# THE WORLD TRADE ORGANIZATION AND THE SITUATION OF DEVELOPING COUNTRIES

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The World Trade Organization (WTO) was formed in1995 and, since then a number of countries - mostly the Lee Developed Countries including Tanzania - have become mebers of this global trading organization.the main objective of creating the WTO was to facilitate international trade. In this regard it has a rather ambitious objective of eliminating tariff and non-tariff barriers to trade between nations. This paper critically analyses the existing international trade paradigms and the opportunities and threats posed by the WTO to a developing country such as Tanzania. In doing so, the paper reviews also the role of the United Nations Conference on Trade and Tariffs (UNCTAD) and the achievements of the various trade rounds organized under its umbrella.

## INTRODUCTION: THE CONCEPT OF FREE GLOBAL TRADE

The theoretical insights made by two British economists, Adam Smith and David Ricardo, during the late 1770s and early 1880s have, to a large extent, influenced the way international trade has been conducted up to the current period. Their views, like those of other classical economists, emphasized among other things, that beneficial trade could take place between countries as long as: (i) trade was totally free and; (ii) countries specialized in the production and hence export of commodities in which they had comparative advantage and import commodities in which they had no or less comparative production advantage (Salvatore, 1990)

The classical free trade perspective can be viewed as some kind of a 'rebellion' against the nationalistic and protectionist views of the merchantilists whose views were dominant before the 1770s in Europe. The latter viewed national prosperity through the inflow of and accumulation of precious metals (including gold and diamond). Adam Smith, David Ricardo, Jevons and other classical economists emphasized that through specialization and free exchange of commodities resources could be utilized in the most efficient way in such a manner that the output of both commodities could rise. This increase in the output was taken as a measure of the gain from specialization in production available to be divided between the nations through trade (Salvatore, 1990).

The free trade doctrine, according to Gote (1994:1) has since then "become one of the most central doctrines in international economics and international politics." Heckscher and Ohlin (1933) equally embraced the notion of free trade in subsequent trade theories. Even in theories considered to be relevant for Less Developing Countries (LDCs) the assumption of free trade is maintained. Indeed, the concept of free trade has been so much enshrined in the economics discipline that:

> If there was an economist's creed, it would surely contain the affirmation *I understand the Principle of Comparative Advantage*" and "*I advocate Free Trade*" (Krugman 1987 as quoted in Gote, 1994: 1).

This free trade concept and its tenets has been applied to developed as well as developing countries irrespective of the inherent economic, technological and other resource disparities.

This paper attempts to analyse the efforts to create global free trade through, for example, the creation of the World Trade Organization (WTO) and the effects of this global organization on the economic development of LDCs. The paper does not pretend to break any new ground in this area. Rather, it attempts to trace the history of the efforts in the creation of free trade and thereby show how LDCs could loose or gain by the creation of free trade.

## INTERNATIONAL TRADE IS NEITHER FREE NOR FAIR

Despite the overwhelming appeal for free trade international trade has never been free nor fair. Several factors have tended to impede the free flow of goods and services between trading nations.

Practically almost all nations of the world impose, for one reason or another, some form

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of trade restrictions. Such restrictions take the form of either tariffs, non-tariff barriers and import quotas. The most important type of a trade restriction is the import or export tariff. This is a tax or duty levied on the traded commodity as it crosses a national boundary. There are different reasons for the imposition of trade tariffs. More often than not LDCs impose import tariffs in order to raise revenue while developed countries use tariffs to protect some industries from external competition.

Although it is generally true that nations impose trade tariffs it is worth to note that in industrial nations tariffs have generally declined since the 2nd World War and now average less than 10% on manufactured goods. However, trade in agricultural commodities is still subject to quantitative and other non-tariff barriers.

Another aspect which renders trade between nations to be both unfair and not free relates to the unequal exchange of commodities between developed and developing countries. For instance ivory from Africa was exchanged for a piece of cloth from Europe whereas gold was exchanged for guns. A number of researchers have succinctly showed, among other things, how this unequal exchange contributed to the underdevelopment of Africa.

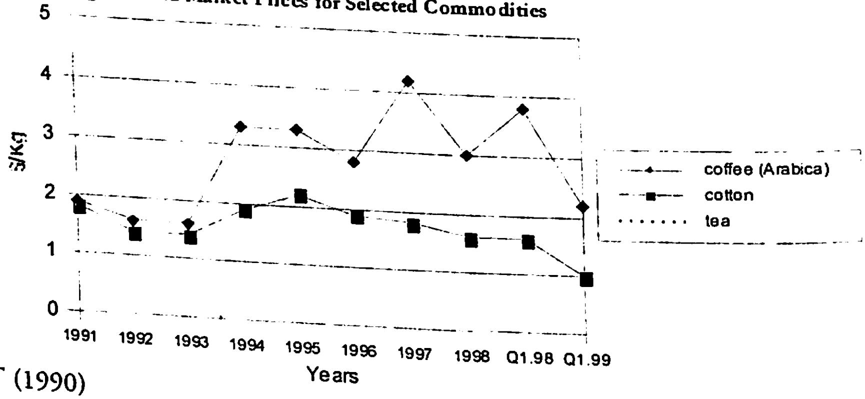
The fact that international trade has been dominated by unfair exchange practices casts doubt as to whether the efforts to lower trade tariffs will result into beneficial trade between nations.

In the case of Tanzania, for example, the world prices for most of its agricultural and mineral based products have either stagnated or actually declined (figs. 1 and 2). The problem is that whereas production of these commodities takes place in LDCs prices for these commodities are decided in world markets. Another problem is that most LDCs especially those in Sub-Saharan Africa tend to produce similar (agricultural and mineral) products. Agricultural products have a further disadvantage in that they are dependent on weather. So periods of good weather result into higher output for some products. However since many countries take opportunity of the good weather a production glut results and, with it, lower prices.

Tanzania and other developing countries in its position are continuing to produce commodities (sisal, coffee, cashew nuts) for exchange in world markets but do not have control over their prices. While in some commodities the quantum of exports from developing countries has declined the negative impact on this fall in quantity of exports on their economies has been worsened by falling terms of trade.

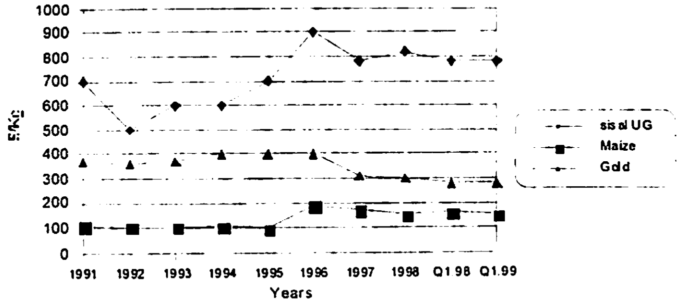
The concern over unequal exchange between developed and developing countries has led to proposals like: (i) de-linking trade relations between the developed North and the underdeveloped South; (ii) increased South-South trade; and (iii) demands for a New International Economic Order. Since the establishment of the United Nations (UN) in 1945, LDCs have tended to operate within the established UN system to make a case for improved trade relations with developed countries. In the following section the paper attempts to trace theLDC's trade problems and prospects since the formation of the United Nations Conference on Trade and Development to 1995 when the World Trade Organization (WTO) was created.

Fig. 1: World Market Prices for Selected Commodities




Source: BOT (1990)

Fig. 2: World Market Prices for Selected Commodities




## GATT, THE ROUNDS, WTO AND EFFORTS TO CREATE FREE TRADE

### The General Agreement on Trade and Tariffs (GATT)

As its name suggests, GATT has, since its creation in 1947, sought to promote free trade through multilateral trade negotiations. The Geneva based organization has tended to operate on three basic principles as follows[2]:

1) Non discrimination. This principle refers to the unconditional acceptance of the most favoured nation clause. The only exception to this principle are made in cases of economic integration.
2) Elimination of non tariff trade barriers (such as quotas) except for agricultural products and for nations in balance of payment problems.
3) Consultation among nations in solving trade disputes within the GATT framework.

About 100 nations are signatories to GATT and currently over four-fifths of all international trade is embraced under GATT rules. The organization has managed to reduce tariffs by a total of about 35% in five different trade negotiations between 1949 and 1962. In 1965 GATT rules were extended to allow preferential trade treatment to developing nations and to allow them to benefit from tariff reductions negotiated among industrial without reprocity. The extent to which LDCs have benefited from the preferential treatment under the auspices of GATT is not known.

[2]See also, Salvatore (1990: 266)

### The Kennedy, Tokyo and Uruguay Rounds

This section traces the historical and economic circumstances that led to the holding of trade negotiations between industrialized and non-industrialized nation since the early 1960s to the current period.

#### *The Kennedy Round*

The fear created by the formation of the European Economic Community prompted the Kennedy administration in the USA to pass the Trade Expansion Act of 1962 which empowered the US president to negotiate across-the-board tariff reductions. Under this act USA under the auspices of GATT initiated wide-ranging multilateral trade negotiations which came to be referred to as the Kennedy Round and which were completed in 1967. They resulted in cutting tariff rates on industrial products. The Kennedy round did not deal with non-tariff barriers especially in agriculture.

#### *The Tokyo Round*

The Tokyo Round negotiations were conducted under the USA Trade Reform Act of 1974 which authorized the US President to negotiate further tariff reductions and non-tariff trade barriers. These multilateral tariff negotiations popularly known as the Tokyo Round resulted in further reduction of tariffs and managed to put a code of conduct for nations to adhere to in applying non-tariff barriers.

#### *The Uruguay Round*

The eighth round of multilateral trade negotiations have been referred to as the Uruguay Round. Negotiations under this round started in 1986 and were concluded in 1990. The

Uruguay Round of negotiations aimed at establishing rules for checking the proliferation of new forms of protectionism and take on board services, agriculture and foreign investments into the negotiations. The Uruguay Round also attempts to negotiate rules for the protection of intellectual property rights and improve the system of settling trade related disputes between nations. However, the actual work of implementation of these rules was left to the WTO. Like in the case of GATT there have been marginal benefits for LDCs in the Uruguay Round of negotiations.

### The World Trade Organizations

The World Trade Organizations (WTO) was established in January 1995. Its prospective membership is already over 130 countries. The WTO was established to facilitate the implementation and operation of all agreements and legal instruments negotiated in the Uruguay Round (1986-1993) and to provide a forum for all trade related negotiations.

The Agreement establishing the WTO reiterates the objectives of GATT, i.e.; to raise the standard of living and incomes, ensuring full employment, expanding production and trade and optimal use of the world's resources. The agreement establishing the WTO mentions the objective of sustainable development in relation to the use of resources and recognizes the need for a special treatment of developing countries especially the least developed among them.

## WTO: Functions, Organizational Structure and Assumptions

### Main Functions

Article II of the Agreement establishing the WTO outlines the two main functions of the organization as to:

a) Facilitate the implementation, administration and operation of the Uruguay Round agreements and;
b) Provide a forum for negotiations among members concerning their multilateral trade relations.

### Organizational Structure

The WTO is headed by a ministerial conference which meets once every two years and is the main decision making body of the WTO. The ministerial conference consists of all member states.

Below the Ministerial Conference is the General Council made up of all member states and shall meet "as appropriate." In the two gears between the meetings of the Ministerial Conference the Council will carry out the functions of the conference. The council will oversee the work of Dispute Settlement Body and the Trade Policy Review Mechanism.

Working under the Council will be three further councils one for trade in goods, the others for trade in services and trade-related aspects of intellectual property rights. Each of these sub-councils is to establish subsidiary bodies for the operation of the various agreements. The WTO has three further committees to deal with budget, finance and administration, trade and development and balance of payments respectively.

The WTO operates on the principle of *one member one vote* and aims at reaching a consensus on all issues. In this regard the WTO is not significantly different from previous trade organizations.

### Assumption in the WTO

The implicit and explicit assumptions of the WTO are that:

i) All member countries have the same set of information regarding the operations and implementation of its rules;
ii) The one member one vote principle implies that all member are equal;
iii) Trade disputes between member countries can be settled quickly and fairly; and
iv) Lowering of trade tariff will lead to increased flow of goods and services, output and increased welfare of the trading nations.

However, the extent to which these assumptions hold for developed and developing countries alike is mutable. Evans (1996: 4) has, for example, pointed out that the "one member one vote" principle notwithstanding, some members are more equal than others. In reality the major trading powers will have more influence over the WTO proceedings than smaller trading nations." This raises concern as to whether LDCs can significantly benefit from the WTO arrangement.

## THE WTO AND LDC'S TRADE: OPPORTUNITIES AND THREATS

At a broader context the creation of the WTO can be viewed in terms of the globalization process which is defined as a rapidly increasing complex interactions between societies, cultures, institutions and individuals worldwide (Wangwe and Musonda, 1999). Specifically, globalization is reflected in such ways as trade and financial liberalizations, internationalization of production, distribution and marketing and the free flows of factors of production.

As an economic phenomenon, globalization is usually taken to mean the increasing density of economic integration among countries, reflected in an increasing share of output in a country belonging to, and being managed by, nationals of other countries and increased financial integration among countries. Globalization is facilitated and stimulated by a lowering of impediments to cross boarder trade through technological progress or through lowering of tariffs and investment restrictions. Inevitably the globalization process produces 'winners' and 'losers' alike.

## LDCs' Opportunities in the WTO

During the Uruguay Round negotiations there were few provisions and some improvements in LDCs trade especially in agricultural trade. For instance during the Uruguay Round negotiations and under the WTO framework arrangements were made to give LDCs improved possibilities for exporting certain agricultural products as well as textiles and clothing to the developed countries. In addition, the poor, net food-importing countries have been promised compensation for expected rising food prices. There are indications however that developed countries have, to a large extent, not yet met their obligations in accordance with what was generally agreed during the Uruguay Round negotiations.

There are other opportunities which LDCs can potentially benefit from the WTO set up. For example the globalization of general competitive behaviour and the globalization of competition in trade is expected to improve trade efficiency and, with it, lower prices and hence improved welfare. These trade benefits are however dependent on the extent to which LDCs can improve their production, marketing efficiency and hence increase their share in world trade.

## Threats Posed by the WTO to LDCs

At a broader context the threats posed by the WTO to LDCs are almost equivalent to those of the globalization process. The following are selected examples of areas where LDCs could be marginalized.

### *Global Flow of Goods and Services*

The move towards reduction of trade protection through reduction of tariff and non-tariff barriers is expected to result into increased flow of goods and services. However, as noted above, for LDCs to be able to benefit more from the lowering of the quantitative trade restrictions they will have to: (a) generate the capacity to import; and (b) find ways to penetrate the markets in developed countries.

However, a more daunting problem for LDCs is that while the lowering of trade restrictions is likely to increase the mobility of factors of production - including labour - the most abundant factor of production in most LDCs which is unskilled labour will not be internationally mobile.

### *Form of Exports and Imports may Complicate LDC's Situation*

Whereas most LDCs have remained producers and exporters of mainly agricultural and mineral products and tend to import petroleum oil and manufactured goods, exports from developed countries to LDCs have tended to be technologically advanced (e.g. computers, etc.) goods and services whose prices in world markets are either stable or rising. This may, in future, complicate the balance of payment situation of LDCs.

### *Income Differentiation Between LDCs and Developed Countries*

The reduction of trade tariffs could lead to more incomes for developed countries who are able to export more and less income to (LDCs) countries which are not able to take advantage of the reduction in quantitative trade restrictions. Unless an elaborate mechanism is put in place to address possible income differentiation which is likely to occur the WTO will not be significantly different from past trading arrangements.

### *Capacity to Negotiate During Trade Disputes*

There is also concern that the majority of LDCs have not yet developed the capacity and expertise to effectively negotiate with developed nations in cases involving trade disputes.

## CONCLUSION

Whether the WTO will provide an opportunity or threat to LDCs will depend, to a large extent, on how this organization will address the specific trade problems of LDCs. The first of such problems is the increasing tendency of nations to by-pass GATT rules and impose other types of non tariff barriers (NTBs) to international trade. There is a danger that if this process continues, the leading nations may even begin to demand specific shares of each other's markets as a condition for allowing continued access into their own markets. Furthermore, there is the danger that the proliferation of NTBs will lead to retaliation and a decline in the flow of international trade. The WTO will have to work to discourage this tendency (Salvatore, 1990).

The WTO will present itself as an opportunity for LDCs if it addresses comprehensively the agricultural problems of these countries. Some of these problems include declining terms of trade for agricultural commodities and increasing non tariff barriers against some agricultural products from LDCs face in developed countries.

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