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The Doha Round after Hong Kong

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WHAT WAS ACCOMPLISHED IN HONG KONG?

Trade ministers from member countries of the World Trade Organization (WTO) convened in Hong Kong in December 2005 to jump-start the flagging Doha Round of multilateral trade negotiations. The Hong Kong ministerial was not a complete bust. But ministers accomplished only the minimum necessary to keep the Doha Round moving forward—toward an undetermined and probably distant conclusion.

The meeting achieved more in spirit than in substance and placed more emphasis on negotiating process than on policy reform. Concluding the talks by the targeted deadline of year-end 2006 is now highly improbable.

Much of the 40-plus-page ministerial declaration confirms policies already being pursued by the major trading nations. The industrial countries anted up kernels of subsidy reform and development assistance, but all of the big-ticket items were studiously deferred to future meetings. Progress on nonagricultural market access (NAMA) and services was microscopic. Ministers were left with little to celebrate, except for a few minor decisions to

- end farm export subsidies by the end of 2013. But such measures are small compared with trade-distorting domestic farm supports: under \$5 billion outright export subsidies versus \$80 billion "amber box" subsidies worldwide, in applied terms. Most export subsidies were already tagged for extinction well before the 2013 date.

- end tariffs and quotas, by 2008, on 97 percent of the tariff lines exported by the least developed countries (LDCs). But this commitment only modestly augments the status quo; for example, the United States already allows duty-free and quota-free imports for 83 percent of LDC trade. Exempting 3 percent of tariff lines actually would affect a much larger share of trade because it would cover the least competitive domestic production. For example, it would provide ample room to continue restricting trade in sugar, clothing, leather goods, and ceramics—key exports of many LDCs.

- end cotton export subsidies in 2006 and all tariffs and quotas restricting LDC cotton exports by 2008. Congress recently enacted some of these reforms to satisfy adverse rulings in a WTO dispute.

- allow LDCs to maintain measures inconsistent with the Agreement on Trade-Related Investment Measures for at least seven years and possibly until 2020. Under this provision, LDCs can legislate "performance requirements" for years to come—measures that often are detrimental to their own development but imposed to satisfy domestic political interests.

- extend the moratorium on tariffs on e-commerce until the next ministerial.

Box 1: Doha Round deadlines (per Hong Kong declaration of December 18, 2005)

Paragraph	Issue
1	Conclude negotiations in 2006.
6	Define export subsidy disciplines by April 30, 2006.
10	Modalities for agricultural market access by April 30, 2006; draft schedules by July 31, 2006.
11	End cotton export subsidies in 2006; end tariffs/quotas on LDC cotton exports in 2008.
23	Modalities for NAMA negotiations by April 30, 2006; draft schedules by July 31, 2006.
Annex C, 11	Revised services offers due by July 31, 2006. Final draft schedules due by October 31, 2006.
Annex D, 2	Provisional decision on regional trading arrangement transparency by April 30, 2006.
Annex F, 36	Provide duty-free and quota-free market access for at least 97 percent of LDC exports by 2008 (or start of implementation period).

MULTIPLE DEADLINES FOR 2006

Trade officials initially had hoped that the Hong Kong ministerial would provide a broad outline of how far countries were willing to go in liberalizing agriculture, manufactures, and services. Agreement on these "modalities" would then enable Geneva negotiators to flesh out specific commitments for the final WTO package by the end of 2006. The United States tried to accelerate the Hong Kong preparations by offering, in early October, to substantially reduce its farm subsidies and import barriers, if other major trading countries did the same. But the European Union countered that its position on farm reform was sufficient and that other countries first had to improve offers on NAMA and services. As a result, the negotiating impasse continued since most countries regard the EU offer as insufficient.

Long before the meeting convened, ambitious expectations for the Hong Kong meeting had been scaled back. Instead of ratcheting up the negotiating stakes, the ministerial became a defensive effort to avoid dumbing down the WTO agenda or—even worse—to avoid a collapse as in the previous Cancún ministerial.

The Hong Kong declaration provided little guidance to negotiators on how to surmount obstacles that have blocked progress on agriculture, manufactures, and services since the Doha Round began in late 2001. But it did announce multiple new deadlines for agreement on the "modalities"—namely, rules and procedures for conducting negotiations—whereby liberalization is finally achieved for trade in agriculture and industrial products and for making new offers on services (see box 1).

In essence, the end of April 2006 has now become the new target for negotiators to achieve what they sought to do in Hong Kong. That is when modalities for the all-important agricultural and industrial tariff negotiations are supposed to be agreed. Recall, however, that every deadline set during the four-year duration of the Doha Round has been missed. This record will likely remain unblemished in 2006.

MUCH ADO...AND MUCH LEFT TO DO

Trade ministers doubtless appreciate the urgency of advancing the Doha agenda but lack the political horsepower to overcome their domestic opponents, especially farmers. This is particularly true in the European Union, where several members of the European Council are seeking to constrain EU Trade Commissioner Peter Mandelson. But the US Congress is also firing warning shots at US Trade Representative Rob Portman.

Progress on agriculture has been insufficient to spur worthwhile offers on manufactures and services, especially from the handful of big emerging-market countries that will enjoy the most growth over the next decade—China, Brazil, India, Indonesia, South Africa, and Thailand. The "mini-ministerial" meeting held in Davos in late January 2006 did little to change the negotiating dynamics. That meeting reconfirmed the Hong Kong commitment to advance other issues in parallel with work on agriculture but also that new offers on agriculture were unlikely from the major industrialized countries. While Brazil, India, and other developing countries may now step forward with new offers on manufactures and services, their proposals are likely to contain only minor reforms that fall well short of what could energize the farm talks. Despite the Davos rhetoric, those countries remain wary, and justifiably so, that key farm reforms will be excluded or subject to lengthy deferment in the Doha Round negotiations.

Without substantive offers outside of agriculture, by both developed and developing countries, the United States, the European Union, and Japan will not be able to maintain—much less augment—their offers on farm reforms. So the talks echo the old "Alphonse and Gaston" routine, in which each side waits for the other to move forward—and consequently neither side moves at all.

In the following subsections we explain what was not done.

Agriculture

Rightly or wrongly, agriculture has become the linchpin of the WTO negotiations—not because of its importance (less than 10 percent of global merchandise trade, and growing slowly) but because it is the sector with the highest trade barriers and the area where product-specific reforms are essential to command the support of LDCs for the overall agreement. To date, the farm talks have lagged due to concerns that (1) the major industrial countries would not reduce their subsidies and/or import barriers, and (2) key developing countries, such as Brazil, China, India, Indonesia, and Thailand, would not lower their own import barriers. Developing countries—some for tactical reasons, others because they face severe pressure from their own farm lobbies—have hesitated to table meaningful offers on industrial products and services absent hard-and-fast commitments on agricultural reform on the part of OECD nations. But Mandelson insisted at Hong Kong that other countries should move ahead on NAMA and services before the European Union considered changes to its negotiating proposals.[1] (USTR Portman had a more flexible negotiating position.) Bluntly put, progress has been impeded by tactical considerations that mask political resistance not only to farm reform but also to lower industrial tariffs and greater access to services markets.

The main "deliverable" from Hong Kong was agreement to phase out all forms of farm export subsidies (including subsidized components of export credits, food aid, and state trading enterprises) by the end of 2013. This agreement was achievable because (1) farm export subsidies are a minor irritant compared with the distortions generated by the combination of domestic farm subsidies and border restrictions, and (2) most US and EU export subsidies are already scheduled to be phased out over the next few years. Even then, the 2013 date, tied to the EU timetable for reform of the Common Agricultural Policy (CAP), allows export subsidies to continue for three years longer than most countries wanted.

The Hong Kong ministerial placed more emphasis on negotiating process than on policy reform.

On domestic farm support, ministers could not reach agreement. Levels of support bound in the Uruguay Round are often twice as high as current disbursements, so negotiators need to accept very large percentage cuts to actually change existing programs. The issue is further complicated by the need to revamp the WTO's intricate set of accounting principles, which determine which payments are subject to cuts and which are not. Some payments are excluded if they fall below the so-called de minimis thresholds (calculated as around 5 percent of the value of farm production). Others are classified as "less trade distorting" because they are accompanied by acreage and production limits, and these are put in a "blue box" with some limits. Still others are deemed "permissible," because they are supposedly decoupled from price levels and production decisions, and these are protected in a "green box" with no limits. Negotiators need to clarify what programs—and maximum subsidy amounts—can be covered by each of these exceptions.

The European Union argues that it has already achieved a substantial reduction from its bound level of domestic farm support through the programmatic reforms adopted in 2003. In fact, the EU reforms would shift many of the CAP

1. An attempt was made to codify this interrelationship in the Hong Kong declaration. Paragraph 24 calls for a "comparably high level of ambition in market access for Agriculture and NAMA . . . to be achieved in a balanced and proportionate manner." EU member states insisted that developing countries be put on notice that the European Union expects better offers on NAMA as reciprocity for its farm offer. But Brazil countered that the language requires similar cuts in farm and industrial bound tariff rates. Since there is often a larger gap between bound and applied rates in the industrial tariffs of developing countries than in the farm subsidies of OECD nations, Brazil's interpretation would require larger cuts in applied rates for OECD farm subsidies and smaller applied cuts by developing countries in their industrial tariffs (see *Inside US Trade*, January 13, 2006, 3).

payments into the blue or green boxes. US farm programs, particularly those added in the 2002 farm bill, would be more directly affected, in applied as well as bound terms, by lower de minimis thresholds and blue box limits (already agreed in the August 2004 framework accord). Nonetheless, in a proposal tabled in October 2005, US officials offered substantial cuts in current US programs if other countries reciprocated.

The most important pillar of the agriculture negotiations, market access, received the least amount of attention in Hong Kong. The Uruguay Round agreement set bound tariffs on farm products at levels well above applied rates. To drain the "water" from these tariffs and create new trading opportunities, Doha Round reforms will have to cut very deep. Furthermore, triple-digit tariffs derived from the mismanaged "tariffication" exercise of the previous round—when most quantitative restrictions were supposedly converted into their tariff equivalents—will require additional reform through agreement on caps for maximum tariffs, preferably in the range of 50 to 100 percent. To date, the European Union has offered average cuts in bound rates far below both the US and the G-20 proposals. The actual differences are difficult to calculate because the EU offer would permit a much larger number of exceptions (products not subject to the full cut or exempted outright) than proposed by the United States or G-20.[2] Hong Kong made no progress in narrowing this gap, and post–Hong Kong comments by EU officials suggest that the EU offer will not be improved anytime soon.

Concluding the talks by the targeted deadline of year-end 2006 is now highly improbable.

Nonagricultural Market Access

Ministers endorsed what had already been accepted in Geneva and adopted a tariff-cutting formula that requires larger reductions for high than low tariffs (a variant of the so-called Swiss formula). But they did not provide guidance on the coefficients to be applied in the formula, which determine how deep the reductions should be and the extent to which cuts should differ between industrial and developing countries. For many developing countries, such as Brazil, China, and India, big air pockets separate bound and applied tariffs, so that, for example, a 30 percent cut in the bound rate might make no difference to the applied tariff.

Ministers also failed to clarify the permissible scope for exceptions to the general tariff-cutting formula. Nor did they provide guidance for sector negotiations, which would cut tariffs more than the formula for selected industries. Thus, the framework for NAMA negotiations remains incomplete. Faced with all these difficulties, the ministers set a new deadline of April 30, 2006, for establishing the negotiating modalities.

An agreement on modalities is only one step toward a NAMA package. The formula will clarify the maximum and minimum cuts across all products, but most of the negotiating effort will then be spent on how the rules are bent for sensitive products—which, by definition, means those protected by high tariffs and nontariff measures.

By far the best result would be to follow the original US proposal to eliminate all nonagricultural tariffs by 2015 (with limited exceptions and longer implementation periods for developing countries). But this outcome is extremely unlikely. US clothing firms strongly oppose tariff cuts, now that the Multi-Fiber Arrangement (MFA) quota system is history. Many developing countries are wedded to their highly protected industries (autos and consumer durables are noteworthy) and their trade preferences in industrial markets. A few small developing countries (for example, Caribbean nations) need tariff revenue to balance their budgets.

Services

Ministers agreed to general objectives and specific approaches for liberalizing trade in services (contained in annex C). The objectives, however, were cast as indicative guidelines, which WTO members should follow "to the maximum extent possible," in crafting offers on each mode of delivery of services and on reducing or removing scheduled exemptions from most favored nation (MFN) treatment.

Due to pressure from the G-90, led by South Africa, ministers agreed that bilateral request-offer negotiations "shall remain the main method of negotiation" (annex C, paragraph 6). The request-offer process is particularly tedious and has achieved virtually nothing since 2000. Indeed, on this basis, the services talks, which started before the launch of the Doha Round, remain stalled five years later.

As of July 2005, only 68 offers (covering 62 percent of WTO members) had been tabled. LDCs are not required to table offers if their development needs would be affected, but even excluding LDCs, 24 developing countries had not been heard from—including South Africa, Venezuela, Nigeria, and

2. The USTR claims that the EU offer amounted to a cut of 39 percent in bound tariff rates, the US proposal to a cut of 66 percent, and the G-20 proposals to a cut of 54 percent.

Ecuador. Moreover, the small number of offers tabled masks even smaller projected reforms—in other words, the "quality" of the offers, especially on the provision of services via commercial establishment (mode 3) and labor services (mode 4) is extremely low. Often the offers merely commit to bind existing practices and thus do not open new commercial opportunities (the old bound versus applied issue). Some offers even propose setting obligations at levels more restrictive than current practice!

Ministers agreed that groups of countries could pursue "plurilateral" negotiations, whose results "shall be extended on an MFN basis"—that is, to all WTO members, even countries that make no concession whatsoever. This process could produce sector pacts; the ministerial declaration makes no mention of specific sectors and does not address the issue of critical mass. But it does reaffirm all of the special and differential provisions in prior declarations that significantly dilute the liberalization that developing countries must undertake.

In agriculture, the main "deliverable" from Hong Kong was agreement to phase out all forms of farm export subsidies by end 2013.

As a ballpark estimate, we assume that at least 15 countries need to agree on economically meaningful offers in 15 sectors, mainly involving telecommunications and financial services, professional services (legal, health, engineering, computer, and education), energy services, and transport and distribution services. According to annex C of the Hong Kong declaration, plurilateral requests should be made by the end of February and offers tabled by the end of July 2006. Since many countries will not develop offers until they see what comes out of the agriculture and NAMA work on modalities (due by the end of April 2006), it seems unlikely that a broad 15 by 15 matrix of plurilateral request/offers can be put together by the July target, much less a final package negotiated by the end of October 2006 as mandated in paragraph 11 of annex C.

For a deal on services to come together, the ad hoc "core group on services" must engage in intensive talks. The United States and India co-chair the core group; other members are Brazil, China, the European Union, Mexico, Australia, South Korea, Malaysia, Singapore, Japan, Argentina, Chile, and Canada. If South Africa, Egypt, and Switzerland join the party, perhaps a critical mass will exist for some key sectors. But this group comprises countries with very different priorities, both by sector and mode of delivery.

Industrial countries seek reforms in infrastructure services where their firms are competitive (e.g., banking, insurance, telecom, and air transport), while developing countries want new opportunities to provide labor-oriented services (e.g., health care, construction, and basic information technology services). Satisfying both camps requires the elimination of nationalistic rules on establishment and governance and the reform of regulation that fosters incumbent suppliers. Changes are doubly contentious when the existing rules reflect national security and cultural objectives.

Commitments on labor services (mode 4) pose a particular challenge. Congress has warned the USTR not to make offers that would alter US immigration policy. Moreover, the electronic delivery of services to OECD markets may prove far more important to most developing countries than new migration opportunities. However, to reach an overall agreement on services in the Doha Round, specific and narrowly focused obligations may need to be undertaken on mode 4. As one way around the impasse, the USTR might discuss a list of activities for which the cross-border provision of temporary labor services, controlled both as to number and length of employment, would be accepted by Congress.

Rules

While the negotiation on rules covers a number of subjects, the spotlight is focused on antidumping and countervailing duties. Disciplines on regional trading arrangements and fish subsidies also attract some notice. In Hong Kong, all these issues were relegated to a single sentence in the ministerial declaration, which merely echoed previous negotiating mandates. However, ministers attending the Davos meeting went further and essentially put the drafting of new text on trade rules on a similar timetable as advances in talks on farm and industrial products.

As the negotiations move closer to a conclusion, the antidumping issue could become more contentious, for two related reasons. Some countries want to curtail the perceived abuse of antidumping practices; others, as a matter of tactics, conclude that US reluctance to move on antidumping will allow them to take their own sensitive issues off the table. Some countries want it both ways: curtail the use of antidumping measures by industrial countries but allow developing countries unfettered use of this safeguard tool. Developing countries, including China, now rank among the most active users of antidumping measures and insist on maintaining their policy flexibility.

Some countries want the WTO rules clarified and augmented with regard to issues dealt with in recent WTO dispute panel rulings.[3] US and EU decisions have been found wanting by the WTO Appellate Body, and some countries seek to codify the case holdings in WTO obligations. Key members of Congress have told US negotiators to reject such demands.[4]

WHAT SAYETH THE CRYSTAL BALL?

Predicting the outcome of a massive trade negotiation is subject to even more than the usual hazards of forecasting endeavors. Nevertheless, national positions have sufficiently hardened, and the time remaining is sufficiently short, that we can hazard a few guesses. We cast our speculation in the form of answers to five hypothetical questions that presidents and prime ministers might pose to their trade officials.

Can the Doha Round Be Concluded in 2006?

The US Trade Act of 2002, which includes trade promotion authority (TPA), requires the president to notify the Congress by December 2006 if he intends to offer amendments to the trade remedy laws (antidumping, countervailing duty, and escape clause legislation), and by April 2007 if he intends to sign an agreement. Any agreement so notified, and signed before June 30, 2007, can then take advantage of the crucial "fast track" features of the TPA law: a congressional vote up or down within 90 days, with no amendments.

Despite these US deadlines, reinforced by the multiple deadlines set forth in the Hong Kong declaration, the prospects for concluding by December 2006, or indeed by April 2007, are near zero. The negotiating gaps are just too great, and the sense of crisis is too far removed, to conclude the round on schedule. Indeed, the history of the Doha Round, from its late inauguration (in 2001, almost seven years after the Uruguay Round was concluded), right through the Cancún and Hong Kong ministerials, is a history of missed deadlines.

Hong Kong closed the door on prospects for completing a big package of agreements by the end of 2006, or even early 2007, in time to allow the United States to implement the results under current TPA. To be sure, trade and agriculture ministers are hard at work trying to disprove our somber assessment. Such efforts are critical to the success of the Doha Round—whether it comes in 2006 or later. As a practical matter, WTO negotiators must operate under the assumption that the Doha Round can be successfully concluded before the expiration of US TPA. There is no assurance that TPA would be extended—given how sharply divided Congress is on trade issues—and there is much evidence that extending the horizon of the talks could undermine negotiating momentum. So ministers will engage in frenetic negotiations to craft a substantive package of trade reforms in all areas of the WTO agenda. Completing such a package by year-end would be an enormous feat and is highly unlikely. But making progress to that end in 2006 is essential—because without such progress, it will be hard for US officials to justify an extension of TPA.

That said, the Doha Round can follow three paths.

Our bet is on the short extension of trade promotion authority, say to December 2007.

The first scenario is outright failure. Under this scenario, countries allow the talks to drift aimlessly because of a lack of consensus. Diplomats go through the motions in Geneva for years to come—an exercise for which they are well experienced. As in the aftermath of the Cancún fiasco, regional initiatives proliferate—particularly in East Asia—as an alternative to WTO liberalization. At the same time, failure feeds strong demands for new protectionism—especially against the "flood" of low-wage exports from China and India.

The second scenario is that countries agree on a minimalist deal that omits reform of key trade restrictions. Some observers believe that even a small deal would keep the multilateral process alive, and that sector negotiations (say, on services) could continue as part of another "built-in" negotiating agenda. But a small package would leave both rich and poor countries deeply dissatisfied. It, too, would provoke a new wave of regional trading arrangements and targeted protectionism.

Why would developing countries agree to postpone a maximum multilateral accord until the next round, a decade or more in the future—especially when there is no guarantee

3. One practice that the WTO Appellate Body has rejected is "zeroing"—namely the exclusion of imports that have a negative dumping margin from the calculation of the average positive dumping margin for the product. Another rejected practice is the "cumulation" of imports from suppliers that are not targeted with dumping duties with imports from suppliers that are targeted in determining injury.

4. In principle, the judicial rule of *stare decisis* does not apply to WTO Appellate Body decisions. Some Congressmen evidently hope that future WTO Appellate judges will take a different view on the antidumping issues lost by the United States. In practice, as scholars have shown, WTO Appellate Body decisions do follow the rule of *stare decisis*, so congressional hopes are unlikely to be answered.

that there will be another round? And why would OECD countries agree to a result that offers no political or economic gain after all the effort? The strongest answer to both questions—weak though it is—is that today's trade ministers and their political leaders do not want to leave office with "failure" written on their resumes.

The third scenario is full-bore negotiations that extend through 2007, possibly longer. In essence, countries are already pursuing this option. Most countries can easily agree to extend the talks. For the United States, however, extending the round requires decisions by the Congress on whether to reauthorize TPA (and, if so, for how long, and whether for WTO talks only or both the WTO and free trade agreements [FTAs]) and whether to extend or rewrite the US farm bill, which expires at the end of the 2007 crop year.

White House officials and business lobbyists have been scarred by the fractious ratification vote on the Central American Free Trade Agreement (CAFTA) and fear that reauthorization of TPA would revisit the battle of summer 2005. The slim protrade majority in the House of Representatives could fall victim to the November 2006 mid-term elections. To legitimize the request for an extension of TPA, the Bush administration will have to demonstrate that large benefits are in the offing from both the Doha Round and big new FTAs under negotiation. To increase the chances of TPA renewal, the Doha Round will have to make significant progress in 2006, particularly in the areas of US export interest: agriculture, services, and NAMA.

Deliberations on a new farm bill may be just as contentious. The administration went out on a limb in proposing major reforms in farm subsidies. While supported by major farm groups (because the US offer was conditioned on reciprocity from US trading partners), some key members of Congress voiced concern. If the Doha Round is extended, Congress will have to decide whether to simply extend the 2002 farm bill (perhaps for the same period as the TPA extension) and await the results of the trade negotiations or to rewrite the farm bill so as to constrain the US negotiating position in the talks. Either way, the subsidy gravy train to US farmers will add red ink to the federal budget.

The serious question is whether a short extension of TPA, say to December 2007, will become the fall-back position, or whether the G-8 and G-20 will decide to "give the round a rest," let TPA lapse, and resume negotiations after the US presidential election in 2008. Our bet is on the short extension: A two-year "rest" would be widely interpreted as a permanent and fatal interment for the Doha Round.

We believe the Doha Round needs a political "jolt" if it is to follow the third scenario and produce a notable result. Trade ministers do not have the political authority to approve reforms in sensitive areas needed to produce a comprehensive package of accords acceptable to all WTO member countries. Decisions by heads of state, perhaps encompassing issues that transcend the trade agenda, probably will be needed to provide each leader political ammunition to counter domestic critics.

Brazilian President Luiz Inácio Lula da Silva vetted this idea prematurely before the Hong Kong ministerial. The timing was wrong, but the idea has merit. A "trade summit" involving countries whose policy reforms are crucial to the success of the WTO venture is needed, preferably before the G-8 summit in St. Petersburg, Russia. The reason for another head-of-state meeting is that certain countries that are key to the Doha Round—Brazil, China, and India—are not members of the G-8, while Russia (a G-8 member) plays virtually no role in Doha talks. Such a meeting should seek to break the negotiating deadlock by raising the prospect of a "grand bargain"; to that end, the leaders should agree to extend the talks for a short period to accommodate their higher ambition.

Of all major countries, China has the most to lose from the collapse of the WTO system.

How Do Negotiations Look from the Perspective of Key Players?

First consider key interest groups. For most CEOs of the Global 1000, the WTO talks are either a yawn or an irritation. The prospective market opening in the big emerging markets (China, India, Brazil, Russia, etc.) is much too modest for CEOs to throw their weight against their formidable domestic opponents. For some of the Global 1000—not only textiles, clothing, and footwear but also pharmaceuticals, entertainment, steel, and autos—the WTO talks are viewed more as a threat than an opportunity.[5] Meanwhile, the domestic opponents of liberalization—farm and textile lobbies in the United States, Europe, and Japan, coddled banks and utilities as well as farmers and manufacturers in most developing countries, and a wide range of nongovernmental organizations (NGOs)—are better organized than the proponents of a big bargain. Finally, without a Cold War, global trade talks don't dovetail with diplomatic imperatives. Hence most foreign ministers, presidents, and prime ministers give trade talks a

5. However, there is strong corporate support for several big-ticket FTAs (e.g., Korea, Egypt, Indonesia, and Malaysia) that could reinforce already substantial US trade and investment interests.

second-tier ranking among their priorities. Attitudes at the top will need to change, dramatically, before President Lula da Silva's "trade summit" becomes a reality.

Now consider key nations. In the European Union, the Council of Ministers is trying to craft language that would rein in EU Trade Commissioner Mandelson. Reform-weary members like France and Italy have been able to blunt reformist proposals by the United Kingdom and Sweden. EU firms seek serious services liberalization and much lower tariffs on manufactured goods in emerging markets, but they have nearly given up hope. Both goals seem remote. Japan is right alongside the EU defensive agenda.

The United States is playing a defensive/offensive hand. Farm lobbies will fiercely resist cuts in applied subsidy levels and tariff/quota barriers until they see equivalent applied liberalization in Europe, Japan, Korea, and elsewhere. Pharmaceuticals, entertainment, and software firms are spending most of their effort to avert backsliding on the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). High-tech manufacturers want zero-for-zero tariffs, and service firms want the right of establishment and national treatment in key sectors. The main difference between US and EU firms with offensive goals is that US firms are somewhat more optimistic that meaningful results can be achieved.

For the moment, China wants to be everyone's friend in the WTO—the OECD, the G-20, etc. At the same time, China argues that it paid when it joined the WTO back in 2001, so it doesn't need to make additional concessions. Looking at China's growing trade surplus and mountain of foreign exchange, no one outside Beijing is persuaded. China's position should change when the round approaches its climax, for two reasons. The strategic reason is that, of all major countries, China has the most to lose from the collapse of the WTO system. China's fast domestic growth rate depends on keeping its export engine running, which in turn requires an open world trading system. The mercantilistic reason is that China's trade barriers are already low compared with its peers (e.g., India and Brazil), so large percentage cuts in base tariff rates will translate into small changes in China's applied tariffs. Besides, contributing more than most developing countries would allow China to respond positively to protectionist pressures in Europe and the United States and would give China a political advantage in its relations with other developing countries.

One of India's priorities is to nourish its golden goose: offshore insourcing. Another Indian priority is to protect its generic pharmaceutical firms and a long list of monopoly service providers. All this translates into blatant mercantilism. Prime Minister Manmohan Singh has capped the more outrageous tariffs, but in multilateral talks, India's position remains faithful to an earlier age. Brazil is right alongside India, except that Brazil has a much wider list of offensive interests. For both Brazil and India, securing permanent seats on the Security Council is far more important than the Doha Round.

What Events Are Likely to Drive Negotiators in 2006?

Three things are likely: (1) Farm legislators and lobbies in the United States and Europe will try to preempt trade ministers by extending subsidy commitments and making them hard-and-fast guarantees, whatever comes out of the Doha Round. These efforts should, at the least, prompt more energetic trade negotiations. (2) A trade-weighted slide in the dollar (we are predicting 10 to 15 percent by December 2006) will modestly allay opposition to greater market access for manufactures and agriculture within the United States but will not make much difference to lobbies for the most sensitive products—textiles and clothing, sugar, and other specialty agriculture. However, if the dollar adjustment falls disproportionately on the euro because of Chinese and Japanese intervention, then the result could be a surge in European protectionism that could doom the round. (3) The absence of an economic, financial, or diplomatic crisis—as the world economy coasts along at 3 to 4 percent growth, as mergers and acquisitions activity thrives, and as the Iraq war winds down—coupled with pending elections in the United States, Europe, and Brazil will deprive the Doha Round of a sense of urgency.

What Are the Wildcards?

Delay means additional risk that trade talks get side-swiped by other developments. Three wildcards—possible but unlikely events—deserve mention: (1) A terrorist attack that involves international shipping or air travel, or pandemic flu that hits North America and Europe, would badly erode public support for trade negotiations. Moreover, new security and health measures would, for a considerable period, offset any negotiated liberalization. (2) A further spike in oil prices, say to $90/bbl or higher (perhaps driven by a face-off with Iran over nuclear weapons), is likely to push the world economy into recession and undermine trade negotiations. (3) Rampant China bashing in both the United States and Europe could provoke tit-for-tat trade retaliation, which in turn would disrupt the Doha Round.

What Happens if the Doha Round Slides to a Shallow Conclusion Late in 2007?

Here is what one of us (Hufbauer) said on October 30, 2003, in the Foote Lecture, delivered at the University of Alberta:

> Following the failure at Cancún, it seems all but certain that Doha negotiations will stretch into 2007. . . .The high likelihood that the Doha Round does not achieve [a significant outcome] does not mean that trade ministers will at some point declare a failure and go home. Career stakes in declaring a "success," no matter how shallow, are too great!
>
> But a shallow outcome will essentially mark the end of the WTO's 50-year run as the lead engine of commercial liberalization. Instead, liberalization will increasingly become the province of FTAs. The European Union and the United States will continue to offer agreements to small and mid-sized countries that are economically and politically attractive….
>
> Big questions revolve around the ways Japan, China, India, and Russia choose to play the FTA game. Will there be a China-Japan-Korea FTA? Will each Asian power form its own network? Will Russia negotiate a special arrangement with the European Union? What will be the foreign policy consequences of competing hubs? The fact that these questions are both big and troublesome does not, in my view, alter the forecast that regional and bilateral FTAs will take the lead on trade and investment liberalization at least for the next decade.

Based on the Hong Kong ministerial and the forces outlined in this policy brief, the forecast that bilateral and regional FTAs will become the engine of liberalization after the Doha Round still seems reasonable.