurozone, China, and the United States); and new programs and initiatives to strengthen social benefits, reduce poverty and protect the most vulnerable from the global chaos (Brazil and France) (IMF, April 2009).

Other forms of intervention have been more conventional. States have a battery of policy instruments with which to protect

**Table 2 The Policy Importance of Rule-Bending Rescue Measures**

	<i>Trade Leverage</i>	<i>Multiplier Effect</i>	<i>Bad Effects</i>
Stimulus package	High	Very High	Debt Overhang
Wage subsidy	Moderate to High	High	Smallish Difficult to Phase Out
Industrial subsidy	High	Strong	Unclear and Difficult to End
Innovation	Low Weight	Unclear	Low for the Moment
Capital controls	Effective for Brazil	Across The Financial Industry	Negligible
Quotas/ antidumping	Small and Merit Tracking	Neutral	One offs Subject To National Interest and WTO discipline
Credit Expansionary Policies	Strategic and Very Focused For Both Private And State Enterprises	Large and Continuous For Corporations and For Offsetting GDP Contraction	Loans and Bailouts Leave A Decade of Legacy Costs

Source: Drache 2009

their industries and work forces ranging from quantity restrictions such as import quotas, export limitations, and voluntary export restraints, to regulatory restrictions such as domestic content requirements, sanitary and phytosanitary requirements, and safety and health regulations. Restrictive rules vary widely and cover every domain of public policy (Trebilcock and Howse, 2005). Rules and regulations restricting foreign investment in the national interest or on grounds of national security are another critical front-line area of state regulation. Currency management is a formidable weapon with which to gain a competitive edge over trading partners in difficult economic times. For instance, China has relied on a devalued

currency to lower the cost of its exports and thereby increase market share; such undervaluation is referred to as dumping or tough competitive practices. The danger here is that during times of high unemployment, currency misalignment can escalate into a full-scale trade war—witness rising China-United States tensions due to the under-evaluation of the Chinese Renminbi.

### **Rule-Bending in Un-normal Times: Both Choice and Necessity**

None of these innovative measures, however, has impacted the way the WTO understands the role of the state in the global economy. For example, its broad interpretation of subsidy rules continues to restrict the ability of governments to use subsidies for many legitimate purposes (Lester, 2010). The rediscovery by governments of these rule-bending rescue measures implemented to shore up the economy after the collapse of financial markets has been nothing short of dramatic. Despite this, we still do not have a sophisticated theory of the role of the state in the current phase of globalization, and there is still a propensity to conflate legitimate government intervention with the trade distorting use of subsidies and other measures.

Importantly, governments everywhere continue to rely on the tax system, competition policy, state enterprises, social policy, technology, and research policy to hold back the full play of free trade dynamics (Hollingsworth and Boyer, 1997). One of the consequences of effective demand management is that it requires a much more innovative role for the state. With the passage of the Lisbon Treaty in 2009, the European Union's process of integration with its large social market serves as a positive model for many other regions particularly Brazil. The Indian government has notably deepened its rudimentary welfare state with the passage of the Mahatma Gandhi National Rural Employment Guarantee. It has guaranteed each family in the rural sector more than one hundred days of paid work yearly at a minimum rate established by the central government (Dailami and Masson, 2009). So the question is, will these new domestic power

dynamics transform the multilateral agenda of trade governance and push the WTO in new and challenging directions (Zakaria, 2008)?

In the crisis, countries found a way to use ‘protection-like’ policies to deal with the exceptional circumstances not to choke off trade.<sup>3</sup> Unmanageable surges in imports, calamitous price rises in basic food items, currency spikes, and other structural and cyclical ‘disasters’ have forced states to bend, and sometimes flout, the WTO rule book, which is opposed in principle to the use of subsidies and rescue packages. It would help to have better WTO rules governing the use of state subsidies, rescue packages, and final bailouts, but it is unlikely that there will be any new framework agreement. Simon

**Table 3 Bending the Rules in Un-Normal Times: The Extended Range of Modern Protection(ist) Practices: A Selected List of Measures**

<i>Difficult</i>	<i>Contentious</i>	<i>Most Controversial</i>
Stimulus packages	Anti-dumping duties	Import quotas
Wage subsidies	Countervail duties	Customs and barriers
Packaging/labelling	Industrial Policy	Beggar-thy-neighbour tariff walls
Tech. licensing restrictng	Currency Devaluation	Voluntary export restraints
Industry rescue \$\$	State Aids/subsidies	Export Bans
Food/health standards	Unilateral safeguard action	
Bailouts	Buy America	

Source: Drache 2009

<sup>3</sup> In light of the need for legitimate government intervention, we can analytically distinguish between modern forms of social protection. Mercantilist protectionism is designed to put the boots to one’s trading partners and choke off exports. The most toxic of these beggar-thy-neighbour tariff walls is the indiscriminate use of quotas. Other measures such as safeguards, anti-dumping, state aids and subsidies, while contentious and subject to retaliatory action, are legal and long established.

Lester looked at the current draft of the revision to WTO subsidies (TN/RL/W/236) and found that it still does not allow governments to rescue industries in a crisis (IELP, 2009). He proposes an exemption for situations where imports have caused harm to domestic markets or world markets. So far, even this modest proposal is not part of the negotiations. Even if there is a ‘Doha-lite agreement’ sometime after 2012, the legal and political boulders on the path to the reform of subsidies and other interventionist measures are formidable. (See Table 2 Bending the Rules in Un-Normal Times)

### **Power Asymmetries and Getting Institutions Right**

The fact that the WTO has been unable to find a new direction requires a better understanding of the case for institutional problem solving. Problem solving is a critical activity encouraging member states to co-operate for common goals on demanding issues and to devise innovative solutions and the realistic means to achieve them. On economic issues, the primary necessity is to rebalance the free trade imperative for global market deepening with non-trade issues such as human rights, the environment, and public health. Global institutions with problem-solving capacity can establish new norms and practices in order to scale up investment in the social market, education, and industrial development. Fernand Braudel (1980) put his finger on the conditions for radical and incremental change: an institution defined by both ‘traditionalism and rigidity,’ cannot respond to the new political and structural realities taking place in the world today. Nor can it readily put itself back into the game because it cannot rebalance its decision-making processes with a new mandate. Critically absent from the institutional culture of the WTO are change-oriented structures as well as the need to reach out to social actors to be part of a new consensus.

Conceptually we can identify the step that the WTO ought to take even if it recoils from that. It makes sense for the WTO to shift focus from getting the prices right to getting the institutions right. Rodrik

(2007) notes that socially advantageous institutions provide 'security of property rights, enforce contracts, stimulate entrepreneurship, foster integration in the world economy, manage risk-taking' and most importantly, manage the trade adjustment process. For him, the most important institutions boosting momentum for growth and providing protection from global shocks are:

- Creating institutions for property rights and contract enforcement;
- Regulating institutions to deal with externalities, scale economies, informational incompleteness;
- Market stabilizing institutions for monetary and fiscal management;
- Legitimizing institutions for social protection and insurance; redistributive policies; institutions of conflict management, and social partnerships (Rodrik, 2002).

He rightly adds that while creating, protecting, and solidifying these institutions takes time, structural problems are always easier to solve under conditions of robust economic growth rather than stagnation. The strength of institutional diversity and localism are 'the most important determinant for long-term growth.' (Rodrik, 2002) A range of policies such as trade protection, temporary monopolies, subsidized credits, and tax incentives often go hand-in-hand with strategies for industrial growth and diversification. The subsidies provided by governments, often for developmental purposes, are essential to recovering the high costs of innovation. Yet many of these practices do not square with the conventional understanding in the halls of power in Geneva of what constitutes 'best practice' in terms of its codes and discipline.

In order to better equip countries to deal with heightened inequality and environmental degradation, he believes it is important to return to a 'thin' model of globalization with less focus on international discipline to harmonize state policies to a single best practice. Designing such a growth strategy is much more difficult

than implementing typical integration policies. The reason for this is that a growth program requires in turn two very different ideas.

The first requirement is an investment strategy to kick-start growth to higher but sustainable levels, and the second, an institution-building strategy to strengthen the economy's resilience in the face of global volatility and adverse shocks. The developing world would be better off with a thin set of rules that promote 'collaborative strategies to foster entrepreneurship and institution building' (Rodrik, 2002). The Doha Round is problematic because its 'thick' rules aim at maximizing trade and investment flows at the expense of policies that would promote more experimentation and a broad agenda of institutional reform.

#### **GLOBAL STRUCTURAL CHANGE AND THE RISE OF THE REST: A NEW DIVISION OF LABOUR**

Trapped by these dynamics, the world's trade authority has not had the ability up until now to take a hard look at itself. Organizations evolve and adapt to structural change most often incrementally, but sometimes, faced with a near-death experience an organization will address the basic question of its survival. With the metaphoric knife at its throat, it has to go into survival mode. So far there is no sign of that the WTO brass believes there is a crisis that demands life-saving surgery. The search for common ground in the draft texts, in May 2010, failed to open any space that would lead to a successful conclusion. The WTO continues to tread water, unable to build a development perspective into the existing texts of the Chairs to forge a consensus. Pascal Lamy, Director General of the WTO, has admitted that there is no way, 'to structure and steer discussions amongst 150 plus members in a manner conducive to discussion.' So what is next for this member-driven organization? How should it redefine its mission? Where to now? Governments and global civil society face four possible outcome scenarios of the current trade negotiations. All have implications for a modern trade policy so it is

essential to understand better where this beleaguered organization is possibly heading.

### **Scenario 1: Functionality Restored**

For the WTO, the most attractive scenario is that the deeply divided membership revive the Doha Round mandate and bring it to a successful conclusion heeding Lamy's call to make a final effort to cut a deal. The hope that new market access will become an engine of growth is a strong incentive forcing major countries back to the bargaining table with a smaller-oriented development package. The elimination of all export subsidies and the substantial reduction in domestic support by 2013, as hoped for by the Cairns group of agricultural countries, must be set aside for less ambitious goals that are more in line with a Doha-lite agreement.

The emphasis on fairer trade is a key demand for developing countries and the suspended talks would get an injection of political will if the Doha negotiators made fairer trade the centrepiece of the Round. Critically, the United States, European Union, and China must recommit to global free trade while, in return, India, China, and Brazil accept a deal on agriculture, intellectual property rights and lower tariffs though with much reduced ambition from the earlier starting point. The United States will cut subsidies to its farmers deeper than previously offered. India and China will accept market opening for some key industries and tariff reduction in telecommunication and chemicals. Significantly there will be more opt outs and side-deals, particularly in agriculture, and the global south will obtain the special safeguard mechanism they wanted. Exemptions for many global south countries with more than fifty percent of their populations in rural agriculture will be built into the texts.

One innovation is that rule of reciprocity-based bargaining will be modified in some instances to allow global south countries to gain larger benefits from the round. Some modest progress will be

made on biodiversity and geographical indicators. More plurilateral agreements can be anticipated in the future, possibly with respect to public health and the environment. They are difficult to organize but the idea that a critical mass of countries can sign an agreement and others will come aboard later has its champions. But the legal straight jacket of the single undertaking remains the founding principle of the organization. If anything, the legal culture of the WTO will emerge stronger at the expense of the informal process of trade diplomacy.

#### *Likelihood*

It is doubtful that this scenario has any chance of success. The United States, European Union, and India cannot agree on the most contentious issue of subsidy cuts to agriculture, and India and other countries do not accept the unreasonable ceilings placed on the proposed safeguard mechanism. Other imbalances are slowing down the institutional reform of the WTO. The tightening of fiscal policies in Europe, the sharp decline of the exchange rate against the dollar as well as tepid Eurozone growth make the likelihood of any deal much more difficult; reinforcing the belief that the WTO is less relevant as a governance institution.

Lamy's repeated appeals for 'greater ambition,' not surprisingly, have fallen on deaf ears. The structural imbalance between surplus and deficit economies demands a bolder step for global macro-economic reform. It is likely that emerging markets will continue to accumulate large foreign surpluses as growth is much faster in developing countries compared to the global north.<sup>4</sup> If Fred Bergsten

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<sup>4</sup> In 2010, China has a saving rate of 38 percent compared to the paltry 3 percent for U.S. consumers. The challenge will be to force Chinese families to abandon thrift for mass consumption and to find a way to entice profligate U.S. consumers to return to their spendthrift ways. So far, no economic theory can explain shifts in consumer norms and practices. It is expected that the current account deficit in the United States will exceed \$800 billion, the record of 2006. Investor appetite post-Greece crisis is to buy United States Treasury securities to finance the American deficits.

is right and these new imbalances threaten a global recovery, they will provoke strong political reaction in the Obama Administration (Bergsten, 2010). Against this backdrop of the sovereign debt crisis and record high unemployment, every indication is that Washington will not assume its old role as consumer and borrower of last resort. It will not push Congress to wrap up the stalled Doha Round.

#### *Implication*

If a deal was reached, it would close the door on the current debate about the WTO's future. Compared to the World Bank and IMF, which have distanced themselves from the former neoliberal, privatization agenda, there would be no uptake for the WTO to reform its rules and broaden its trade agenda to function differently or embed a development agenda in the core understandings of the organization.

#### **Scenario 2: Trade Pause**

With the deep divisions between the global north and south, a trade pause scenario may be attractive for countries left exposed to the global economic crisis. The principal idea behind an extended suspension of negotiations is that, at present, the negotiations collapse because common ground in key areas such as agriculture, intellectual property rights, and non-agricultural sectors such as chemicals is shrinking. There are simply too few bridges to span the negotiating divides. Currently, U.S. negotiators prefer 'no deal to a bad deal,' and China, with its informal preferential trading system with Latin America, Asia and Africa, recognizing the advantages to putting negotiations on the back burner, tacitly supports the idea of the pause. The European Union finds much to support in a trade pause that leaves its social market protected from any new de-regulatory pressures. Very large spending cuts and tax increases in the European Union have made the Eurozone wary about any deal that would result in a flood of low price goods from China and other low cost

producers. The threat of further job losses to the Eurozone from southern producers is seen as an unacceptable risk to communities and industries struggling to cope with the harsh conditions of a very modest recovery.

The global south, having mastered the intricacies of complex, reciprocal concession bargaining, is unqualifiedly likely to support a trade pause. Mini-lateralism offers them a regional alternative to the stalled Doha round. Their command of technical expertise has changed the dynamics of negotiations and given the global south new confidence to challenge U.S. and E.U. dominance in the bargaining process. To a degree that was absent in previous rounds, its trade negotiators have learned how to calculate the consequences of a deal on farmers in rural India, China, Indonesia and sub-Saharan Africa, and the risk of displacing millions of people outweighs the benefits of liberalizing agriculture at the present time (Tussie 2009). With no consensus on the horizon, the trade pause is a very attractive low political cost though problematic scenario. Given the new dynamics of power, it creates many uncertainties for the future of the WTO. If it is on life support many members will take it as a legitimacy crisis which would add greatly to its current institutional gridlock.

#### *Likelihood*

This scenario is the most probable. The questioning of market-based efficiency is well documented in the literature on trade and development and is centered on two ideas. First, at the beginning of the millennium, neither Marxist dependency theory nor liberal economic theory foretold the rise of the BRICS and such large-scale development. Their share of global GDP has overtaken that of advanced capitalist economies. Their real GDP growth has been without precedent in modern annals. The ‘big emerging economies’ have not only caught up but are now in overdrive compared to the anaemic performance of the United States and the European Union. In 2006, *The Economist* reported that half of the world’s industrial products were produced in the global south, and according to the

newest research, that within a decade, 20 percent of the Fortune 500's firms would be southern multinationals (Drache and Froese, 2008). Secondly, for many emerging economies not part of the BRICs, the high cost of an export-driven strategy is that it leads to overspecialization in a handful of goods. Over concentration in a single market or a group of countries has created new structural problems for many southern economies and with it increased vulnerability to highly unstable global commodity markets.

*Implication*

An extended trade pause could be the trigger that forces the WTO to redraw the line between trade and non-trade issues, and develop new processes and practices. The modality would be the establishment of a high-powered Commission very different from the failed Sutherland Commission and closer to the Warwick Commission with its wide-angled analysis of global change. The WTO would then have to consider different kinds of reforms to its rules and norms, and more particularly to the role of its executive and legislative arms (Sauvé, 2007).

**Scenario 3: Messy Multilateralism**

Richard Haas (2010) has coined the term 'messy multilateralism' to grapple with the fact that the world is too complex. There are too many countries at the table to strike large legal agreements when each sovereign state gets a vote. Democratic multilateralism is often a recipe for doing nothing as the Doha Round makes abundantly evident. Moises Naim (2009) has given legs to the idea of strategic, targeted, plurilateral deals arguing that smaller deals and agreements are the only practical solution to address the world governance crisis. Naim argues for abandoning 'the grand bargain' as a house of mirrors and a fool's paradise of failures. Deals could involve, he says, the top twenty global traders, or the top 20 polluters or the 20 sub-Saharan countries most in need who would

be invited to the table to make smaller, exclusive deals that others can join later on. All this requires, he emphasizes, 'is the smallest number of countries needed to have the greatest impact in solving a particular issue.' (Naim, 2009)

Mini-multilateralism would be criticized for being anti-democratic and exclusive he argues, but in a world that needs to put a premium on pragmatic problem-solving and moving the envelope forward, it should be apparent that countries are already practicing mini-multilateralism regionally and, in the absence of an inter-state consensus, are very keen to sign preferable trade agreements. Mini-deals are open to any country and are a functional alternative to the deadlocked Doha Round. Another advantage is that they are a highly attractive alternative for a multi-polar world with sharply divergent agendas. If countries cannot build credible long-term policies with consensus, they need to abandon this kind of outdated thinking for plurilateral deals requiring only a critical mass to come into effect.

#### *Likelihood*

This option appeals to the newfound confidence of the global south. Nora Lustig and Luis Lopez-Calva (2010) recently tested the proposition that a rising tide of trade lifts all countries that have significant numbers of citizens living at or below the poverty line by analyzing declining inequality in Latin America between 2000 and 2006. Their findings are significant because although inequality continues to be a dominant reality in Argentina, Brazil, Mexico, and Peru, out of seventeen Latin American countries for which data are available, twelve experienced a decline in the GINI coefficient. The largest decrease in the earning gap occurred in countries with equalizing contributions and government transfers to the poor. In Argentina, Brazil and Peru, these kinds of redistribution initiatives targeted the upgrading of skills and broadening access to education. The report underscores the fact that making public spending and taxes more progressive and improving the quality of public services for the poor, especially in education, is a key measure to

keeping society on the path towards greater equality of opportunity (Lustig and Lopez-Calva, 2010, 6).

In another recent report, the North-South Institute documents the failure of the trade liberalization model to benefit the least developed countries. Countries such as Mali, Mozambique, and Sudan send 55 to 80 percent of their total exports to a single country. Exceedingly high levels of partner concentration in exports are evident in the cases of Bangladesh, Bolivia, Colombia, Ghana, and Honduras. Continued reliance on this model has pitfalls—on the export side, almost all of these countries are vulnerable to cost volatility due to their dependence on importing energy. The earnings from their ‘so-called’ success in single agricultural commodities often add up to 15 percent of the total cost of imports. The essential problem is that many developing countries cannot afford to consume imported goods and services at the rate needed to function effectively (Heidrich and Weston, 2010, 40).

Developing countries have learned to support strategies that make it easier to move up the value added chain by transitioning from producing raw materials to processing agricultural and manufactured products rather than supporting strategies driven by the free trade model. Rules need to be asymmetric, but in Stiglitz’s words, ‘asymmetric in the precisely opposite way to ... the present configuration that discriminates against developing countries’ by preventing them from developing their own institutional response to the need for competitive, redistribution strategies. In the nineties, East Asian countries intervened in their markets and used a variety of means, including subsidies and capital controls, to grow faster than many Latin American governments that relied on unfettered neoliberalism (Stiglitz, 2006).

This diagnostic framework is encouraging global south countries to experiment with pluralistic, highly diverse strategies tailored to actual conditions. Unprepared to wait for the reform of international institutions, they have already taken on new roles at the global level most importantly in the G20. While not without its critics, the G20

has become more inclusive and representative of the new geometry of global power. Of course, it is too early to predict whether mini-multilateralism will replace the multilateral system as a forum for global governance, but it is likely to remain the WTO's chief rival and competitor for the near and mid-term future.

#### *Implication*

The reconfiguration of the world trading system into a more fragmented and regionally anchored proliferation of regional agreements will leave a legal gap for the near future. The unwinding of multilateralism will generate new trade fictions and stress test the WTO's dispute settlement mechanism. The fragmented nature of national sovereignty requires that democratic politics be carried to the global level. As countries shift their attention to creating domestic policy space to maintain social peace and stimulate economic growth, a global architecture that is more sensitive to the developmental needs of rich and poor countries alike will eventually emerge.

#### **Scenario 4: Institutional Break-up**

If tensions become too great to manage, one or more of the major countries may decide to disinvest in the WTO and disengage itself from the Doha Round. Any such decision would lead to a decline in the credibility of the talks and the WTO itself. The Marrakesh Agreements enable a member to withdraw on sixty days notice but no country Steger reminds us has ever quit the organization. (Steger, 2007) A country would not have to leave definitively but could simply decide to disengage itself politically from the Round. For instance they could minimally participate in the negotiation process and committee work. Frustration with the deadlocked round could unleash a backlash against this moribund organization that has lost the functionality to negotiate further reductions in tariffs or mutual concessions to liberalize trade. Orderly withdrawal from the WTO is messy, and legal experts are divided about the feasibility of

this option. Steger's view is that a country 'cannot withdraw from only one part of the WTO treaty, it must withdraw from the WTO Agreement as a whole' that works as an effective deterrent against the most stout-hearted (Steger, 2007, 491). Given that the WTO is a binding international treaty and unlike a commercial contract that a country can cancel whenever it is expedient to do so, no country can easily walk away from the WTO's comprehensive legal regime effectively shutting down this option.

However the idea of going around the WTO instead of through it is an option for a handful of key countries like China, which has complex relations with Africa and other developing states. China is making commercial deals that give them strategic access to resources in Africa and Latin America. The growth of these preferential trade deals certainly is a new development and bears monitoring. De facto they create new external pressures and challenged for the world's multilateral trading system. So even if some countries were to quit the organization, the WTO's legal culture and dispute resolution mechanism are likely to survive. The GATT codes survived the collapse of the ITO in 1949, the one enduring part of its historic legacy. One could imagine the WTO functioning as a shadow of its former self with much of its legal regime in trade jurisprudence surviving its demise. (Picciotto, 2011)

#### *Likelihood*

On first glance this scenario is the most improbable, but with the collapse of the Doha Round, it is less remote than previously thought.

#### *Implications:*

The failure to conclude the Doha Round could be a wakeup call forcing member states and the WTO to take a serious look at the rules and operating procedures. The accumulation of political and market power in the global south, the WTO's hyper-legalism, and all-or-nothing process of bargaining have taken their toll on the world's

trading system. The system under siege is providing fewer tangible benefits to the developing world, which raises further doubts about the ability of the Round to bring greater coherence between trade and development. The angst of failure could also fan the flames of popular disgruntlement and trigger a much deeper legitimacy crisis of the multilateral trading system in the need of significant reform.

### UNILATERAL TRADE LIBERALIZATION OUTSIDE THE WTO: FEWER POLITICAL COSTS, MORE ECONOMIC BENEFITS

Conventional wisdom had long suggested that developing countries required the Doha Round to liberalize their economies. In this vein orthodox economists bet on the power of reciprocal bargaining to deliver an agreement. But negotiating environment has changed so much and it is no longer certain that the old model deal making is any longer a fruitful tool to close a deal. Many developing countries aren't waiting to cut their tariffs on the outcome of reciprocity based bargaining. According to the World Bank's *Global Economic Prospects* report in 2005, as much as two-thirds of the tariff cutting by a large

**Table 4 A Failed Round Doesn't Cost China or India Much;  
Less So for Brazil**

Country	<i>Calculations based on Largest Estimates Reported by CEPII Staff</i>		<i>Calculations based on Largest Estimates by World Bank Staff</i>	
	<i>Estimated gain (US \$ billions, 2005)</i>	<i>Days of economic growth needed to generate this gain</i>	<i>Estimated gain (US \$ billions, 2005)</i>	<i>Days of economic growth needed to generate this gain</i>
Brazil	1.77	.37	3.90	82
China	-0.61	n.a.	1.70	3
India	2.70	18	3.50	24

Source: Evenett, 2007

sample of developing countries was due to unilateral reforms. Cutting tariffs unilaterally had the advantage for many southern countries of substantial economic gains with no political costs. Simon Evenett (2007) calculated the costs of the Round's failure for China, India, and Brazil. China and India effectively lose a trifling three days GDP growth while Brazil loses one to three months growth. The accompanying table on real global income gains from the Doha Round dramatically illustrates how little is actually at stake in reciprocal multilateral trade negotiations for many countries.

Sandra Polaski, formerly with the Carnegie Endowment for International Peace, calculated that the original estimate of \$500 billion in benefits for developing countries has been closer to \$40–\$60 billion (Wise and Gallagher, 2006). She has employed six scenarios using a variety of possible outcomes from moderate

**Table 5 Global Real Income Gains from Trade Scenarios**

<i>Scenarios</i>	<i>Gain (billions of dollars)</i>	<i>Gain over Base Year GDP (Percent)</i>
(1) Doha Scenario for Agriculture	5.4	0.02
(2) Doha Scenario for Manufactures	53.1	0.17
(3) Central Doha Scenario	58.6	0.19
(4) Central Doha Scenario with 'Special Products for Developing Countries	57.7	0.18
(5) Modest Scenario for Manufactures	38.1	0.12
(6) Hong Kong Scenario	43.4	0.14
(7) Limited Scenario for Agriculture	2.9	0.009
(8) Scenario with Limited Agriculture and Ambitious Manufacturing	56.0	0.18
(9) Full Liberalization	168.1	0.53

Source: Polaski, 2006.

liberalization in agricultural trade to full liberalization to understand the gains better. She makes two fundamental points: first that the gains to global trade from a successful Doha Round are quite modest, and secondly, most of the gains go to the developed countries. Certainly, the actual proposals do not look very compelling as a set of negotiating principles for the global south (see Table 5: Global Real Income Gains from trade scenarios).

Many developing countries rely on tariffs for more than a quarter of their tax revenue, and for smaller countries, the number rises to over fifty percent. Wise and Gallagher estimate that ‘the total tariff losses under NAMA [in the Doha negotiations] could be \$63.5 billion, or almost ten times the projected gains’ (2002, 3). According to the WTO website, more than 100 bilateral deals are under negotiation around the world. It is no accident that a record number of countries are queuing up to negotiate regional trade deals for their own strategic ends.<sup>5</sup> In over a decade, a preferential system of bilateral deals has become a very common. The immediate effect has been to undermine the foundational principles of non-discrimination and national treatment—the core ideas behind the GATT culture of legalism (Dieter, 2009). For Steger ‘the non-discrimination principles enshrined in Articles I and III of the GATT ... have become more intrusive norms through their interpretation and application by GATT and WTO panels’ (Steger, 2002, 141).

### **Article XX: The Long Tortuous History**

Steger’s point, shared by many experts, is that there has been little room for a culture of adaptive legal exceptionalism to emerge. In its

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<sup>5</sup> In a curious turn of fate, preferential trading agreements (PTAs) ‘require rules of origin to establish the nationality of a product’ (Dieter 2009, 397). New non-tariff barriers of one kind or another proliferate. The WTO has been unable to minimize the negative effects of regional trade agreements; while the WTO membership been unable to reach agreement on the modality for changing the rules to minimize negative effects on third party members.

place, the legal culture of the WTO has not allowed broader kinds of policy goals to balance the drive for open markets (Picciotto, 2011). Why is this? One answer is that its legal culture has a systemic bias against linkage with non-trade issues. For example, the Appellate body of the WTO has given only limited reading to the exceptions contained in Article XX to protect public health, culture and the environment. Steger and others contends that Article XX has a 'long, torturous legal history' and the dispute settlement bodies have never clarified its scope or recognized its competence to bend the rules in order to equip the organization to face challenges of the new economic order (Steger, 2007).

Even the innovative decision in the *Asbestos Case* giving France the right to 'suspend' the national treatment principle against Canada's right to export asbestos, which is banned in every jurisdiction in Canada as a carcinogenic health hazard, did not clarify the grounds on which Article XX could be used by states to defend global public health needs (Drache et.al. 2001). Cerny's description of the restructuration process critically reminds us just how far the WTO is from recognizing the need for greater institutional coherence between the trade and development agenda. (Cerny, 2009) Joseph Stiglitz and others have made the compelling case that social justice has to be part of the WTO's tool kit, an idea reassuring to a political scientist but, so far, not part of the lexicon of trade law (Stiglitz, 2006).

Although Steger notes that the Appellate Body and some of the dispute bodies have gone so far as to include the goal of sustainability and development in their decisions, unsurprisingly, these decisions have not become part of the 'accepted theology or culture of the WTO' (Steger, 2007, 486): Instead, the best practice of open markets embedded in the WTO's legal regime remains powerful because it underlies the free trade model's ultimate intent—to move the world trading system towards a private model of wealth creation in which the state adopts a market-friendly de-regulatory culture (Kwa, 2007: Khor, 2009).

### **Knowledge Based Bargaining and Institutional Flexibility**

Many scholars and critics are attracted to the notion of institutional flexibility as the path to reform. However, the global south remains unconvinced of this, for the moment, particularly if such change would make the WTO more intrusive. Instead, they have channelled their energies into mastering the negotiating rules and learned to change the bargaining dynamics through knowledge-based bargaining to employ Diana Tussie's apt phrase. Coalitions are results-driven and groups such as the G20, G33, the Cotton Group, and the Core Group have used south-oriented public policy and political economy successfully to push back on the Singapore Issues that include competition policy and other very difficult issues (Tussie 2009).

Tussie's fundamental insight is that the global south has been technically empowered by knowledge-based bargaining (2009). The shift in policy focus from traditional border barriers to domestic, regulatory, and legal systems has hardened the resolve of the coalitions to reject their traditional role as rule takers as they were in the Uruguay Round. Instead, they have become 'refusniks' with respect to the need to offer reciprocal concessions where the gains of one sector are traded off against heightened import competition in another sector. This model of bargaining worked reasonably well between developed countries where governments used subsidies and non-tariff barriers to soften the costs of adjustment. However, when the negotiations directly involve the survival of hundreds of millions of peasants, as they do for the emerging economies of the global south, the concession model of trade bargaining breaks down. What is new in this round is the politicization of issues such as access to generic drugs and price supports for the millions of farmers who live on \$2 a day or less. Tussie persuasively argues that the free trade-protectionist binary influences the global south less than the pragmatics of protecting their domestic policy space.

The WTO membership has yet to address the call for new governance arrangements with explicit development provisions. In the last two decades, civil society and other critics have demanded greater openness and participation in decision making at the WTO (Deere-Birkbeck, 2009). While some progress has been made in this direction, it is likely that the calls for greater accountability are little more than rhetoric.

### **THE MILLION-DOLLAR QUESTION: WHAT DOES THE GLOBAL SOUTH WANT?**

For more than 80 years, the GATT has defined the legal culture of trade and investment, and its dispute mediation has given it legitimacy even as the multilateral system suffers from legislative gridlock (Sauvé, 2007). The multilateralism of the future is one in which 'developing countries will be able to flexibly assess and adopt various policy models, approaches, and mixes in support of their goals.' In her far-reaching paper, *Rethinking the Trading System*, Aileen Kwa (2007) outlines the guiding principles that would change the trading system and rebalance power between the big players in the global market. In this system, 'there must be checks and balances in the power of the biggest players.' Her idea of adopting human rights as the underlying rationale for the functioning of the trading system would radically alter multilateralism as we know it.

It is too early to say whether investing in human development and re-localizing and broadening the developmental prospects of national economies would stave off further decline of the world trade authority. The most important lesson to take from Kwa's analysis of the world trade organization is that opposition to aggressive market opening and the demand for deregulation of national economies is not a passing phenomenon. Far from it. From the outside, the committees still meet and members parse every word to the umpteenth draft. In the negotiation world of giving little and squeezing your trade rival the negotiation environment has dramatically altered in ways that

no one could predict. There can be no return to the club model of the Uruguay Round where the few decided for the many, and the WTO will continue to be stalemated because there is no effective decision-making mechanism available to complete the Doha Round and broaden its non-trade agenda. Therefore, the great issues of the moment—human rights, the environment, poverty eradication—will not figure into its governance lexicon.

### **The Bias of Membership Organizations: An Innate Conservatism?**

This paper has argued that the dynamics of power and the way the WTO conducts its business have changed beyond recognition. Still the riddle inside the paradox is that membership organizations, like the WTO, are strongly biased towards the status quo and all of its defects and shortcomings. Frequently global membership organizations are conservative, top-down organizations deeply divided and fragmented by competing national interests. Still countries have learned from the past and are not ready for a trade war with mile high tariffs. So despite a feeble recovery in leading industrial economies, the old demon of classical protectionism is largely confined to the margins where it belongs (Drache, 2010).

In terms of what is next for the WTO, a trade pause is the most likely scenario. We have also insisted that international organizations like the WTO need to be able to evolve and adapt to structural change whether incrementally or by some near-death experience. If they cannot do so, then global governance institutions lose their way and their influence on the global economy radically declines. Scholars and experts have compiled a very long list of the most egregious institutional boulders that have pushed the WTO off course. There is no epistemic consensus on which of these has had the most damaging effect but these explanations are worth recalling just briefly. These include: the one-size-fits-all free trade model (Rodrik, 2002), the divisiveness of intellectual property rights and agriculture as deal

breakers (Ismail 2009), the power dynamics of club versus coalition bargaining dynamics (Narlikar 2010), the absence of policy coherence (Blouin 2007), the paradigm shift in the climate of ideas (Ostry 2002), the 'rise of the rest' hypothesis (Zakaria 2008), mountain-sized institutional rigidities (Matoo and Subramanian 2008), EU-US power rivalry (diverse authors), troubled multilateralism (Bhagwati 2005; Stiglitz 2006), a declining interest in trade liberalization (the new Obama administration), pushy new actors with transnational social networks (Kwa 2007), the pull of regionalism (diverse experts), weak problem-solving capacity (Picciotto 2007), the uncertainty of looming regime change (Hefler, 2004), institutional over-reach without reform of the WTO legal culture (Khor 2009), the need for new institutional structures and practices (Steger, 2007) and the success story of new policy spaces and second best institutions (Rodrik, 2007). The only thread of a consensus among such divergent scholars is that they are unanimous on one point: the WTO is a troubled institution facing the prospects of decline.

A decade ago, the WTO was one of the pole stars of the triumphant globalization movement; regarded by critics and supporters alike as the most powerful global governance institution because of its legal muscle. Since the moral victory of the legalists has imploded, the legalization of global politics is itself on trial. The shifting power of geography encourages countries to look for new frames in which to pursue their strategic interests. Is it far-fetched to suppose that Keynes and Prebisch have much more to teach us about the institutions and norms of global governance than the uncoordinated market capitalism of Hayek and Friedman (Skidelsky, 2009)? The transition from the club dominated by the US and EU to the coalition model of trade governance of the many is the clearest indication of the slow decline in the status and effectiveness of this world trade organization. In the future, it will likely have a smaller institutional reach and less legal clout although the legal adjudication function will operate in much the same way as it has for technocratic efficiency-based reasons.

Pessimists predict a hard landing for the Doha Round reflecting the new power relations in Geneva and beyond. Optimists envisage a different kind of global trade institution, one in the mirror image of the emergent balance of power taking shape in this highly focused global governance institution. Both may be right for reasons of timing and sequencing. Deadlock is a state of impasse where in modern organizational theory neither side has the authority and sufficient clout to impose its will on the other. As the multilateral trading system continues to be without coherent direction, trade negotiations are a second order difficulty in a global economy hard pressed to sustain a strong recovery.

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