India and the Global Trading System by C. Fred Bergsten

The year 1999 is likely to be a watershed year for the world trading system. The Ministerial Conference of the World Trade Organization in Seattle in November/December hopes to chart a course for global trade policy in the early part of the 21st century. The European Union, Japan, the United States and Canada-the Quadrilateral Group that functions as an informal steering committee for the system-and many other countries have already agreed to use that occasion to launch a Millennium Round of multilateral negotiations to liberalize trade further and write new rules to govern additional types of economic transactions among nations.

At the same time, a substantial backlash against globalization is clearly gathering force in some quarters. If successful, that backlash could both derail the effort to commence new international liberalization initiatives and promote the creation of new protectionist pressures around the world. Some of the backlash can be found in developing countries, including India. Surprisingly, however, very little reaction against trade liberalization has surfaced in the East Asian countries that have been hit hardest by the global financial crisis (and even their pullback from full participation in global financial markets has been quite limited). The most worrisome tendencies are in fact emerging in the United States, despite the continued strong performance of its economy, and must be of deep concern to all trading countries because of America's pivotal role in both world trade and the functioning of the global trading system.

India has a strong national interest in the outcome of these global economic debates. The sharp expansion in India's trade and global market share after the reforms of 1991, which has been promoted by the international liberalization agreed in the Uruguay Round, contributed importantly to the improved growth performance of recent years. However, export growth has slowed recently and India has only begun to exploit its potential international economic role. With proper policies and a supportive international climate, India could become the next "miracle economy". Moreover, nothing could promote India's quest for enhanced international recognition more than full realization of its enormous capacity for economic dynamism and positive leadership in the global economic debate.

Let me digress for a moment on this crucial question of India's world role. In the past - Cold War world, it is clear that the most effective path to global respect and clout is economic success. Attainment of nuclear status has very little impact in this respect, as India has seen over the past year. The sharp increase in China's world role over the past two decades stems from its dynamic economic growth rather than its nuclear program (or other military prowess). Economic progress should of course bring its own reward but India would also derive substantial political and even security benefits from achieving the kind of rapid development for which it clearly has potential.

Global economic leadership and attention have rotated among a succession of "newcomers" throughout the postwar period. Japan emerged in the 1960s. Some OPEC countries achieved prominence in the 1970s. China and the newly industrial countries of East Asia were the stars of the 1980s. South-East Asia attracted enormous attention in the 1990s (before its crisis erupted in 1997). India could certainly play a similar role in the early part of the 21st century.

As the world's fifth largest economy (with exchange rates converted at purchasing power parity), India can certainly play such a leadership role. If it adopts a positive and constructive role toward the new round of trade negotiations, it can help shape both the agenda of those talks and the pace at which they proceed. India clearly has a number of national interests that it should pursue vigorously in the Millennium Round including lower tariffs on textile, apparel and some agricultural products in the industrial countries; tighter disciplines on their use of anti-dumping duties and other protective procedures; liberalization of movement of natural persons, where India has a strong comparative advantage; and new arrangements to encourage inflows of foreign direct investment in ways that ensure that India derives its fair share of the benefits.

We are thankfully a long way from 1986, when India tried to block the launching of the Uruguay Round (from which it subsequently derived considerable benefit). I would hope that India will pursue a positive trade agenda into the early 21st century rather than try to delay or truncate the new negotiations, or seek reincarnation of outmoded devices like "special and differential treatment" for developing countries that are as discredited as the import substitution policies thatIndia itself pursued in earlier decades. The world trading system cannot marginalize India-but India could marginalize itself if it fails to take advantage of the opportunities that will present themselves over the years ahead.

As the world's largest democracies, the United States and India must face openly, and deal effectively with, the adjustment problems that accompany trade liberalization. Our two countries should work closely together in this effort to construct a global trading system that promotes both growth and equity in industrial and developing countries alike.

In addressing these issues, and devising a strategy for the Millennium Round and beyond, it is first essential to sketch the pattern of global trade policy that has been evolving over the past couple of decades. I will then analyze the contemporary threats to the trading system, with considerable emphasis on the trade policy of the United States, and propose a strategy to avoid a renewed slide toward protectionism around the world.

Finally, I will attempt to draw out several implications for India and other developing nations, proposing that they adopt a proactive role in both moving the global system in a constructive direction and pursuing their own national interests within that context.

The Trend toward Free Trade

A large part of the world has eliminated all barriers to trade or is in the process of doing so. The fifteen members of the European Union have created a "single internal market". Australia and New Zealand have completed their free trade area. Several large groupings are enroute to a similar outcome: the North American Free Trade Agreement (Canada, Mexico, United States), Mercosur (Argentina, Brazil, Paraguay, Uruguay) and the ASEAN Free Trade Agreement (Brunei, Indonesia, Malaysia, Philippines, Singapore, Thailand and now Vietnam).

In addition, a series of newer groupings have pledged to abolish all impediments to their international trade in the coming years. The European Union and the Mediterranean countries (EUROMED) have committed themselves to free trade by 2010. The 34 democracies of the Western Hemisphere agreed at their Miami

Summit in December 1994 to work out a Free Trade Area of the Americas (FTAA) by 2005 and negotiations to that end began last spring. The 21 members of the Asia Pacific Economic Cooperation (APEC) forum - which account for half of world output and include the three largest national economies (United States, Japan, China) - decided via their Bogor Declaration of November 1994 to establish free trade and investment in the region by 2010 for their higher income members, that make up 85 per cent of their commerce, and by 2020 for the rest.

Over 60 per cent of international commerce now takes place within these existing or planned free trade regimes (Table 1). This share is rising rapidly, both because of the creation of new arrangements and because trade expands more quickly under such conditions. The question thus arises: why not eliminate all trade barriers throughout the world? Why not launch a movement toward global free trade at the upcoming WTO Ministerial Conference in Seattle?

Competitive Liberalization

In answering these questions, it is first essential to understand why so many countries, in so many different parts of the world, with such different economic systems, at such different stages of development, have all headed in the same direction. There are of course different national circumstances which explain the detailed strategies and timing of the individual initiatives. The overarching force, however, has been the process of competitive liberalization.

The rapid increase of global interdependence has induced virtually all countries, whatever their prior policies or philosophies, to liberalize their trade (and usually investment) regimes. Economic success in today's world requires countries to compete aggressively for the footloose international investment that goes far to determine the distribution of global production and thus jobs, profits and technology.[1] Most countries offer direct incentives to foreign investors but an open trade and investment regime is even more critical for this purpose. Mexico was traditionally a very closed economy (and was extremely wary of embracing its northern neighbor), for example, but decided to liberalize and propose NAFTA when it became convinced that doing so was essential to avoid losing out in the global competition for capital.

Moreover, success in today's global economy requires countries to compete effectively in international markets rather than simply at home. This is true no matter how large the domestic market: some of the world's most self-contained economies including Brazil, China and perhaps most notably the United States - which maintained extensive quotas on autos, machine tools, steel and numerous other products less than fifteen years ago - have joined the competitive liberalization race.[2]

Competitive liberalization is pursued by countries that until recently had deeply entrenched protectionist traditions. France is a dramatic case in point. So is virtually all of Latin America, which embraced import substitution doctrines as recently as two decades ago. The most stunning reversal of all comes from many of the former command economies of the Communist world, ranging from China through Central Europe to parts of the former Soviet Union and now Vietnam.

An intellectual and ideological sea-change underlies this historic development. Import-substitution and even autarkic models of development and national economic strategy were reasonably respectable into the 1960s and even the 1970s. But their shortcomings were then exposed, including by the third world debt crisis of the 1980s, and replaced by a new consensus of "outward orientation".

The Asian, now global, financial crisis has interrupted neither these policy actions nor the intellectual trends. To be sure, there has been some East Asian reaction against short-term capital flows (though even Malaysia liberalized its treatment of foreign direct investment, including short-term transactions within multinational firms, at the same time it imposed new barriers to hot-money flows). But there has been very little recourse to new trade barriers. Korea and Indonesia have in fact reduced their barriers sharply. The ASEAN countries have decided to accelerate the timetable for achieving free trade under their ASEAN Free Trade Agreement (AFTA).

This change in basic thinking does not, however, explain the onset of regional or other international trade arrangements. Why didn't the new attitude simply produce a spate of unilateral trade liberalization, which textbooks recommend as the most direct route to maximizing trade benefits for an individual country? The answer lies in the politics of trade reform.

The Political Economy of Trade reform

To be sure, some unilateral liberalization has taken place. This has been especially true in East Asia and Latin America. Most of the 100 or so instances of "unilateral liberalization" over the past couple of decades were adopted within the context of IMF or (especially) World Bank adjustment programs, however, suggesting that "reciprocity" in the form of foreign financial assistance played an important role in those decisions.

In most cases, domestic political opposition blocked countries from abolishing their traditional barriers. Entrenched interests fought hard, and frequently with prolonged success, to maintain their protected positions. The politics of economic reform were difficult and contentious in virtually every case.[3]

The standard strategy for achieving trade reform was to mobilize enough pro-trade interests to overcome the forces that resisted further market opening. These included beneficiaries of imports such as consumers and industrial users of imported inputs.[4] However, such groups are rarely organized and their gains from liberalization are both modest and widely diffused. Hence they typically produce little political counterweight against those who would be adversely affected by increased foreign competition.

To overcome such opposition, it became necessary to appeal to exporters and others who gain directly from the opening of markets abroad. The political economy of trade liberalization in individual countries thus rested heavily on parallel liberalization in partner countries. The most assured technique for achieving such parallel action was to insist on reciprocity, through the negotiation of trade agreements with enough existing or potential markets to tip the internal balance in favor of the desired liberalization. The United States finally agreed to get rid of its textile quotas by negotiating foreign concessions from the rest of the world, in the Uruguay Round at the GATT, on intellectual property rights and agricultural distortions. Through that same negotiation, Japan and Korea began to open their rice markets by appealing to the export interests of their

(especially high-tech) manufacturers. It is not only respectable but essential, for even the largest economies in the world-especially when they are also effectively functioning democracies-to use external pressures for liberalization to overcome internal political resistance; India's leaders can invoke similar strategies to pursue the positive trade agenda that will be so helpful to the country as a whole.

Negotiated liberalization thus turns out to be far more feasible than unilateral liberalization. The key becomes a country's ability to persuade its foreign partners to proceed in tandem with it. Large trading entities, such as the United States and the European Union, obviously have the most leverage in this context because of the attraction to others of the opening of their markets.

Another key variable is the stage of liberalization at which a country finds itself. Initial reductions of very high tariffs can be relatively easy because they put few dents in the real level of protection and thus can often be implemented unilaterally. But most countries have found that they must apply the traditional political economy approach to engineer the later and most difficult phases of the process.

Regional vs. Global Liberalization

In seeking reciprocal liberalization, countries could turn either to their respective geographic region or to the global trading system as a whole. The global approach is fundamentally superior because it maximizes the number of foreign markets involved and avoids the economic distortions (and political risks) of discrimination among trading partners. Indeed, the succession of GATT "rounds" throughout the postwar period has made a major contribution to the freeing of global trade.

As the urgency of competitive liberalization accelerated over the last decade or so, however, the regional approach has played an increasingly prominent role. It has turned out to be less time-consuming and less complicated to work out mutually agreeable arrangements with a few neighbors than with the full membership of well over 100 countries in the WTO. Moreover, regional groupings are demonstrably willing to proceed much more boldly: many of them have decided to adopt totally free trade, as noted above, whereas none of the global conclaves to date has even considered such an ambitious goal. The rapid growth in the membership of the WTO, whose predecessor GATT had fewer than 50 members, through the first several postwar negotiating "rounds", has further complicated multilateral initiatives in the WTO and thus added to countries' propensities to pursue the regional alternative.

Desires to overcome traditional political rivalries have also been a driving force in the success of several of the regional economic arrangements. The cardinal goal of the European Union was to end the historic hostility between France and Germany. Mercosur sought to end the arms race, including its nuclear dimension, between Argentina and Brazil. A successful APEC would reduce the risk of intra-Asian and trans-Pacific conflicts, which have been so prevalent over the past century. A successful South Asian FTA would presumably help ease tensions between India and Pakistan. Regional trade arrangements are thus often motivated by priority national security concerns. This is another reason why they often move more quickly and more boldly.

Let me again digress to a set of broader political questions that are of central importance to India: its relationship with Pakistan. Why not follow up the inauguration of bus diplomacy by initiating a strategy of economic integration on the subcontinent to overcome the hostility that has such pervasive effects on your economy as well as your security? France and Germany fought three wars in 75 years and their nationalism was certainly as virulent as the cleavages that have triggered three wars here in the past 50 years. They decided to reverse course by pursuing economic integration, which over 50 years has now even led to a common currency and rendered conflict impossible between them.

Brazil and Argentina were also historic antagonists, and began developing rival nuclear programs in the 1970s that persisted into the early 1990s. Recognizing the enormous danger they were creating, they too then reversed course by choosing a strategy of economic integration. Their Mercosur is less tested than the European Union but, to date, has succeeded well. It has already permitted the countries to abandon their nuclear programs and thus end the huge risks they faced only a few years ago.

In both cases, traditional foes adopted economic policy tools to achieve their overriding national security and political objectives. In both cases, smaller neighboring countries participated on the integration strategy so both the economic and political benefits were extended. Why cannot India and Pakistan, along with the rest of South Asia, adopt such a course and thereby transform the security situation as has previously occurred in Western Europe and South America?

Reverting to my trade policy theme, much of the political economy of competitive liberalization in recent years has in fact played itself out in the dynamic interaction between regional and global initiatives to reduce trade barriers. The United States initiated the Kennedy Round in the 1960s to counter the discrimination inherent in the creation of the European Common Market (as well as for broad foreign policy reasons) and the Tokyo Round in the 1970s to counter the additional discrimination from the Community's expansion to include the United Kingdom. The Europeans cooperated in both ventures and thus enabled the regional and global efforts to "ratchet up" the scope and pace of liberalization.

The positive interaction between the two strategies accelerated sharply in the 1980s and 1990s as competitive liberalization became the norm and countries searched for tactics to obtain the needed domestic support. The United States reversed its traditional aversion to regionalism by embracing free trade agreements with Israel and Canada after the European Community blocked the launch of new negotiations in the GATT-to which the EC responded by dropping its veto and permitting the Uruguay Round to begin. When the Round faltered in the late 1980s, the three North American countries launched NAFTA and the Asians initiated APEC.[5] When the Round almost failed to meet its final deadline in December 1993, APEC's initial summit in Seattle in November 1993 induced the Community to finally agree because, according to one top European negotiator, it "demonstrated that you had an alternative and we did not". The regional initiatives also reinforced each other: APEC's Bogor Declaration was instrumental in galvanizing the Miami Summit, a few weeks later, to commit to free trade by a date certain in the Americas.

This positive interaction also extends to the subregional level. President Bush's offer in 1990 to negotiate free trade pacts throughout the Western Hemisphere led to an explosion of bilateral and plurilateral agreements across South and Central America as countries sought to prepare themselves to qualify for free trade with

North America. In Asia, AFTA has accelerated its timetable and substantially broadened its coverage to stay ahead of APEC. AFTA and Australia-New Zealand have discussed possible linkages between the groups.

Hence regional and global liberalization initiatives have been mutually reinforcing throughout the past three decades or more. The fears of some observers that regionalism would derail globalism have been demonstrably overcome.

The Threats to the Trading System

But determined leadership has been required to avoid conflicts between regionalism and globalism. Doing so has also required the maintenance of effective global trade rules to provide a framework that would deter conflict between the regional arrangements, including rules that apply to the arrangements themselves, and an institution to enforce them. Even so, there have been some close calls - especially when the global system faltered. The new regional arrangements spawned by the missed deadlines of the Uruguay Round were intended to serve as alternatives to the global regime if needed. An ultimate failure of the Round, which almost occurred, would have discredited the entire global system and raised a real spectre of competing blocs.

Moreover, the European Union frequently seems to focus so heavily on its regional agenda that it forgets its global responsibilities. The United States is sometimes viewed as preoccupied with NAFTA or APEC. By joining East Asia and North America, APEC has eliminated any possibility of the evolution of the three-bloc world that was so widely-and rightly-feared a few years ago but a failure to work out accommodations with Europe could instead create a two-bloc world that would convey substantial dangers as well. South America might decide to halt its liberalization once Mercosur has consolidated, and Brazil might be happy to leave its new leadership of that region undisturbed for at least a while. Countries not participating in any of the major regional pacts, such as India, correctly see a risk of increasing discrimination against them if regionalism were to become the dominant form of trade liberalization. There is a constant need to keep the global-regional interaction on a supportive course.

This is one key reason why a new initiative is now required to consolidate the regional liberalization initiatives into an agreement to achieve global free trade in the early 21st century.

There are other risks to the continued progress of competitive liberalization that need to be met by a new global initiative. The most threatening of these challenges do not arise in the countries that have rejected openness most strongly in the recent past - some developing countries and the former command economies - although some of them do harbor lingering doubts that could again assume ascendance. Paradoxically, the strongest pressures to reverse the liberal course can be found in the countries that created, nurtured and championed the postwar order: the United States and the European Union.

Two structural changes dominate the evolution of the American economy over the past generation. One is globalization: the share of trade has almost tripled in a generation and now exceeds the same share in the European Union as a group and (especially) in Japan. The other is the stagnation of real incomes and a regressive shift in income distribution: the United States has created tens of millions of new jobs but the

average real wage, despite a pickup in the last couple of years,is still lower today than a generation ago and only the top 20 per cent of the population is unambiguously better off.

The central question for present purposes is the degree of casualty between the two phenomena.

Globalization, like any dynamic economic change, of course creates losers as well as winners despite its net positive effects on the economy, and virtually all economists agree that it has contributed to some of the problems cited. The majority believes the relationship accounts for only 10-20 per cent of the problem and that a retreat into protectionism would make it worse.[6] American politics frequently reflect this tension. Only the extremists of both right and left have launched frontal attacks on the bipartisan trade policies of the past 60 years and all their nationwide campaigns have been decisively rejected. But organized labor and its allies have succeeded in bringing US trade policy to a stalemate over the past four years, persuading the Congress to deny the President any new trade-negotiating authority despite the strength of the American economy. Labor and its allies remain implacably opposed to any new trade (or international investment) liberalization, and are indeed seeking new protection in steel (and perhaps other sectors in the near future). President Clinton and the Democrats are deeply indebted to labor for delivering the votes and money that produced their surprise "victory" in the 1998 Congressional elections. The President has indicated his intention to seek new negotiating authority from the Congress but, as the United States now enters its next Presidential election cycle with the Democrats hoping both to retain the White House and regain control of the Congress, he-and especially the Vice President in light of his desire to be the next occupant of the White House-may not be inclined to resist the unions. Especially when cyclically adjusted, US trade policy is in serious trouble.

Moreover, the US trade and current account deficits are likely to exceed $300 billion in 1999 and continue growing for the foreseeable future. These numbers are double the previous record of the middle 1980s and are approaching those deficits' record share of the total economy. During that previous episode, the dollar dropped by over 50 percent against the other key currencies and the Congress almost passed massively protectionist trade legislation (and did substantially tighten the anti-dumping statutes and enact the infamous "Super 301" provision). Any significant slowdown in the US economy and concomitant rise in unemployment could turn US trade policy in a protectionist direction.

The situation in Europe is fundamentally similar if quite different in its details. Europe's chief economic problem is high unemployment, which has risen from 2-3 per cent a generation ago to above 10 per cent now-from well below the American norm to more than twice as high. But average wages and incomes in Europe have risen substantially over this period, in sharp contrast to their stagnation in the United States.

These two great industrial areas have thus made very different social choices. By limiting its social safety net, the United States essentially forces its displaced workers to find new jobs even at a lower wage. Because American firms are able to fire workers, they are willing to hire new workers. In essence, the United States prices its labor competitively and thus maintains full employment. Europe has by contrast become a generous welfare state with extremely rigid labor laws, discouraging new hires from both the supply and demand sides while maintaining social peace through governmental transfers of a large share of its higher incomes to the poor.

The bottom line is that neither Europe nor the United States has been able to generate a steady increase in the number of well paying jobs. Europe has rising incomes but high unemployment. America has low unemployment but flat incomes. Perceptions and politicians in both could come to treat trade as a major source of the problem, or even the major source of the problem, and thus pave the way for a massive reversal of global liberalization.

The Asian giants, Japan and China, also pose major threats to the continued openness of the trading system. The political economy of liberalization succeeds in winning domestic support, even in a country as large as the United States, only when its major foreign markets (especially if they are also its toughest competitors) are seen as joining the process and contributing their fair shares to the process. Japan has grudgingly participated in all the GATT rounds but access to its markets remains extremely truncated (and it single-handedly blocked APEC's latest liberalization initiative).[7] China has not yet committed to the minimum reforms necessary to join the WTO. Protectionists in other countries, with some justification, will use the reluctance of Japan and China to liberalize to oppose further reduction of their own nations' barriers.

Restarting the Bicyle

Why do all these threats to future liberalization matter? International trade and investment continue to flourish, if at a modestly slower pace due to the financial crisis. Does business simply need to be assured that no new impediments will be erected?

The problem with this "stand pat" scenario is its instability. The history of trade policy teaches forcefully that failure to move steadily forward toward liberalization condemns the trading system to tip over in the face of protectionist pressures-the "bicycle theory". For example, protectionism scored major successes, especially in the United States, during the prolonged periods when the GATT became moribund immediately after the successful conclusion of the Kennedy Round in the late 1960s and the Tokyo Round in the early 1980s. It is no accident that protectionism is on the rise in the United States, despite the strength of its overall economy, in light of the current trade policy vacuum.

One of the great advantages of the contemporary regional initiatives is that they have kept the bicycle moving forward after the conclusion of the Uruguay Round. The Round itself also helped by scheduling future negotiations in a number of sectors, and the three subsequently successful sectoral agreements - on telecommunications services, information technology and financial services - also maintained the forward momentum. But no additional agreements are in sight and none of the regional negotiations are making headway. No serious trade-liberalizing effort is underway anywhere in the world at this time. Hence it is necessary to launch a new global strategy that will simultaneously keep the bicycle moving forward and avoid the centrifugal risks of drifting into conflicting blocs. The United States and European governments want to launch a new Round to do so, as noted earlier, but now need agreement with the rest of the world to offer a prospect with sufficient benefits to win their difficult domestic debates over proceedings.

The substance of a new global initiative should include elimination of all remaining tariff and non-tariff border barriers. The Uruguay Round teed up these remnants of traditional protection for decisive action by converting

agricultural quotas into tariffs, removing quota protection from textiles and apparel, and obtaining bindings of most duties. One more major effort could condemn these practices to the dustbin of history.[8]

In addition, new negotiations are needed to enable the global system to catch up with some of the "new problems" that are plaguing international trade relations. Protectionists in all countries are ingenious in staying "one step ahead of the judge" and the system needs continuous updating to stay within reach.

For example, most American (and others') complaints about Japan no longer relate to that country's border barriers. They focus instead on the anti-competitive behavior of its firms with their exclusive supplier or distributor arrangements (vertical keiretsu, as in auto parts and film respectively) and domination of particular markets (horizontal keiretsu, as in glass or soda ash). The United States has unfortunately but perhaps necessarily been using trade measures, such as Section 301, to address such non-trade problems. There is an urgent need to work out new international agreements on competition policy and corporate behavior.

Investment is a second area in which the international rules have lagged far behind commercial practice. Investment is now an essential element of international trade, especially in services but in traditional manufacturing as well. Aside from a few very modest covenants on trade-related investment measures agreed in the Uruguay Round and APEC's inadequate "non-binding investment principles", however, there are virtually no multilateral agreements on the issue.[9]

Since India and some other developing countries are both major recipients of direct investment and are legitimately concerned that they reap a fair share of its benefits, addressing that issue in the new round should be high on their priority lists. New research shows that many of the devices used by host countries in an effort to maximize their gains, such as local content, joint venture, and technology transfer requirements, are in fact counterproductive because they discourage the firms from transferring their best know-how and integrating the covered subsidiaries into their best-practices global networks. Nor can most developing countries compete with the industrial countries in offering investment incentives. On the other hand, export performance requirements may be quite effective and economically justified. Hence India and other developing countries have a high stake in working out new and better international rules in this area, trading their residual desire to impose domestic content, joint venture, and technology transfer requirements for limits on the rich countries' use of locational subsidies and investment incentives.[10]

Another pending issue is regionalism itself. The GATT article that governs such arrangements is extremely weak and its implementation has been even weaker: of the 100 or so "free trade agreements" that have been notified to the GATT, none have been rejected and only a very few have been approved. Now that regionalism is so prevalent, the WTO needs to adopt much stronger provisions and procedures to make sure that they evolve in an open manner.

A number of other topics must be addressed as well. The numerous linkages between environmental measures and trade must be sorted out. The relationship between trade and labor standards needs to be resolved as well. Both must of course be handled in ways that do not provide new excuses or justification for protectionism.

A broader yet clearly related issue is international monetary arrangements. The current regime of flexible exchange rates periodically permits sizeable and prolonged misalignments of major currencies, such as the huge overvaluation of the dollar in the first half of the 1980s and its more modest overvaluation now, and the large undervaluation of the yen in the late 1980s and again until quite recently. These misalignments in turn lead to large trade imbalances that intensify protectionist pressures in the deficit countries by tilting the domestic political balance against exporters and in favor of import-competing industries. The WTO will not solve this problem but should push the International Monetary Fund, and the G-7 as its informal steering committee, to improve the functioning of the monetary system to reduce some of the pressures on the trade regime.[11] Such trade-monetary linkage featured prominently in the original planning for the Tokyo Round in the early 1970s and to a lesser extent in the planning for the Uruguay Round in the middle 1980s.

The need for the WTO to address a series of new trade issues also replicates the earlier postwar history. The Kennedy Round produced a major reduction in the high tariffs that were the major tool of protection in the early postwar period. The Tokyo Round then attacked government procurement, subsidies and other non-tariff border barriers. The Uruguay Round turned to major behind-the-border problems such as intellectual property rights and services rules. Each of these reforms exposed a new set of constraints on market access that required a further initiative to bring the international rules up to date, and the present period is no exception.

It would be possible to address all these issues in a series of separate regional negotiations. Indeed, some of the regional agreements have innovated successfully in addressing new topics in the past: the Canada-United States Free Trade Agreement provided a model for some of the services talks in the Uruguay Round, Australia-New Zealand successfully meshed their competition policies in a manner that also enabled them to eliminate anti-dumping duties, and NAFTA has pioneered in forging effective rules on investment. There would be a serious risk of inconsistency if such issues were addressed differently in the different regional fora, however, and it would be much more efficient to derive worldwide approaches that could be applied by all. The case for globalism is again compelling.

The "Grand Bargain"

The members of the WTO should therefore agree to consolidate the free trade arrangements that have already been set at the regional level, covering more than 60 per cent of world trade as described at the outset, into a global commitment to achieve worldwide free trade by a date certain. The date could be 2010, on the APEC and EUROMED models, with a possible extension to 2015 or 2020 for the poorer countries. Implementation of the agreement would keep the bicycle moving forward for some time.

Such a commitment would have to rest on a "grand bargain" between two groups of countries: the high-income mature economies of North America and Western Europe and the rapidly growing, lower income countries that make up most of the rest of the world plus Japan. The lower income fast growers (and Japan) owe much of their success in recent decades to the openness of the world economy that enabled them to pursue "outward oriented" development strategies. Hence they need insurance against any reversion to protection by the "old rich", especially in the wake of the adverse impact on those countries' trade balances during the financial crisis.

There is a second component of this "insurance motive" in a number of developing countries: insurance that their domestic successors will not reverse the recent liberalization of their own economies. Such reforms can be "locked in" by binding the country's liberalization in international agreements, regional and/or global. Such bindings apply only to international trade and investment policies, and directly related domestic measures, but it would be difficult to reverse most domestic reforms if it were impossible to raise new external barriers to support a reversion to dirigisme.

The Asian and Latin American countries have been predominantly concerned about a possible reversion to protection in the United States, by far their largest market, and hence have emphasized trade deals with that country. They are also concerned about Europe, however, so are pursuing that dimension as well: Mercosur through a pending trade agreement with the European Union, East Asia through its new summits with the Europeans. Neither of these arrangements are likely to produce much substance, however, so East Asia and Latin America-which are likely to be two of the fastest growing parts of the world economy over the coming decades despite the current crisis-would benefit greatly from engaging Europe and Japan in the same kind of free trade commitments they have already elicited from the United States. This can probably be done only through a global effort in the WTO.

The second part of the "grand bargain" would provide the higher income countries with increased, and eventually full, access to the markets of the lower income but rapidly growing countries around the world (and Japan). Most of this latter group, despite their impressive liberalizations over the past decade or so, retains substantial trade barriers.

This part of the bargain would be attractive to the rich countries because they too are heavily dependent on integration into global markets. Such dependence is nothing new for Europe but, as noted above, has only evolved in a major way for the United States over the past two or three decades. This rich-country interest focuses primarily on countries with large and rapidly growing markets that still maintain substantial access barriers, such as India. Hence the United States and Europe would benefit greatly from the proposed "grand bargain".

There is nothing new conceptually in this proposal for the "old rich" to pledge to avoid new barriers while the "rapid growers" commit to eliminate theirs. Such asymmetric liberalization has lain at the heart of the agreements on NAFTA, the FTAA and APEC, the European Union and even the Uruguay Round itself. In these versions of the "grand bargain", the poorer countries have bought assured continued access to the markets of the rich countries by agreeing to catch up over time with those countries' prior liberalizations. There is rough justice in the proposed asymmetry because the willingness of the rich countries to facilitate the "outward oriented" growth strategies of the poor, by reducing their barriers much further and much faster, enabled some of the latter to start catching up with the income levels and standards of living of the former.

The novel element here is to shift the context to the global plane via the WTO. This would consolidate and link the existing regional agreements. It would also bring South Asia, the former Soviet Union, Africa and the few other uncovered parts of the world into the deal. It would keep the bicycle moving forward for some time.

The Implications for India

India clearly reaped important gains from the Uruguay Round of multilateral trade negotiations.

Estimates of the resulting increase in its GDP range from 0.5 per cent to over 4.5 per cent (for South Asia as a whole).[12] Coverage of Indian exports by foreign non-tariff barriers will drop from 30 per cent to 5 per cent, mainly due to the phase-out of the Multifiber Arrangement. US tariff equivalents will drop by about two-thirds on Indian exports of apparel and by about one half on India's exports of textiles.[13] India also gains from the total ban on Voluntary Export Restraint agreements (VERs) that was concluded in the Round.

In addition, the creation of the WTO (to replace the GATT) and especially its Dispute Settlement Mechanism (DSM) are of enormous value to India (and other developing countries). The greatly increased effectiveness of the DSM, which has already been clearly demonstrated, provides substantial protection for countries with smaller levels of trade. The United States, in particular, has accepted every decision against it and has changed its practices accordingly - including in two cases brought by India in 1996 concerning trade in textiles and apparel.

As in any reciprocal negotiation, India, of course, made several "concessions" in the Uruguay Round. Most of those "concessions", however, such as reductions in tariffs, phase-out of import quotas and elimination of some TRIMs, on balance benefit the Indian economy itself by reducing costs to consumers and to industrial users. Even in purely mercantilistic terms, India did not pay a very high price in the Uruguay Round: it bound most of its tariffs at rates (25-40 percent) which were both quite high and above the applied rates, and tariffed its agricultural imports at rates of 100-300 percent (as opposed to applied rates of 20-40 percent).

The agreement on trade-related intellectual property (TRIPS) will have a mixed impact. Short-term costs, defined as higher domestic prices for pharmaceuticals, eventuate fully by 2015 but the agreement should produce gains over the medium to longer run as Indian firms take advantage of patent protection to increase their own competitiveness. Korea, for example, now files about 5,000 patent applications annually in the United States-up from 162 in 1986, when it adopted widespread patent protection, and compared to only 140 for India today.

Nevertheless, like the United States and all other countries, India experiences some costs from trade liberalization and some elements of society may on balance lose from the phenomenon. Hence domestic policy must provide for these contingencies, helping to smooth the required adjustments and to equip all segments of society to benefit from globalization rather than feel victimized by it. As an effectively functioning democracy, India (like the United States) is probably subject to more pressures of this type than most trading countries. Indeed, the responsiveness of its political system to such concerns adds to the prospect for positive adjustment and thus its ability to benefit from the globalization process.[14]

Looking to the future, it is clear that India has a major national interest in an early launch and successful completion of the Millennium Round. Failure to turn back the rising threat of protectionism, especially in the United States and the European Union, by restarting the bicycle of liberalization, could levy substantial costs on Indian exports through a proliferation of anti-dumping cases and other new barriers. It could even jeopardize implementation of the complete phase-out of textile/apparel quotas agreed to in the Uruguay Round.

Moreover, a failure to pursue new multilateral liberalization could lead to renewed emphasis by India's major trading partners, the United States and the European Union, on their regional arrangements. India could thus suffer the double loss of renewed barriers and renewed discrimination. India (along with the rest of South Asia and most of Africa) thus has an even greater interest than other developing countries in convening and successfully pursuing the Millennium Round.

India's opportunities from such a new multilateral negotiation are in fact enormous. On the one hand, Indian export growth accelerated sharply after the reforms of 1991. Partly as a result, Indian growth also accelerated. Both have held up surprisingly well in the face of the Asian/global financial crisis despite the recent slowdown in export growth.

On the other hand, the Indian economy still has the lowest export share of any major developing country. That ratio has increased less for India than for any other important developing country (except Indonesia because of the sharp drop in prices for its dominant oil export). Numerous other developing countries that also had very low export shares in the 1970s--such as Mexico, Turkey, China and Bangladesh--have tripled their ratios since then. Hence a combination of domestic policy reforms and increased market access abroad could enable India to launch a period of trade-led development that would substantially increase its rate of growth. The Indian economy appears to be "teed up" for such a take-off.

Needless to say, India should vigorously press its own priority national interests in pursuing the new Millennium Round. This outside observer would suggest a few possibilities:

- elimination of the high tariffs that will remain, especially in the United States, on many Indian apparel and textile exports after the phase-out of quotas under the MFA;
- elimination of the very high tariffs on agricultural imports in many industrialized countries, especially on products of export interest to India (such as rice);
- new agreements on foreign direct investment that would both expand its levels and help India achieve a fair share of its benefits, as described above;
- tougher disciplines on the use of anti-dumping duties, especially by the United States and the European Union;
- liberalization of movement of natural persons, where India has a strong competitive advantage, under the General Agreement on Trade in Services;
- elimination of preferential tariffs in regional arrangements, including the EU and NAFTA, that discriminate against Indian exports; and
- further strengthening of the DSM to help protect the rights of countries with smaller trade levels.

In short, India has a great deal to gain from a new multilateral round. Pursuing these goals actively would seem to be far preferable to seeking re-negotiation of the Uruguay Round, as some developing countries are considering, which would clearly jeopardize phase-out of the MFA as well as theother gains to India cited above. It is certainly a better strategy, and far more likely to succeed, than trying to block the launch of a new round pending full implementation of the Uruguay Round agreements, which will surely occur before implementation of the outcome of a new round would commence; such a negative course would replicate India's futile effort to block the Uruguay Round, which discredited India in international trade circles for a prolonged period and would have turned out to be against the country's own interests. India should avoid free riding on the system, as implied by its recent decision not to participate in the second phase of the Information Technology Agreement. It certainly should avoid any push for renewed "special and differential" treatment of developing countries, which was effectively terminated by the creation of the WTO and never paid off for

developing countries anyway, rather than seeking full and active participation as an equal partner in the trading system. The recent tariff increases, which will impede export expansion, seem counter-productive.

Global free Trade by 2010

A wide variety of considerations thus point in a single direction: launching later this year, at the Seattle Ministerial Conference, of a new Millennium Round in the WTO, perhaps within the context of a decision to aim for global free trade by 2010. Such initiatives are needed to keep the bicycle of competitive liberalization moving forward. They are essential to provide effective multilateral means to deal with the trade and other international economic disputes that will inevitably increase as economic interdependence grows further. They are necessary to avoid the risk that the rapidly proliferating regional arrangements could turn into hostile blocs with adverse effects on international security as well as global prosperity. For India, active participation in such initiatives could be part of a new strategy to attain both faster economic growth and the greater global role that the country seeks and deserves.

Finally India might also want to couple such a global strategy with the new economic initiative toward Pakistan suggested earlier-an offer of true economic integration in order to heal the security and political wounds of half a century. If France and Germany could do it, and Brazil and Argentina could do it, why not India and Pakistan?

Both trade initiatives that I suggest would aim to achieve major Indian political goals. Building on the tried-and-true experience of other countries, they would reject the view that trade liberalization is a political threat to India and instead see it as a potent tool for enhancing India's highest political objectives.

From an American standpoint, "global free trade" would provide an opening of markets in the largest and fastest growing economies in the world-and thus stimulate rapid growth in exports and the good jobs that they produce. From a European standpoint, such export growth could bring down unemployment. From the standpoint of India and the rest of the developing world, new trading opportunities would result and outward-oriented growth strategies could be sustained and accelerated with an assurance that the rich industrial markets would not turn inward.

The proposed "grand bargain" would globalize the enormously encouraging progress in bridging the North-South gap that has been pioneered in recent years by the key regional agreements-the European Union, NAFTA, APEC and the FTAA-and which began at the global level in the Uruguay Round as well. The countries that account for the bulk of the world's population, and virtually all of its population growth, would become increasingly enmeshed with the "old rich" in a web of cooperative and mutually beneficial economic arrangements. There could be no better investment in securing future peace as well as prosperity.

Regional Free Trade Arrangements Share of World Trade, 1995

(Percentage)	
EU	22.8
EUROMED	2.3
NAFTA	7.9
MERCOSUR	0.3
FTAA	2.6*
AFTA	1.3

AUSTRALIA-NEW ZEALAND	0.1
APEC	23.7*
Total	**61.0**
* Excluding subregionals	

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has coordinated US foreign economic policy as Assistant for International Economic Affairs at the National Security Council in the White House. Besides being a Senior Fellow at the Brookings Institution, Carnegie Endowment for International Peace and Council on Foreign Relations, Dr. Bergsten has authored several books on international economic issues. He has also been conferred with several meritorious awards.

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