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Setting the Record Straight Free Trade and the WTO

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EXECUTIVE SUMMARY

Melbourne will host the East Asia Economic Summit of the World Economic Forum (WEF) on 11-13 September. The WEF is a Swiss-based foundation that monitors international competitiveness and networks with businesses around the world. Its annual meeting in Davos in February this year was treated to a scaled-down version of the Seattle demonstrations against globalisation. The Swiss authorities, however, showed less sympathy for the ragbag of complaints against globalisation and more resolve in restraining protestors than did the US authorities in Seattle. It is to be hoped that the Victorian authorities will be similarly disposed in upholding the law.

One of the striking features of the Seattle demonstrations was the range of accusations levelled against globalisation and the World Trade Organisation (WTO) for its part in it. Yet the complaints from participating non-government organisations (NGOs) showed little or no knowledge of the WTO agreements or how they operate. Worse, serious inconsistencies among the NGOs amounted to contradictions in the anti-globalisation coalition.

- Environmental lobbies regard trade and economic development as a threat to nature conservation and fear that their single-issue solutions will be rejected when governments are exposed to the benefits of global arrangements.
- Trade unions in manufacturing industries that have come under cost pressure from newly industrialising economies want to preserve old jobs and privileges and, above all, wage relativities. This is their argument for 'fair' trade.
- Cultural protectionists dislike foreign competition even though it gives people greater choice. This justifies trashing McDonalds, no matter how popular the fast food chains are with low income families.
- Development lobbies want more aid (which raises their incomes) rather than more trade (from which they gain no credit). Never mind which is more effective in overcoming poverty. Some even argue that trade is impoverishing, apparently because badly governed, centrally controlled and protected, small African countries are not keeping pace with open market developing economies.

The Seattle demonstrators shared a hatred of multinational enterprises, free trade and international cooperation, but had many differences. Their many objectives were not consistent, exposing deep divisions in the anti-globalisation coalition.

For example, attempting to enforce universal labour standards by applying trade sanctions could increase poverty in countries where labour productivity is still low. The poorest developing countries would be deprived of the opportunity to compete internationally if the labour unions' demands for 'uniform labour standards' were enforced.

Oddly enough, this danger did not seem to concern even the development NGOs in Seattle. Doubts about the justification for forcing outside standards, with their economic costs, on developing countries were absent. But such costs could be significant and could bring the present global prosperity to an end. Look what happened the last time sanctions and trade wars were practised in the early decades of the 20th century. What began with protectionism ended in the world economic crisis of the 1930s, mass unemployment and world war.

This paper will explain the role and record of the WTO (and its predecessor GATT) and attempt to correct some of the false assertions about it. One of the WTO's difficulties is that some of its member governments and many outside commentators want to enlarge its responsibilities (Robertson 1994: 108-119). Yet adding topics with only tenuous links to trade to the WTO's agenda was one of the main reasons why the Ministerial Council meeting in Seattle last December failed to launch a new Round of trade negotiations. Most media reporting from Seattle, however, focussed on the anti-globalisation demonstrations and did not address the problems of the Ministerial meeting itself.

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SETTING THE RECORD STRAIGHT ABOUT FREE TRADE AND THE WTO

The case for free trade is based on the benefits of voluntary exchange, the division of labour and individual freedom. As long as there are differences in the comparative costs of production between countries, trade will take place with mutual benefit to the participants.

At a global level, free trade promotes economic growth. It leads to job creation, forces companies to be more competitive and lowers prices for consumers. It also gives poor countries the opportunity to develop, owing to injections of foreign capital and technology, and, by facilitating the spread of prosperity, creates the conditions in which democracy may grow.

However, anti-globalisation protestors charge that trade liberalisation—supervised by the WTO—has undermined employment and wages in OECD countries, lowered environmental standards, increased disparities between rich and poor nations, and weakened democracy and national sovereignty.

The WTO is also accused of being supranational (its 'decisions' overriding national governments), untransparent (its decision-making processes being hidden from the public), undemocratic (ignoring NGO demands and minority interests), and is charged with 'marginalising' poor countries (anti-development).

These assertions are at best parodies of reality, but they get wide publicity and attention in the media. Clearly, ignorance of the functions, structure and decision-making of the WTO continues to drive the anti-globalisation coalition. Few even bother to look at the WTO agreements and procedures, or its history. The institution is guilty by association with globalisation.

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The facts about the WTO

Free trade has never been a specified goal of the GATT or its successor institution, the WTO, although trade liberalisation has been an important instrument in promoting economic growth since 1950. The establishment of multilateral trade rules to reduce trade conflicts and to lower commercial uncertainties has been achieved by introducing reliable and simple rules into the GATT-WTO. There are very good reasons for keeping the international trade regime simple: only simple rules are effective.

The WTO is built on the foundations laid by the General Agreement on Tariffs and Trade (GATT 1947). This was a contract (among 23 governments originally) to eliminate non-tariff barriers to trade and to liberalise tariffs progressively by negotiating reductions (concessions) based on reciprocity.

The principal rules since 1947 have been *transparency* of trade policies and *non-discrimination* in trade among members.¹ These multilateral trade rules are intended to facilitate international trade, but there is no commitment to reduce or remove tariffs over a specified period.

From the outset, governments were intent on preserving their sovereignty. Many exceptions are included in both the GATT and WTO agreements to protect national interests such as health and safety, national security, moral standards, natural resources, etc. Escape clauses also safeguard member economies from unacceptably disruptive imports caused by foreign subsidies, dumping or unexpected import surges. After amendments in the 1960s and 1970s, developing countries were permitted—almost certainly a mistake in retrospect—to increase trade protection to promote economic development (infant industries, balance of payments protection, public enterprises, etc).

The WTO agreements, which took effect in 1995, extend the basic GATT rules to cover trade in services, intellectual property and dispute settlement procedures.

Neither WTO agreements nor WTO rulings become national laws without domestic legislation. All WTO decisions are made by the General Council, which meets at the level of ministers or permanent representatives in Geneva. Decision-making is based on consensus as the WTO is an intergovernmental agreement. The rules agreed upon by all member governments constrain nationalist economic opportunism of the sort that did so much harm in the first half of the 20th century.

¹ Non-discrimination has two parts: (i) *most-favoured-nation treatment*, which requires that a specific import from any member country receives the same treatment irrespective of which member country it comes from; and (ii) *national treatment*, which means once an import crosses the frontier it receives the same treatment as 'like' domestic products (i.e. domestic taxes, industrial standards, etc.)

The WTO is not a supranational organisation. The Secretariat acts as directed by the Council, which in turn is responsible for all decisions and the wording of agreements. Any national policies not consistent with WTO rules can be taken to the dispute settlement body for arbitration if members cannot resolve the problem in discussion.

The reality of the WTO is therefore rather different from the following typical attack: . . . decisions affecting people's daily lives are being shifted away from our local and national governments and being placed increasingly in the hands of unelected trade bureaucrats sitting behind closed doors in Geneva . . . Once the WTO's secret tribunals issue their edicts, no independent appeals are possible. Worldwide conformity or continued payment of fines are required. (Ralph Nader, *Public Citizen*, December 1999)

WTO dispute settlement

The dispute settlement understanding (DSU) has given real meaning to WTO agreements because violations carry consequences for offending economies. Unlike the GATT provisions, where enforcement required unanimous consent of the Council and where a veto could block a decision, the WTO rules allow decisions on disputes to be implemented unless there is an unanimous rejection. A permanent appellate body reviews disputed panel rulings to establish consistent interpretations.

The environmental NGOs and the labour unions have taken a special interest in the WTO since they became aware of the DSU, as they believe it offers the potential to exert leverage in panel hearings and the appeals process. In other words, NGOs see WTO rules as opportunities to introduce new international standards for the environment, labour and other social issues. The allusion to international law also attracts NGOs, who cannot obtain sufficient support through legitimate political processes, notably parliamentary elections. International agencies allow them to seek power over national governments.

In its five years of operation, the DSU has been invoked almost 200 times. Only a quarter of disputes where consultations were requested have not been settled amicably; only a handful went to appellate body rulings.

The two major exceptions concern US complaints against the EU over imports of Central American bananas and over imports of hormone-treated beef. In both cases, the EU refused to amend its regulations to conform with WTO requirements and the US Administration introduced WTO-approved trade sanctions according to DSU enforcement procedures.

The problem with trade sanctions

Resort to trade sanctions has had two unsatisfactory consequences. First, if the trade sanctions ('suspension of tariff concessions' in WTO parlance) do not elicit a favourable response, trade protection rises. This contradicts the principal aim of the WTO, which is to reduce trade barriers. Applying trade sanctions is made difficult because they have to be non-discriminatory, which requires careful selection of imports originating predominantly in the offending economy. Nonetheless, such trade sanctions could stimulate retaliation with grave trade-reducing effects, though this has not occurred in the two cases mentioned.

Second, the use of trade sanctions to enforce DSU rulings has alerted NGOs to new opportunities to interfere in trade. Environmental groups and labour unions (plus some human rights activists) see scope for using discriminatory trade sanctions against countries failing to meet what they regard as appropriate 'standards'.

Environmental NGOs have sought to participate in panel hearings, such as the tuna-dolphin case and the shrimp-turtle case where the US Administration placed embargoes on imports of tuna and shrimp caught in ways that did not meet fishing standards required under American law. Both cases were lost, not because of the standards set, but because the measures discriminated against identified exporters according to the method of fishing.² This did not conform with GATT articles I and III. These decisions brought outcries from 'green' NGOs in the United States and demands to be heard in WTO panels.

² In both cases, the US authorities were not allowed to discriminate against selected foreign suppliers: *Tuna-dolphin dispute* (1991). Mexico complained about a US embargo on imports of tuna because dolphins were becoming trapped in tuna fishing nets in greater numbers than US tuna fisherman were allowed. *Shrimp-turtle dispute* (1998). Malaysia, Pakistan and Thailand complained about a US ban on shrimp imports. Imports were not allowed from countries that do not protect sea turtles.

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Advocates of international labour standards similarly aim to use trade sanctions to enforce compliance with 'international standards'. However, no OECD government has yet been prepared to confront the 100 plus developing countries in the WTO.

At the Singapore Ministerial Council in December 1996, member governments agreed that ILO 'core' labour standards should be observed. But it was also recognised that economic growth and development, fostered by increased trade and trade liberalisation, would promote these standards. The Ministerial Council therefore rejected the protectionist sentiment behind calls for labour standards and agreed that the comparative advantage of developing countries in labour-intensive production should be safeguarded.

There is no convincing case for complicating the WTO system by incorporating environmental or labour standards. To do so would not only undermine the developing countries' comparative advantage in labour-intensive production, but also reduce their wage rates and economic growth. Developing countries are opposed to both proposals. They do not want first world standards for the environment, labour, intellectual property, industry and social welfare if the cost is deeper poverty, slower growth and more dependence on OECD charity.

Anti-globalisation NGOs express concerns about the political rights of minority groups, including citizens of developing countries, yet the standards they demand are seldom helpful to the poor in non-OECD countries. Mexico's former President, Ernesto Zedillo, expressed this concisely after the Seattle meeting when he said:

A peculiar alliance has recently come into life. Forces from the extreme left, the extreme right, environmentalist groups, trade unions of developed countries and some self-appointed representatives of civil society, are gathering around a common endeavour: to save the people of developing countries from—development. (Referred to in Lukas 2000)

The threat to liberal trade

The prospect of the wide employment of trade sanctions has become a threat to trade liberalisation. Trade sanctions pervert dispute resolution by turning it into a process that raises protection, increases trade tensions and weakens the multilateral trading system. Trade sanctions also damage exporting economies as well as importing economies by raising the prices of import-competing industries to the disadvantage of consumers and, ultimately, export industries.

More significantly, trade sanctions conflict with the purpose of dispute settlement, which is intended to reduce trade barriers. In other words, trade sanctions are only effective if their use remains a threat. The game is lost if the bluff is called.

A much better approach would be to insist that those offending parties who refuse to conform with WTO rules should *compensate* the complainant with some unrequited tariff concessions. This would bring trade gains to both parties, as multilateral cuts do. The threat of trade sanctions establishes a community of interest in the offending country in favour of accepting a dispute settlement ruling (i.e. the exporters fear losses from sanctions); compensation would have the same effect on import-competing industries. These industries would face increased foreign competition from unilateral tariff reductions, and would lobby the government to amend the offending regulations.

The compensation alternative is recognised in the dispute settlement provisions. If it became the enforcement instrument of choice, the new temptation seized by NGOs to slow liberalisation and globalisation would be removed.

GLOBAL CIVIL SOCIETY OR CIVIL SOCIETY IMPERIALISM?

Representing a broad array of groups and lobbyists, the anti-globalisation coalition has adopted the term 'global civil society' because it suggests community service based on voluntary organisations. Nothing could be further from the truth. Although some NGOs are nationally based, they usually have international links and act internationally. They therefore lack the traditional obligations of citizenship and the legal status associated with 'civil society'.

Moreover, most NGOs are run centrally by small powerful elites and are unaccountable to their societies. They have failed to gain representation in parliament. In fact, the term non-government organisation is a misnomer because most NGOs are funded, at least in part, by government agencies. Their political stances are often disguised by well-meaning objectives, but exposed by the bullying mechanisms they use to achieve

their ends. Most are little more than single-issue lobby groups gathered into a coalition against mostly imagined enemies.

Trade liberalisation is one of these imagined enemies. Trade liberalisation has facilitated trade flows, but it is technological change that has been the driving force behind globalisation. The NGOs themselves rely on the revolution in telecommunications to coordinate their international protests. Do they really believe they can stop the benefits of globalisation from spilling into the global economy?

Transnational NGOs can be classed as either 'operational' or 'advocacy' groups. International organisations (WHO, UNEP, UNHCR, World Bank) and development agencies contract 'operational' NGOs to deliver services such as health care, education, famine relief, etc. 'Advocacy' NGOs seek to influence decision-making by governments and international agencies such as the WTO. Referring to 'global civil society' blurs the division, which suits the political activists. Their aim is to promote public participation and social change where their endeavours fail to do so through democratic processes such as voting systems.

Global governance

NGOs believe that a 'democratic deficit' has developed because globalisation has dispersed decision-making outside national borders. 'Global civil society' therefore advocates 'global governance'. This is no doubt why NGOs are welcomed within the United Nations (UN) family. The NGOs lobby national governments on behalf of UN agencies. This gives them status in the international community and allows them to pursue their political aims, which tend to match those of most UN officials.

In the case of the WTO, NGOs try to bolster their case for participation by misrepresenting it as an instrument of 'post-sovereign governance'. The WTO has been described as 'supranational, able to by-pass governments and to pursue global social and ecological objectives' (Scholte et al. 1999). No evidence is provided, but this propaganda allows the NGOs to present themselves as a 'countervailing force'.

The rise in NGO influence has been assisted by the unwillingness of national governments to confront them at home, passing them off as an international phenomenon. This has encouraged the NGOs to seek influence in intergovernmental agencies. Eventually, governments will have to confront the NGOs in international agencies, including the WTO, if they wish to retain national sovereignty.

Many national governments and international organisations are bullied into supporting environmental and labour NGOs. Unelected EC officials support single-issue groups in an effort to stall the liberalisation of trade in agriculture (Rabkin 1999). The EC gave financial support to Greenpeace to subvert the Kyoto negotiations by promoting a position on greenhouse gases that served European industrial interests (Kellow 2000).

The environmental lobby

Although most NGOs are committed to 'global governance and international equity', they often pursue nationalist protectionist policies. Yet demands for 'fair' trade, to give but one example, would only benefit trade unions in sunset industries at the expense of those in new industries.

Punitive trade policies designed to punish developing countries that do not adhere to the standards of high income countries would only increase the very gap between rich and poor nations for which the NGOs blame the WTO. This is best illustrated by the contrast between NGOs from developing countries and those that claim to promote development, and the environmental and labour NGOs.

The development NGOs divide around two traditional political poles. Most support economic reforms and improved access to OECD markets as the driving forces behind economic development in poor countries. They are inspired by the highly successful export-led growth strategies of East Asia, where real per capita incomes have increased by 4-6% per annum since 1960. And, indeed, research shows there is a clear correlation between GDP per capita and openness to international trade and development (Lukas 2000). Although some NGOs still argue that closed economies with central controls to promote import substitution and dependence on foreign aid can succeed, they can bring no evidence to support their case. African countries are the only ones still following their advice.

Environmental NGOs in OECD countries have been trying for many years to employ trade restrictions in their pursuit of environmental objectives. When the Uruguay Round Final Act (1994) led to the establishment of the WTO Committee on Trade and

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Environment (CTE), 'green' NGOs believed that they would be able to use trade policies to support their environmental goals.

One popular proposal involved the use of trade sanctions against countries with inferior environmental standards, but this ran foul of the fundamental WTO non-discrimination principle. Import restrictions on products that threaten a country's environment or health and safety are permitted. But this is different from the same international environmental standards being required of all countries. Uniform standards would not allow for differences in income levels, cultural and community priorities, climate and geography, demographic structures, industrial structures, etc. They would erode national sovereignty.

Legitimate transnational environmental differences should be addressed through global environmental agreements. Imposing trade sanctions on poor countries that do not comply with prescribed production methods or environmental standards would divert resources from development, which, perversely, would increase pressures on the environment.

The right to national self-determination of health, safety and environmental standards does not only apply to OECD countries but to all WTO members. Because economic progress raises living standards, it also tends to raise national environmental standards as more resources can be devoted to reducing environmental degradation. Using trade sanctions as a punitive instrument would reduce trade and growth, and probably increase environmental damage.

The labour lobby

Linking labour standards—i.e. uniform conditions of employment—to WTO sanctions would increase protectionism. Labour unions in rich countries with declining industries do not try to disguise this basic fact. In OECD countries, the case for uniform labour standards is presented in two ways: either as a means to overcome 'unfair' trade because low-wage labour undercuts OECD production costs, or as low-wage labour holding down the wage levels of unskilled labour in OECD countries, thus increasing income disparities.

Since the International Labour Office (ILO) is already charged with raising labour standards around the world, the only reason to introduce labour standards into the WTO is to gain additional leverage through trade sanctions. Yet raising trade restrictions against labour-intensive exports from poor countries will not help the workers in those countries, many of whom would lose their jobs and be forced into even deeper poverty.

Similarly, those who seek to drive children from the workforce by using trade sanctions would lower family incomes and drive the children into prostitution or scavenging, and even premature death. There are seldom schools for these children to attend. Besides, most child labour is used in the non-traded sectors of the economy, which makes trade sanctions unlikely to be effective.

Implementing labour market reforms (minimum wages, health insurance, limits to working hours, rights of association, use of child labour, etc.) depends on raising living standards and productivity. Only that way are surpluses produced to finance social reforms. OECD studies have shown a positive association over time between sustained trade reforms and improvements in core labour standards (OECD 1996).

The safest and surest way to promote labour standards in non-OECD countries is for OECD countries to remove all trade restrictions on labour-intensive imports. Yet these are the sectors where tariffs (and quotas) are still the most restrictive, because liberalisation would require adjustments from the workers and the unions. To prevent such structural adjustments, unions pursue labour standards in the WTO.

The cultural lobby

Protection of national or regional cultures is another reason for NGO activism. Cultural lobbies were an important force behind the French government's withdrawal from the OECD negotiations on the Multilateral Agreement on Investment (MAI) in 1998 after it orchestrated a worldwide internet campaign among client lobby groups (Henderson 1999).

Protecting 'national cultures' (arts and languages) provides another reason for attacking globalisation. These concerns are evident in several WTO committees, including GATS (audio-visual) and TRIPs (native species). Trade in services depends much more than merchandise trade on the nature of domestic regulations and institutions. This means that liberalising trade in services offers high returns in terms of efficiency. But the

converse is that domestic suppliers earn high protection rents; they therefore oppose liberalisation.

THE WTO IN NEW CIRCUMSTANCES

The WTO is facing a new political landscape, not least because NGOs have identified new political opportunities. The anti-globalisation coalition's attack on the WTO in Seattle and subsequent criticisms of the failure of the Ministerial meeting from WTO supporters have forced a review which is now stretching the organisation's slender resources. Member governments seem unable to decide on priorities and there seems to be little enthusiasm or commitment on the part of international bureaucrats to respond to the attack on them by 'global civil society'. Indeed, political concessions to NGOs as well as tax-funded subsidies to the anti-globalisation coalition are already worsening tensions in the WTO.

In addition, multinational enterprises (MNEs) are showing less interest in the WTO, probably because liberalisation has left few barriers to their trade and investment activities. Large MNEs can usually negotiate bilaterally with potential host governments without the need to wait for multilateral agreements.

At the same time, the new WTO agenda and the growing activities of NGOs mean outspoken MNEs risk becoming victims of NGO campaigns of 'naming and shaming' aimed at enforcing corporate social accountability. For all these reasons, business support for liberal trade has declined. This loss of interest by the business community relieves the pressure on governments to pursue trade negotiations just when NGOs are pressing their anti-globalisation programme.

Worse, a rift is now opening up between developing countries and the OECD. In fact, developing countries are already complaining—with good reason—about the slow progress towards implementing the Uruguay Round Agreement on Textiles and Clothing by 2005. They are also very wary of the new trade-linked proposals coming from 'global civil society'.

Counter-attack

A first step for the WTO under this anti-globalisation threat is to launch a new Round of trade negotiations to fill some of the gaps that NGOs are trying to exploit. The agenda for the new Round should be made manageable by removing many of the controversial new issues. The 'built-in' agenda from the Uruguay Round—covering agricultural trade, trade in services and reviews of specific agreements, including dispute settlement—provides a good basis for negotiations if industrial market access is added.

To reassure developing countries, the OECD governments will have to begin confronting NGOs over their more provocative proposals in order to discourage resort to mercantilist instruments such as trade sanctions. Yet a number of major governments are preoccupied by domestic political matters. These include the internal EU conflicts over enlargement of its membership. As the WTO is only an intergovernmental agency, it is national governments that determine the WTO agenda. At present, regional trade blocks and NGOs are making the running.

Regional trade agreements are now so widespread that multilateral agreements have become little more than the foundation on which to build these complex arrangements for regional integration, including 'harmonisation' of national policies (for example, cooperation among competition authorities, mutual recognition of industrial standards, common environmental standards, social policy harmonisation, etc.).

These processes strengthen interventionist bureaucracies like the European Commission. As international negotiations become more technical and specialised, national bureaucracies also grow. Once an accord is achieved among the 15 EU countries (often with general consent from associated countries) there are obvious political gains from seeking to extend its scope beyond the EU.

This is evident in present EU proposals for the WTO agenda to include investment rules, competition policy and the 'precautionary principle' for the environment. The latter was set out in the Rio Declaration (1992), which stated that '[i]n order to protect the environment, the precautionary approach shall be widely applied by States according to their capabilities. Where there are threats of serious or irreversible damage, lack of full scientific certainty shall not be used as a reason for postponing cost-effective measures to prevent environmental degradation.' Now the EC has proposed that this should be

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adopted in the WTO, and should allow for socioeconomic risks and consumer opinion. Environmental NGOs are supporting this.

Yet there is no compelling case to include investment rules or national competition policy on the agenda. Introducing the 'precautionary principle' in WTO deliberations on the environment or attempting to find a new agreement on biodiversity would also be unwise when so many questions remain unanswered. In any case, developing countries have other priorities. Moreover, the 'precautionary principle' would be a blank cheque for opportunistic interventionism by NGOs, which would quickly undermine WTO agreements.

NGOs favour bureaucratic approaches. After all, lobbyists do not thrive in transparent markets. The larger the negotiating group, the greater their chance of being included. This is consistent with their commitment to 'global governance' built around the UN model.

The present agenda of the WTO is loaded with issues that lend themselves to the bureaucratic approach and large committees. This alone should convince WTO supporters that the agenda needs to be pruned and some subjects diverted elsewhere. The first task should be to remove outstanding weaknesses already identified in the multilateral trading rules and to improve enforcement procedures for dispute settlement.

Conclusion

The WTO is no longer a simple trade contract. Social issues have been allowed onto the WTO agenda using tenuous links to trade policy. In this way, the WTO Council has placed the organisation in the vanguard of political skirmishing over globalisation. Multilateral trade rules remain important, but new political forces are now in play.

As a medium-sized OECD economy with little bargaining power, and buffeted by the revival of protectionism in Europe, Japan and the United States, Australia depends on multilateral rules to protect its trade interests. Australia's participation in a strong WTO and an increasingly integrated global economy provides support for national independence and should not be sacrificed to lobbying by NGOs.

The WEF meeting in Melbourne this month seems like a good place to begin a counter-attack against the anti-globalisation lobbies. Speakers at the WEF forum should emphasise the benefits of globalisation and the great lesson of the 20th century: that liberal trade promotes prosperity and that meddling with the principles of free trade can easily trigger economic stagnation and the cataclysms that follow from economic despair.

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