

Small developing economies and the multilateral trading system:



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A Caribbean perspective

Small developing economies are often constrained in participating in the negotiation and regulation of multilateral trading rules due to severe cost and resource limitations. This article argues that, despite the costs and difficulties, small states must remain engaged in the multilateral trading system in order to ensure that their specialised commercial interests are recognised and to protect their rights. Umbrella entities like the Caribbean Regional Negotiating Machinery (CRNM) provide a means of maximising the influence of small states in an international forum such as the World Trade Organization.

Small developing countries often find the costs of participating in the negotiation and adjudication of rules in the multilateral trading system very onerous. Indeed, many governments in small or developing countries regard the cost as prohibitive. This has elicited three responses. First, and regrettably, countries drop out of the process, except for a few high-level meetings. Second, their participation may become heavily dependent on funding from multilateral financial institutions and bilateral donor agencies in developed countries, whose interests, ironically, are often diametrically opposed to those of the beneficiary countries. Third, and all too infrequently, they combine their resources and form common entities, for example the Caribbean Regional Negotiating Machinery (CRNM), which serves 15 Caribbean countries. The CRNM fulfils the functions of technical advice, monitoring, analysing, reporting, co-ordinating common positions and negotiating (where appropriate) on behalf of member states.

Often, trade ministries are limited in participating in trade negotiations less by constraints on fiscal expenditure than by the failure of cabinet colleagues, in particular finance ministers, to fully appreciate the repercussions that can result from changes in the rules and provisions of the multilateral trade system. The overarching rationale for trade negotiations is liberalisation, which obviously has implications for fiscal revenue, both directly through tariff reductions, and as a

consequence of a wider adjustment process.

Despite the costs and difficulties involved in participating in multilateral trade negotiations, there are five compelling reasons why small states must remain engaged in the multilateral trading system and participate as fully as possible in the current and future negotiations in the World Trade Organization (WTO):

- The importance of international trade to small economies;
- Their vulnerability to external developments;
- The distinct and sometimes unique nature of their interests;
- The enhancement of negotiating leverage; and
- Protection of their rights.

Importance of international trade

The highly open structure of small developing economies means that international trade is large in relation to domestic production, reflected in a high trade/GDP ratio. Small developing economies exhibit more reliance on international trade than large and developed economies. Imports are of critical importance in production and consumption, both quantitatively and qualitatively. Growth is therefore extremely dependent on imports and consequently on import capacity, which is in turn a function of the quantum of foreign exchange inflows. These inflows are determined by export

earnings and net capital inflows, i.e. foreign investment, development assistance and loans.

Small developing economies have greater need for access to external markets than large economies because the small size of their domestic markets and limited resource base cannot sustain economic growth. Unfavourable external developments in either imports or exports, including changes in trade arrangements, can lead to a collapse in export earnings or a surge in

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economy-wide prices, precipitating prolonged periods of severe contraction in the wider economy.

Vulnerability to external developments

Small developing countries are especially vulnerable to external developments because they are characterised by a high degree of openness, compounded by a concentration of exports on a very small number of products which in many instances are primary products and/or agricultural commodities that are exported with minimal processing. This vulnerability becomes acute when product concentration is compounded by exporting to a single or a limited number of overseas markets. A dramatic example is the implosion of the economy of Dominica, which depended solely on exports of bananas to the UK until the banana regime of the European Union was changed.

Small developing economies must therefore be a part of trade negotiations in order to protect current trade privileges and ensure that new rules adequately take account of their particular circumstances. Exposure to external events will increase as trade liberalisation proceeds and globalisation intensifies the inter-connectedness of world economies.

Given the importance of trade, their vulnerability and the ever-expanding coverage of trade agreements, small developing economies cannot afford to ignore the various trade negotiations. The challenge is to mobilise sufficient human and financial resources to adequately cover the plethora of trade negotiations being conducted bilaterally, regionally and multilaterally. The alternative of inadequate or no participation would cause serious adverse economic impact.

Distinctness of interests

Small developing economies are a subset of the developing countries economic category. Their concerns and objectives are distinct, and in some cases unique, differing from other developing economies. They must participate in trade negotiations in order to ensure that their particular specialised interests are recognised and accorded appropriate treatment. The uniqueness of the agenda of small developing economies is highlighted by the fact that much of the resistance to special and differential (S&D) treatment for small developing

economies, beyond that allowed to developing and least developed countries, has come from other developing countries.

Special and differential treatment

Currently small developing economies are struggling to retain existing preferences in key markets and to establish the principle that small size is an additional constraint on development and should be accorded S&D

treatment. This challenge is illustrated by the situation confronting CARICOM countries. These states enjoy preferential market access for trade in goods with Canada through Caribcan, with the European Union under the Cotonou Agreement and with the US by the Caribbean Basin Economic Recovery Act (CBERA) and associated legislation. But all three trading partners have signalled their intention to dismantle these preferential arrangements in favour of reciprocity. At the same time, the CARICOM countries, along with other small countries in the Pacific, Indian Ocean and Africa, have led the advocacy for S&D for small developing economies in the Free Trade Area of the Americas (FTAA) and in the World Trade Organization. The Declaration of the WTO Ministerial meeting in Doha established a work programme on small economies.

In the Doha Development Agenda and in other ongoing trade negotiations such as the FTAA, and to some extent the ACP-EU context, there is an increasing recognition that small states or 'smaller economies' have unique problems due to structural and permanent characteristics, which require a special dispensation in the international trade regime. Research on the concept of small, vulnerable economies has significantly advanced over the past decade and there is increasing scope for making a special case for them in global and regional trade rules. The FTAA process has acknowledged the need to reflect 'differences in size of economies and levels of development' as a basic principle in the negotiations. The negotiations between the EU and ACP countries, although not as overt regarding the special importance attached to small economies, have nonetheless signalled an intention to make the Economic Partnership Agreements (EPAs) development-focused and to include a fundamental principle ensuring that the vulnerability of land-locked and island states shall be taken into account. But in order to ensure that these considerations are firmly embedded in rules, which are legally binding commitments, it is essential for small states to remain engaged in the process and maintain a consistent approach across all negotiating forums.

Enhancement of negotiating leverage

A rules-based regime for the conduct of international trade and the resolution of disputes is of more importance to small countries than to large ones because

it is through this type of arrangement that small states can increase their limited leverage through consensus decision-making and by the use of strategic alliances. Multilateral negotiations allow small countries to exercise countervailing power against the predominating power of large countries such as the US, the European Union, Brazil and India. Large countries, particularly the highly developed ones, wield near-dominant influence due to their market size, share of world trade and political power. The mere threat of trade action by a large country can disrupt global markets, impede market access and unsettle production and investment. Small countries exercise limited influence in trade negotiations because their small national markets and insignificant share of world trade provide little or no leverage in bargaining. Their best prospect for influencing trade

have the enforcement of their rights and privileges by compelling other countries to adhere to multilateral rules. This result could not have been achieved in a bilateral engagement.

Fairness and participation

Despite Antigua and Barbuda's success, small economies have limited administrative capacity and human resources, which make it difficult for them to use the provisions of the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU) in the WTO. The cost of participating in WTO dispute settlement proceedings is very high. Small economies have very limited capacity to either initiate or defend cases. Current negotiations in the WTO on improvement of the DSM are seeking to address these institutional issues. It is therefore important for

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policy is a rules-based multilateral trading system. In this context, raw power and economic size are subsumed in a transparent, democratic decision-making process based on consensus.

By establishing clear disciplines applicable to all WTO member states, multilateral trade rules prevent arbitrary behaviour by governments and ensure predictability in trade relations. It also curtails the potential abuse that can occur between countries vastly different in size, level of development and power. The rights of small states are most likely to be protected from the hegemony and pressure that larger and/or more powerful countries can exert by participating in multilateral institutions such as the WTO.

Protection of rights

Attaining rights in a multilateral trade system is only one aspect and has to be complemented by ensuring that these rights are respected, or at least not disregarded. A rules-based multilateral trade system provides the best rights protection for small states. Small states can have recourse to the WTO dispute settlement mechanism (DSM) to vindicate their rights, free of the power disparity that would operate in a bilateral situation.

Antigua and Barbuda provides an example. With a population of only 90,000, tourism and financial services account for approximately 92% of GDP and more than 90% of exports. Tiny Antigua took the mighty US to the WTO's DSM in a dispute over Internet gaming and won. A WTO Panel ruled in March 2004 that Antigua and Barbuda's right to conduct cross-border gambling and betting services trade over the Internet was being violated by US measures to restrict such activities. This ruling, when officially released, will demonstrate the importance of multilateral trade rules to small countries. Not only can the smallest of trading partners have their grievances adjudicated in the WTO, but they can also

CARICOM states to participate actively in these discussions to ensure that their interests are reflected in any changes to the current dispute resolution regime. Similarly, Costa Rica successfully brought a claim against the US regarding the latter's commitment under the Agreement on Textiles and Clothing (ATC). The WTO Panel ruled that the US had violated its obligations by imposing a restriction on Costa Rican exports of underwear without demonstrating that this was the cause of serious damage or threat thereof to the US domestic industry.

The decision-making processes in the WTO, while far from perfect, are in stark contrast to other less representative and transparent bodies. This is graphically illustrated by the Organisation for Economic Co-operation and Development (OECD), whose Financial Action Task Force (FATF) created plurilateral standards and regulations that are being applied internationally. These plurilateral standards were formulated without input from all the countries affected by the applications of these standards. Several of these small developing economies, with significant export-oriented offshore financial services sectors, were never consulted. They were faced with implementing arbitrarily promulgated complex external regulations in order to continue operating and to avoid the imposition of punitive sanctions by large developed countries. Antigua and

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Barbuda witnessed the closing of 35 licensed banks from 1999 to the present as a result of actions taken to enforce regulatory and legal standards devised by the OECD.

Small states in the WTO, including some from CARICOM, tabled a proposal to the WTO's Committee on Financial Services that aimed at ensuring greater fairness and participation by all in the process of setting international standards for the regulation of financial services. The proposal attempted to minimise the implications of financial standards that are not formulated by all countries. The reaction to the proposal in the WTO was mixed, with many small developing countries voicing support for it, and developed countries arguing for further discussion on certain issues. The proposal focused attention on the fact that small states would incur disproportionate administrative costs in implementing and complying with new financial and banking standards, that they had no part in formulating. However, since its initial introduction in the GATS negotiations, the proposal has fallen by the wayside due to non-representation by Antigua and Barbuda at the subsequent meetings of the Committee on Financial Services.

Conclusion

It is a grave error to believe that small developing economies gain little benefit from a multilateral trading system and that their participation in negotiations will not significantly influence the outcome. These countries have no alternative but to be involved, given the paramount importance of international trade to their economies. The instances of the vindication of their rights demonstrate that their interests can be protected under the aegis of the multilateral trade system. Therefore, small developing economies, despite the costs and difficulties involved, must participate in international trade negotiations to pursue their commercial interests and protect their existing rights. Furthermore the prospects of securing the protection of their rights in the WTO are better than the potential to do so in regional and bilateral arrangements. Absence from the negotiations would mean that small developing economies could not influence the content of the rules that impact on their vital trade relations, nor ensure that their rights are fully respected.

Dr. Richard L. Bernal was educated at the University of the West Indies (UWI), University of Pennsylvania, and Johns Hopkins University. He holds the degrees of BSc, MA, PhD. (Economics), and MIPP (International Public Policy). He is currently Director-General of the Caribbean Regional Negotiating Machinery and previously served as Jamaica's Ambassador to the US and OAS. He has been CEO of a commercial bank, served in the Central Bank of Jamaica and taught Economics at the UWI. He is also Honorary Professor, Sir Arthur Lewis Institute of Social and Economic Studies, University of the West Indies, Mona, Jamaica. Dr. Bernal has published over 100 articles in scholarly journals, books, and monographs and opinion pieces in the *Wall Street Journal* and the *Washington Post*.

Formally established on April 1, 1997, the **CRNM** received its mandate from the Conference of Heads of Government of CARICOM. The CRNM works to develop a cohesive and effective framework for the coordination and management of the Caribbean Region's negotiating resources and expertise. Its mission is to assist member states in maximising the benefits of participation in global trade negotiations by providing sound, high quality advice, facilitating the generation of national positions, co-ordinating the formulation of a unified strategy for the region and undertaking/leading negotiations where appropriate.

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