Trading in the 21st Century: Is there a Role for the WTO?

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As the World Trade Organization begins its third decade, its future is less certain than at any point in its history. While there is no move to dismantle the organization, the initial expectation that the WTO would be the fulcrum for future international trade agreements has not been met. At best, we can say that its tenure has had mixed results. On one hand, the organization continues to be an adjudication focal point, with nations using panel processes when there is contestation over rule interpretation. But more problematic given the function of the organization, the legislative arm of the WTO is moribund. If we were to compare the first two decades of the WTO with that of its predecessor organization, the General Agreement on Tariffs and Trade, the WTO would appear lackluster. This essay examines the scholarly literature on the trade regime and argues that this pessimism may be misplaced.

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As the World Trade Organization (WTO) begins its third decade, its future is less certain than at any point in its history. While there is no move to dismantle the organization, the initial expectation that the WTO would be the fulcrum for future international trade agreements has not been met. At best, we can say that its tenure has had mixed results. On one hand, the organization continues to be an adjudication focal point, with nations using panel processes when there is contestation over rule interpretation. But more problematic given the function of the organization, the legislative arm of the WTO is moribund. If we were to compare the first two decades of the WTO with that of its predecessor organization, the General Agreement on Tariffs and Trade (GATT), the WTO would appear lackluster. What happened? And was this predictable from the scholarly literature?

This essay examines the WTO, its history, and its relevancy today to our understanding of trade agreements. The review concludes on a more optimistic note than often found in the contemporary press. WTO members, on the whole, have resisted protectionist pressures, which have risen substantially in recent years and by and large, have complied with their formal agreements. As so, we may want to think of the WTO as "insurance," in that membership protects against ad hoc changes at the border. Still, there should be no expectation that there will be a new global agreement to deepen liberalization from the organization. It is this lack of momentum, even given continued effectiveness of the WTO, which is the puzzle addressed below.

The essay is divided into three parts. Part one addresses the political consequences of GATT/WTO membership, focusing both on the rules and norms of

the regime and the explanation for why they have become less functional over time. Part two looks at the effectiveness of the WTO and the dispute settlement system in encouraging trade and compliance with agreements. Section three concludes with some general thoughts on the impact of shifting mass opinion on the virtue of trade agreements and other stumbling blocks the WTO faces.

A number of general points motivate the essay. First, looking at the literature, too few scholars have paid attention to the negative distributional effects of trade agreements and how that interacts with constraints on policy making in member states. As the 2016 US presidential election has shown, trade policy is an easy target for demagogues in part, because the idea of comparative advantage is one of the more opaque ideas to come out of economics. But it is more than the complexity of trade theory that has undermined support for trade. As Robert Driskill (2012) has observed, even economists who are trained to ask questions of trade-offs, treat the promises of free trade "akin to a zealous prosecutor's advocacy of a point of view" (3). And while it may be excusable to have the economic discipline focus solely on the aggregate welfare benefits of free trade, political scientist should be more cautious, given the discipline's focus on distributional effects. Open markets may be good in the aggregate, that is, for the nation as a whole, but global forces are not kind to every individual. We need to better understand the more micro effects of trade agreements in order to understand when and why the WTO, and its agenda to further reduce impediments to trade, is supported by member nations.

Second, the focus on dispute settlement finds that while the WTO may have failed to legislate deeper trade agreements, it has been active in creating a forum for

dispute adjudication. This has spurred a robust debate about the WTO as an international court, adding significant knowledge, and some optimism, to the possibility of solving disputes without endangering trade. Yet, the success of the courts may well be related to the failure of the legislative process. As nations fear an inability to renege in hard economic times, they become wary of signing new agreements that may be difficult to adhere to. The result is an efficient court and a broken legislative system.

Third, trade policy-making is a two level game: nations cooperate in order to increase their aggregate welfare but the form and extent of cooperation reflects the aggregation of domestic political interests. These domestic interests vary across nations, both a function of their specific endowments and the incentives of social groups to organize. Political and economic analysts approach the "game" somewhat differently and in fact, Donald Regan (2015) has argued that the two approaches are contradictory. Political analysts, he argues, see trade agreements as a way to undermine political support for import competing groups; the reigning economic theory of trade agreements, by comparison, focuses on terms of trade manipulation. The difference, he says, is significant because in one, the purpose of tariff protection is to "affect domestic relative prices, in response to special-interest politics, [while] terms of trade manipulation aims to affect world prices, to increase national income" (393). While not agreeing with this sharp distinction, this essay chooses to set aside the terms of trade explanation for the WTO and instead, focuses on the interaction between international rules set by the trading regime and the domestic preferences of signatories. As such, some economic literature, especially literature on rent

seeking of domestic groups are considered (e.g. Grossman and Helpman 1994), but given the extant attention to terms of trade issues, we will leave that debate to economists.[1]

We begin with the observation that from the earliest days of the trade regime, finding a majority coalition in support of open borders was problematic for the member states of the WTO. The problem is that the distribution of social preferences is often more parochial and nationalistic than assumed in economic models (See Milner and Kubota (2005) for an alternative perspective). Even in the US where there has been a common understanding that very high protective walls is bad for the economy, there has never been a consensus on free trade being the replacement policy. In this sense, the GATT/WTO system has always had tenuous roots. To the extent that open markets were assumed to lead to growth, and export interests remained powerful, nations were willing to cooperate on trade agreements. Today, not only is the pro-trade coalition harder to assemble but also, there is far less confidence that more openness, will in fact, lead to more growth.

The result has been a legitimacy crisis for the WTO. Debra Steger (2007), the first Director of the Appellate Body Secretariat of the WTO, has called for "major surgery in order [for the WTO] to respond effectively to the new political realities in the international economic system" (495). T.N. Srinivasan (2005), long an advocate of open borders, has commented on the archaic nature of the nondiscrimination principal in the WTO, which, he claims, is touted as a fundamental principle while in practice, is rife with exceptions. Gowa and Hicks (2012) find the principle

[1] For an exhaustive review of the economics literature, readers should see Bagwell, Bown, and Staiger (2015).

problematic and in fact, argue that it was never universalized and Esty (2002), suggests that no matter the rules, there is a fundamental legitimacy problem with the WTO that can only be solved via an expanded mandate into a set of fundamental economic issues, ranging from poverty alleviation to public health. Political support has waned over time. Why?

The Rules and Norms of the Trading Regime

The fundamental goal of the trade regime is to increase the flow of goods and services across borders. To achieve that goal, members have focused on regularizing and minimizing border restrictions. As well, and more recently, the WTO has regulated aspects of trade that are "behind the border." Legislating occurs episodically during Rounds of trade talks. Since the WTO's creation, there have been no successful Rounds. This is not to say that the system is totally broken; as a forum for discussion, the WTO continues to tackle trade problems although larger issues, such as the current query of whether or not China is an open economy and how, for example, that influences dumping margins, are stumbling blocks. Legislating is difficult, in part, because of a consensus norm. As the number and type of nations that entered the WTO expanded, interests diverged and consequential issues languished. To explain why the organization chose a consensus norm as well as most contemporary trading rules, we need to return to the WTO's predecessor, the GATT. The WTO incorporated the GATT into its text; and those GATT rules arose from a specific set of historical and political constraints that faced the organization's founders, and in particular, the United States.

Where did the rules come from? The explanation begins with US politics in the interwar years. In 1932 a new majority Democratic Party inherited a high tariff wall, a remnant of the 1930 Smoot-Hawley tariff. Recognizing that the closure of the US market to European goods contributed to an ensuing disorder in international financial markets and job displacement for their constituents, the traditional party of Southern exporters sought a change in policy. But given that party control in the US is ephemeral, the new majority sought to guarantee their preferred trade policy against future legislative log rolls. Their method of assuring open trade in the Reciprocal Trade Agreements Act (RTAA) in 1934 was to shift institutional responsibility for trade treaties to the Executive branch (Bailey et al. 1997; Goldstein and Gulotty 2014). The form of this delegation to the President, however, was less radical than is often portrayed. Some scholars have argued that delegation removed Congress from tariff setting (Haggard 1988); it is more accurate to see delegation as a change in form, and not a loss of control.

In the RTAA the President was given a "first mover advantage" in that he had authority to negotiate trade agreements, but the process was constrained by, and in the shadow of, congressional oversight. Legislation specified the upper limit of tariff reductions and a fixed period in which he could negotiate. As well, Congress specified exactly how the reductions could occur. Treaties needed to provide most-favored-nation (MFN) treatment, and all tariff cuts needed to be met with reciprocal reductions by the other nation. Further, any product subject to negotiation had to be authorized prior to negotiations, and those negotiations had to be focused on the principal supplier of the good. Delegation required regular renewals, forcing the

Executive to return to Congress to report on trade agreements and to ask for continued authority. To assure renewal, the President needed to maintain a pro-trade coalition in Congress, which was in no way assured. Mindful of the need to show results, the State Department worked diligently and was able to conclude 38 agreements.

As WWII entered its last phase, the US was also involved in talks on a more inclusive body, the International Trade Organization (ITO) that was to be an international organization regulating most aspects of commercial policy. In parallel and interrelated, the President continued to ask for congressional approval of his tariff setting authority. But the timing was off; fearing political resistance in the upcoming 1948 renewal discussions, the State Department wanted earlier tariff talks in order to legitimate an expansion of negotiation authority. Attempting to finesse the timing issue, the US had gained acceptance for an Interim Tariff Committee at the ITO's London Conference. Under that umbrella, the US invited a set of other nations in 1946 to meet in Geneva to conduct bilateral tariff negotiations. Twenty-three nations came to Switzerland and over a nine-month period were able to agree to reduce particular tariffs. At the completion of the talks, a set of rules was attached on top of the new tariff schedules. This became the GATT.[2] While thought at the time to be an interim agreement, the failure to create the ITO made these

[2] There were some differences between the GATT 1948 and the RTAA treaties. Reflecting the ITO talks, not part of the RTAA and in the GATT were: a prohibition against preferences on all articles (not the particular ones in the bilateral agreements); export taxes were prohibited; national treatment was extended to imported articles; there were more narrow rules on antidumping and countervailing duties (an injury criteria was included); there was an expansion of the details on nullification and the escape clause; there were new exceptions for balance of payments reasons, to create customs unions, and economic development. See Barton et al. (2006).

rules, which were modeled on the 38 earlier US agreements, the backbone of the trade organization until the WTO's creation.[3]

What explains the choice of rules that were institutionalized in the new GATT? Each was a rational response to a political problem faced by Congress at the time. The *principal supplier* rule purposefully focused negotiations on low cost producers. But the principal supplier rule was not only about prices; it served the political function of providing, ex ante, information to legislators on whether or not products in their district would be in the reciprocal bundle and subject to import pressures. *MFN* merged America's multilateral aspirations with the principal supplier rule by assuring producers and their congressional representatives that MFN, which increased the potential entrants into the US market, would not lead to deeper price competition. Finally, the *reciprocity* rule assured equity in swaps but more importantly, it motivated exporters to political activity.[4] In the past, few exporters had mobilized on tariff issues, creating a pro-protection bias. Bundling

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[3] The ITO was never ratified by Congress and so the GATT, which would have been Chapter V of the ITO charter, became the de facto organization dealing with international trade. Initial GATT participation was legislated as RTAA renewals in 1948, 1949, 1951, 1954, 1955, 1958 and 1962.

[4] The 1934 Act and subsequent renewals stipulated very clear procedures for vetting potential product cuts. According to legislation, the President needed to seek advice from the Tariff Commission, the Departments of State, Agriculture, and Commerce and from all other appropriate sources before lowering a tariff. To accommodate this mandate, a series of committees, the Trade Agreements Committee, country-specific committees, and the Committee for Reciprocity Information, were assembled to give interested parties the opportunity to present views. They took briefs and held public hearings. Until 1937, a formal announcement of intent to negotiate was accompanied by a list of the principal producers who could potentially get a tariff cut; afterward, this was later replaced by the "public" list, which signaled all items that were under consideration in any negotiation. The 1934 Act also dictated the form of tariff setting. All agreements were bilateral with some foreign government and although treaties had only two signatories, their effect extended beyond the two nations. After 1923, the US was bound by Executive Order to grant MFN privileges to its trading partners. Also, the Executive was bound by law to negotiate *reciprocal* agreements, extending to parties withdrawing from the treaty.

import cuts with export access allowed congressional representatives to advocate for the broader interests in their districts.

Reciprocity, MFN, and principal supplier based negotiations were well entrenched by the time the US began talks on the trade regime and thus it isn't surprising to see them in the early documents from the wartime conferences on the future of global trade (*Chapter III of the First Session and Chapter IV of the Preparatory Committee's second session report*). In these sessions, the US demanded, that tariff talks mimic the RTAA process, that is, that reductions would be reciprocal and thus mutually advantageous and MFN apply to both reductions in general and reductions in preferential rates. Negotiated rates would be bound and if reneged upon, would need to be compensated in some other part of the tariff schedule. Exempted from these rules were previous preference agreements—they did not have to be granted MFN privileges. These included not only the British Imperial system but also Cuban-American preferences.

There was a fourth US contribution to the GATT framework whose importance is often overlooked, that is, the accounting system used for reciprocal deals. In the GATT, reciprocity mandated that all trade deals be bilaterally balanced; because of the MFN rule, their effect was multilateral. The process of agreeing to a bilateral cut was iterative—nations produced a list of products on which they wanted their trading partner to grant them increased access, and the other nation responded with a list of offers of access. The two then sat down to balance what each wanted and received from the other. When a deal was struck, the nation received what was called an initial negotiation right (INR). The INR was a property

right, derived from the original concession. If a nation rescinded on the bilateral deal at any time after the negotiations, the holder of the INR could demand that the other nation make them "whole" via a reduction on another product of equal value to their exporters. While third countries could be compensated, it was the original holder that had the guarantee. These INRs created an unexpected path dependency, privileging prior partners over later negotiators. On one hand, the INR system stabilized deals, making it more difficult to renege; but as well, it skewed the products and nations who held a "property right" and thus an investment in the GATT system.

These rule choices had long lasting effects and ironically, the features that explain early success became the Achilles heel of the WTO. Shifting patterns in both the direction and the type of world trade had the unanticipated effect of generating political challenges for the organization. What was good for the domestic politics of the creators became counterproductive as the organization grew for three key reasons.

First, the GATT was mindful of the domestic constraints faced by leaders in committing to market liberalization. This attention to domestic politics was eroded by the WTO. In the GATT, nations were provided with many ways to renege and centralized decisions were stipulated to be only by consensus. The "weakness" of the central regime was viewed positively by then current and potential members, and encouraged expansion. And while each subsequent member of the GATT/WTO created a positive network effect making membership even more valuable, the organization itself became less of a club of like-minded democratic nations (Gowa

and Kim 2005). Over time and as a result of the success of prior agreements, international trade moved from manufacturing items to services, and from commercial transactions to foreign direct investment. Nations' interests diverged. As behind the border policies replaced the earlier negotiations over border measures, non-governmental actors, such as labor and environmental groups, increasingly turned their focus on GATT/WTO policies. NGOs participated independently and through national members, increasing the difficultly in crafting a consensus among the voting nations, even around technical issues.

Shifting interests of the members increasingly divided along North-South lines, especially with regulatory harmonization after 1995 and the inauguration of the WTO. The new rules often required fundamental change in the domestic legal and regulatory regimes of the developing member states and were unpopular in their national capitals. And, as the rules became more demanding, compliance expectations grew, in part because the end of the Cold War fueled ideological fervor in those who supported free markets. This expanded commitment to open markets then made salient the counter to pro-trade argument that harmonization was leading to a "race to the bottom." By the end of the century, labor and environmental groups had all turned against the WTO. From the perspective of leaders in national capitals, the WTO appeared to have turned a "deaf ear" to the changing political landscape they faced at home.

Second, the new entrants to the regime rejected the fundamental norms of the system, pushed by the US, that was the backbone of early cooperation. As a negotiating system, the use of reciprocity for most of the 20th century was based on

a mercantile notion of trade, that is, trade deals were bilateral and composed of equal swaps. Specific reciprocity and balanced bilateral trade is not a concept that adheres to basic notions of comparative advantage. Reciprocity with MFN, however, is diffuse—with the MFN rule, one's partners may be viewed as a group and there is less of an emphasis on equivalence (Keohane 1986, 4). Specific reciprocity limits the range of possible trade swaps; diffuse reciprocity, as encased in MFN, is more inclusive, because it requires "a widespread sense of obligation" (20).

From the start, parties to the GATT needed to believe in the underlying goal of universalizing trade deals, even though they sought reciprocal swaps during negotiations. This belief was never universalized and by the 1960s, both the use of specific reciprocity in trade Rounds and the expectation of diffuse reciprocity in access to markets had been rejected by the developing world. At the request of the emerging market nations, Part IV of the GATT was legislated, stipulating that a set of member nations were no longer expected to give access to other GATT members' imports in return for access for their exporters. Further, a subset of nations now claimed a need for differential and special access to other members' markets, greater than that given to other regime members. But, even in the absence of the "revolt" from the developing world, MFN would have become problematic as the organization moved into the realm of domestic regulatory harmonization. If nations harmonized on strict standards, the developing world balked; if there was standardization at lower levels, there was a cry of race to the bottom.

As problematic for harmonization attempts in the latter part of the 20th century was Article III of the GATT, which specified national treatment. While in

origin, national treatment was to be a guarantee of non-discrimination, it undermined the internationalization of production standards. Since the use of domestic taxes and/or regulations as a form of protectionism was illegal, it encouraged nations to use standards to influence investment and trade patterns. In practice, it was hard to compare products; some nations began to give imports an advantage not given to domestic producers in order to incentivize foreign direct investment (FDI). While a somewhat simple concept, that is, the prescription to treat all products, domestic or international, in the same manner, national treatment or "inland parity" proved unworkable in practice.

Third, the founders of the WTO and the GATT had very different beliefs about the optimal specificity of trading rules. The GATT's founders sought "thin" and ambiguous rules; imprecision created space for countries to placate powerful domestic groups, when necessary, without endangering their general commitment to the regime. For the first 40 years, disputes were most often settled without formal procedures, a reflection of a shared vision of the purposes of the organization. The GATT was purposefully a "member driven" organization with a small and ineffectual secretariat—centralization and authority at the center of the regime was not what the founders wanted.

Over time, flexibility became a problem. It granted new members license to ignore the spirit of the rules. It encouraged "grey area" responses to problems, such as voluntary export restraints (VERs), so as to accommodate the needs of members. The fundamental rules of the system became rife with exceptions. It is not surprising that the response to this shirking in 1995 was to re-legislate in order to

more clearly specify rules and then relatedly, make it more difficult to break an agreement. From the perspective of the reformists, and in particular, the US, Canada, and the EU, it was the other members of the regime who were out of compliance, not them. As a result, there was consensus among the larger nations of the need for a more robust organization and the WTO treaty was, in fact, more specific, stricter and mandated universal adherence. But there was an unanticipated effect. Even the early supporters found themselves in court over rule violations and rule specificity and mandatory dispute settlement created a fear of signing onto any new agreements. Legislating trade liberalization ground to a halt.

Assessing Success

How well has the trade regime's rules and norms served the function of trade liberalization? To better assess the underlying rules and norms, two aspects of the regime's effectiveness are considered below. First, the literature on the WTO, trade barriers and trade flows is examined. Second, a very lively debate on how to assess the dispute resolution system is considered.

Trade Barriers and Trade Flows

Trade barriers today are at historic lows. While nations, including the US, continue to have heterogeneity in their tariff structure, overall, the average tariff of trading nations has been dramatically reduced in the post WWII era. Focusing on tariff reductions, we see three different patterns in the degree of openness of WTO members. This pattern holds for non-tariff barriers as well. High-income nations

have average MFN tariffs that are low and bound; the emerging nations have higher rates but the rates are mostly bound; the developing world has rates that are higher and less of the rates are bound (see Table 1). The US, as an example of the first category, has a tariff average slightly above 3%; only Australia among the high-income nations has a lower average tariff. India has the highest average tariff at about 14% among the emerging economies, and retains a number of unbound rates. In the developing world, the tariffs vary dramatically, from a low of 6% for the Philippines (with 67% bound) to 17% for Egypt (99% bound). Both reductions and binding of tariffs are consequential. Binding provides predictability—insurance that the tax would not capriciously be changed. Reviewing Table 1, it is apparent that while the 21st century is not about free trade, the world is far more open than at the inaugural meeting of the GATT. But still, how much of world trade today was made possible because of the creation of the GATT/WTO? On this question, there is much disagreement.

Until 2004, most analysts assumed that GATT/WTO membership explained both the liberalization of trade in the postwar years and the resultant increase in bilateral trade. In that year, however, Rose (2004) penned a paper that suggested that membership was, in fact, not consequential. Using the value of bilateral trade from 1948 to 1999, and controlling for a host of factors in a gravity model, Rose found that while some factors were associated with the level of trade (such as membership in a currency union), GATT/WTO participation was not.

The Rose paper elicited much attention to both the method and its findings. Subramanian and Wei (2007) re-ran the data and with a slightly different data set

and a tweak to the model, argued that membership in the GATT/WTO did account for an increase in world trade, by about 120 percent. They did acknowledge, however, that the increase was not uniform.[5] Goldstein et al. (2007) and Tomz et al. (2007) also puzzled by the findings re-ran the Rose data, using the same method but adding trade data from the pre-GATT days and including trade for nations that participated in the GATT while still part of a colonial structure. The expansion of the data set was consequential, and now the GATT/WTO had a positive and significant effect on bilateral trade. Gowa and Kim (2005) also find a positive effect of the GATT on trade, but the increase is specific to trade between five states: Britain, Canada, France, Germany, and the United States. Instead of seeing the GATT/WTO as having universal effects, they argue that the benefits were only for a privileged group of members. And most recently, Allee and Scalera (2012) look again at the data and find that countries that undergo rigorous accession processes are the nations more likely to experience an increase in trade flows.

Other scholars suggest that the WTO increases trade volume as a result of oversight by the dispute system. Bown (2004), and Bown and Reynolds (2015) examine variation in the outcome of specific dispute cases and trade flows; Bechtel and Sattler (2015), employing a matching approach, also find a positive effect of dispute settlement on bilateral trade, in fact, for both for the main participants and third parties. On average, Bechtel and Sattler (2015) claim that sectoral exports

[5] The datasets are different. Rose uses the average of import and export as the dependent variable; Subramanian and Wei only use import data. Subramanian and Wei include country fixed effects in all of their models; Rose does not. Subramanian and Wei assume a hierarchical relationship among other trade agreements, in which the effect of the GATT/WTO would be inconsequential in the presence of free trade agreements (FTAs) and the generalized system of preferences (GSP) and so code a country pair as a WTO member only if the two countries are not part of the same FTA or GSP.

from complainant countries to the defendant increase by $7.7 billion in the three years after a panel ruling, as compared to similar pairs of countries that did not undergo dispute settlement, which is not statistically different from the gains obtained by third parties. At the same time, exports to the defendant from pro-complainant third party countries, increase by about $6 billion, as compared to neutral third parties. Not only is the dispute system assuring the flow of trade but also, they suggest that the dispute decisions have a spillover effect on third, and often smaller, nations.

On the other hand, Chaudoin et al. (2016) report less promising results on disputes and trade flows. Rather than examining the relationship of dispute and trade at the dyadic level, they look at trade in disputed products from WTO members to respondent countries and disentangle the various categories of dispute settlement.[6] They find that import values in respondent countries increase by less than 10 percent after a dispute, which is not statistically significant with country-year fixed effects. Only in cases that have been withdrawn do they find an increase in import values; disputes do not consistently and robustly increase trade flows when controlling for dispute characteristics, such as issue area, and country-specific respondent characteristics.

As well, a set of scholars has suggested that membership may affect economic behavior more broadly. Carnegie (2014), for example, argues that membership can forestall a hold up problem between politically dissimilar pairs of countries. Employing a log-linear gravity model of trade, she asks whether the effect of WTO

[6] The dispute is broken into five categories: pre-dispute (baseline), ongoing, mutually agreed, withdrawn, and panel ruling.

membership on trade is greater for dyads that are politically dissimilar, as measured by the difference in capability (power) and regime type and by their alliance status, relative to similar pairs of countries. Under different model specifications, her main finding—that WTO membership increases trade most for dissimilar country dyads—consistently holds. She further tests the causal mechanism by examining the effect of WTO membership on trade in goods that are contract-intensive and on fixed capital investment, areas in which political hold-up problems are most likely to occur.

Carnegie's findings support the idea that the WTO successfully constrains members from using trade policies as political leverage. Büthe and Milner (2008) find a similar virtue from signing any trade agreement. They suggest that trade institutions convey member states' commitment to liberal economic policies, mitigating time inconsistency problems and thereby increasing the flow of foreign direct investment. Membership reassures investors, and the monitoring and compliance mechanisms of the trade agreement raise the reputational costs of a violation. Their empirical findings show that the GATT/WTO and PTAs are positively associated with inward FDI, and the finding holds under different robustness checks, including an instrumental variables method.

As well as influencing FDI because of this reputational and information link, membership has been shown to constrain behavior in other domains. Simmons (2000) explores the link between monetary and trade policy through a study of Article VIII obligations of the IMF. With respect to GATT membership, she hypothesizes that the "GATT might encourage a country to maintain free and

nondiscriminatory foreign exchange markets" (596). She finds that GATT membership is negatively correlated with violations of Article VIII obligations, but the effect is not statistically significant at conventional levels. In a more recent study, Copelovitch and Pevehouse (2013) re-examine a potential link between GATT/WTO membership and exchange rate policy choices and like Simmons, cannot find empirical support for the connection.

The relationship between WTO membership and the signing of a PTA is explored in numerous papers and with different conclusions. For example, Tobin and Busch (2010) employ a rare events logistic regression on a propensity score-matched dataset of 132 low- and middle-income host countries and 23 developed partner countries, seeking to explain PTA formation, controlling for GATT/WTO membership of the host-country; Mansfield et al. (2002) also include GATT membership in exploring the effect of democracy on PTA formation during the period from 1951 to 1992. Contrary to the insignificant result found in Tobin and Busch (2010), Mansfield et al. (2002) find a statistically significant, positive effect of dyadic GATT membership on PTA formation. In a later paper, the reason for the relationship between GATT membership and PTA formation is explored (Mansfield and Reinhardt 2003).

While there are convincing quantitative studies suggesting different degrees of GATT/WTO effect, there is still a lack of clarity of when and how the effect is manifest. As a result of a declassification of data on the specifics of trade Rounds, a number of recent papers address this lacuna, beginning to provide these micro-foundations. Bagwell, Staiger, and Yurukoglu (2015) in an intensive study of the

1950 Torquay Round, connect the GATT's negotiating rules with a specific pattern of tariff reductions; Goldstein and Gulotty (2016) provide a similar exercise for the 1947 Geneva Round. Both analyses are based on tariff level coding of offers, responses, and the final outcome of the bargain and both argue that the chosen rules and norms of bargaining were consequential for outcomes. In these two Rounds, reciprocity in bargaining over tariff cuts was both a goal and an outcome, although there was less back and forth bargaining than had been assumed. Once offers and requests were made, nations tended to either reach agreement or move on to other products. If there was a modification, it was less likely to be on the requests than the offers. Further, the offers were more or less in line with the principal supplier expectation and swaps were often on very narrow products. While there was some evidence of diffuse reciprocity, both papers find that most of the bargaining was bilateral and specific.

These studies of the early GATT are instructive. Bargaining over both the binding *and* reduction of tariffs in the Rounds suggest that the founders conceived of the purposes of the organization as providing transparency and predictability in trade, and not just deeper market access. As well, both studies reveal that the GATT worked by facilitating the creation of big and flexible "bundles" of reductions. The system of requests and responses allowed political leaders to pick and choose among producer groups while establishing a majority coalition in support of the overall agreement. Reciprocity kept exporters interested and was able to be tailored to specific products. In fact, the specificity of the deals suggests that "new-new trade theory," pointing analytic attention to firm heterogeneity, may also explain the

outcome of the early Rounds. Today, as in the early days of the GATT, policy makers appear to have paid close attention to specific firm interests and then, as now, exporters were a small but cohesive fraction of all firms within an industry.[7] This may be an important insight because as Kim (2016) finds in his study of contemporary firm lobbying, firms that trade in the most differentiated goods within a sector, are the firms most willing and interested in lobbying for free trade. Whereas previous work on rent seeking by industries focused on why we do not see free trade (e.g. Grossman and Helpman), this new line of analysis provides a more varied view of firms' interests and related lobbying activities. This particularism may bode well for the future of the trading system.

To summarize, while the number of articles on the WTO is voluminous, few focus directly on the effects of deeper liberalization at the level of specificity found in the Kim (2016) study. This is a lacuna in the literature. While there are economic assessments of welfare and job growth/loss due to trade liberalization (see, e.g. Attanasio et al. (2004); Pavcnik et al. (2004); Goldberg and Pavcnik (2005a, b)), there are far fewer analyses of the political effects. To know who benefits and loses from a trade agreement, analysis must connect shifts in production and jobs at the firm and/or product level with the norms and rules used to make policy. This is not to suggest that international bargaining has been ignored. Rather, it is that the literature on economic bargaining has traditionally focused more on inter-national negotiations (e.g. Odell (2000)), than on the more microanalyses of the domestic winners and losers, often at the firm level, from a trade agreement. Making these

[7] At the turn of the century, exporting firms constituted a small proportion of all firms within an industry, in fact, less than 5 percent of the 5.5 million firms in the U.S. (Bernard et al. 2007).

micro connections between domestic firms and industries and the potential outcomes of a trade agreement needs further study and remains the frontier for future work.

Next we turn to the analysis of dispute settlement. The judicial system created in the WTO treaty has spurred in depth analysis of all aspects of adjudication, explaining who files, who wins, and even who is "in the room" and why.

The Function of the Courts

In theory and practice, the founders of the trade regime understood that there needed to be oversight and a sanctioning system to undermine the incentive of members to abrogate inconvenient agreements. And given the lack of any centralized policing powers, the dispute settlement system needed to be self-enforcing. As a result, the GATT system encouraged arbitration and mutual recognition and thus adjustment, to trade shocks. GATT47 granted the secretariat neither oversight of infractions nor judicial power. The original wording in Article XXIII, was a very thin set of procedures in cases where the parties could not agree even after consulting on a violation. The need for some judicial procedures was acknowledged in 1947, but how that was to be done was relegated to the Annex and customary, rather than a set of specific practices. Over time that Annex became more detailed, covering issues on how to create an adjudication panel, and included rules on notification, the selection of panel members and the role of member governments. Under pressure, the GATT secretariat created a separate legal division in the early 1980s, and the staff participated in the writing of a series of

understandings among the members on the structure, timing and rules for the resolution of disputes. In 1989, the last vestige of the old order was eliminated, that is, the right to veto an inconvenient decision for domestic reasons.

In its most stripped down version, the GATT/WTO dispute settlement mechanism (DSM) remained constant over time. A complaint by a member mandated consultation with the aggrieved party. There was the expectation of some joint, mutually acceptable agreement. In the absence of a consensus, the parties could ask for a decision from a panel of experts on whether or not there was a breach and the extent of the damages. If ruled against, the offending party was expected to change policy and if that did not occur, retaliation was within the rights of the hurt party. After 1995, most parties asked the appellate body of standing judges to re-examine the panel's findings.

With the creation of the WTO, the number of disputes that went to panels increased dramatically. The result has been more clarity on policy, and a form of "common law", reinforced by decisions by the appellate body. But both because of complexity and the appellate stage, cases take longer to adjudicate and may actually encourage "foot dragging." According to Rachel Brewster (2011), instead of the new system encouraging compliance, the DSM created a remedy gap. Respondent states could violate trade rules for several years without facing trade retaliation, undermining the incentive to early settlement.

The WTO's dispute system has engendered considerable interest and differences of opinion on its efficacy. The rise in cases, to over 500, is used both as an example of its success, that is, easier access especially for developing nations has

undermined the asymmetry in economic power, and by its critics to suggest that too much litigation is a sign of failure since nations are not self regulating.

The new WTO and binding dispute settlement was initially interpreted through the lenses of what appeared in the 1990s as a more general shift in inter-state relations toward legalization. Legalization, or the increase in the degree of obligation, precisions and delegation found in international agreements, seemed to characterize not only the WTO but other agreements which allowed for an increase in the autonomy of courts (Alter 1998; Burley and Mattli (1993); See Annual Review of Law and Social Science Vol. 7). The increased autonomy of WTO courts also gained attention because of the vastly expanded legislative domain after 1995, in particular, the expansion of jurisdiction because the single undertaking, which eliminated the previous "a la carte" set of obligations, and the regulation of behind the border production in the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) (See Barton et al. 2006).

Twenty-five years later, the scholarly community continues to debate the virtues of this increased judicialization in light of the WTO mandate. For some it is the source of WTO strength; for others, it has undermined cooperation. The heart of the issue rests with the concept of "efficient breach." According to Schwartz and Sykes (2002), the role of the WTO dispute system is not to punish violations through deeper penalties but to assure that unilateral sanctions will not spiral out of control. The role of the DSM is to set the "price" of an efficient breach, that is, allow defection when the cost of compliance is higher than the cost of noncompliance. The standard for an efficient DSM is that it deters, not punishes. In equilibrium, we should see

cases decreasing in line with the clarification of what is, and is not, a punishable breach of the rules, because as Maggi and Staiger (2011) suggest, the role of the DSM is to complete and clarify aspects of the WTO's "incomplete contract."

As clarification, although the new DSM is often said to be binding, the compliance mechanism remains self-enforcing: nations comply because of the potential of a sanction hurting a powerful domestic exporter and/or a fear of a reputational externality. But, how much of a sanction is necessary and as Pelc and Urpelainen (2015) ask, when is it acceptable for a nation to buy their way out of a violation? More generally, there is still a lack of consensus on the degree to which domestic flexibility will either encourage compliance or alternately, lead to shirking. To better understand whether or not the current system of rules is efficient, we need to explore not only when and why nations comply but also, how exceptions are viewed as signals to domestic actors (Pelc 2016).

Rosendorff (2005) and Rosendorff and Milner (2001) present a logic for why the DSM's design is consistent from an efficient breach perspective, focusing on granting nations increased flexibility by legitimating a system of temporary escape from rules (Rosendorff 2005). Goldstein and Martin (2000) and Gilligan et al. (2010), however, are less sure about the optimality of the constraints imposed by the WTO's rules, including the fail-safe escape clause mechanism. Goldstein and Martin (2000) argue that legalization increases the clarity of the effects of a rule violation, and as such, can have the unintended effect of mobilizing the wrong domestic groups. Anti-trade groups, when mobilized, undercut the ability of leaders to both sign and adhere to inconvenient trade obligations. Gilligan et al. (2010) concur but offer a

different logic. Strong courts, they argue, can create a disincentive for states to reveal information, undermining pretrial arbitration and making brinkmanship and conflict more likely without the intervention of the court. Alter (2003) also implies that too much international litigation may actually undermine support for the international legal system.

Like Rosendorff (2005) and Rosendorff and Milner (2001), Kucik and Reinhardt (2008) present evidence that suggests that the escape provisions are, in fact, efficient. Similar to Carnegie (2014), they see the escape rule as solving a time inconsistency problem—at some future moment a nation may need to renege because of changed circumstance. Thus, "counter to intuition, formal provisions for relaxing treaty commitments can actually boost cooperation relative to what would otherwise be possible" (478). Focusing on antidumping cases, Kucik and Reinhardt support the WTO's level of flexibility. After accounting for a host of selection issues, they find that states with legislated antidumping provisions are more likely to join the GATT/WTO and to bind their tariffs.[8]

The assessment of the DSM is ultimately an empirical issue and there is a large number of studies that provide insight into who files and who wins cases. The findings have been quite diverse. In 2000, Busch and Reinhardt argued that the WTO dispute procedures still lacked enforcement power and therefore its success depended on "its ability to encourage bargaining in the shadow of weak law" (160). A few years later, Iida (2004) looked at the cases and found that the dispute system

[8] Dumping regulations are a significant source of protectionist pressures and disagreement among WTO members. Most recently, the use of zeroing in the US in antidumping cases has led to significant criticism on the part of trading partners. For an explanation, see Ikenson (2004).

had partially done what was expected, pointing in particular to a decline in unilateralism by the US. Since the fear of American unilateralism was a key reason that many of the regime's members were willing to accept a reformed DSM, this could be interpreted as a strong metric of success. Still, a review of the many scholarly papers on the DSM reveals that effectiveness is often in the eye of the beholder.

First, a set of authors looks at domestic political characteristics to explain initiation and outcomes. For example, Rickard (2010) collects data on democracies and electoral institutions as explanation for the variation in case behavior. She finds that majoritarian systems, like the US, are, on average, less likely to comply and are more constrained by particular segments of the electorate. Using data on complaints filed at the GATT/WTO over illegal narrow transfers, she finds that having a majoritarian system significantly increases the probability of a nation violating an obligation. Chaudoin (2014) also looks at domestic constraints but focuses on the timing of disputes, which he argues varies with the political and economic conditions in the defendant country. Complainants are more likely to find international arbitration appealing when there is a high probability that the case will mobilize pro-compliance domestic audiences. This will be more likely at particular moments, for example, during an election year or when there is some shift in the domestic economy. Using data on potential disputes against the US, Chaudoin finds that trading partners of the US are more likely to file complaints during election years with low unemployment rate.

Second, authors, such as Davis and Shirato (2007) have used industry characteristics as an explanation for dispute initiation and thus outcomes. Focusing on Japan and its production profile, they find that industries characterized by many product lines and rapid product turnover face higher opportunity costs of filing an objection and are less likely to request dispute resolution. Using data on potential cases for WTO litigation in Japan, they show the importance of a number industry variable, including industry size, past political contributions, and concentration.

Third, many authors have suggested that the variation in cases filed and case outcomes resides in the size and strength of one or both of the parties. Richer nations may be at an advantage in being able to utilize the system in a manner not available to the emerging or developing economies. Although developing countries can build procedural power by forming coalitions, high capacity members hold positional strength, or structural power, at the WTO (Elsig 2006). Thus Guzman and Simmons (2005) explain that there are significant costs to litigation and monitoring and Kim (2008) and Bown (2005) find that judicialization has provided disproportionate benefits to those with greater institutional capacity.

The cost of litigation has elicited considerable attention. For example, while recognizing that there may be a fixed and high cost to litigation, a number of papers have implied that developing nations can affect dispute outcomes by either participating as third parties (Busch and Reinhardt 2006; Johns and Pelc 2014) and/or learning how to strategically use the system. Davis and Bermeo (2009) argue that the cost of litigation is largely a function of information; countries spend resources in the process of fact-finding, which is specific to each case but they also

pay a significant amount of fixed cost in the process of getting acquainted with WTO rules and procedures. Having experience in WTO adjudication reduces such fixed costs for governments and their domestic producers. Examining dispute initiation for 75 developing countries between 1975 and 2003, they find that prior experience, either as a complainant or a respondent, increases the probability of dispute initiation. In the same vein, Conti (2010) finds that the relative experience between the complainant and respondent influences the manner in which the dispute unfolds. Experience seems to predict whether or not a nation settles or goes to panel. His data shows that early settlement is more likely in cases where the complainant has been involved in more disputes relative to respondents, while the odds of going to a panel increases when respondents have more experience. Prior experience in WTO litigation may also have spillover effects on dispute initiation in other trade courts. In examining the determinants of formal dispute initiation in regional forums among South American countries from 1996 to 2008, Gomez-Mera and Molinari (2014) find that prior dispute experience at the WTO influences dispute initiation at the regional level.

Figure 1 shows the use of the DSM over time. It is noteworthy that the number of requests for consultation by an aggrieved party has started to shift downward. Given the increase in politicization of trade in just about all WTO member nations, how should we interpret the relative decline? Is the decline indicative of a clarification of a previously underspecified contract and thus better information on the potential outcome of a case or is the decline simply an indicator that nations comply, even in hard economic times? Maggi and Staiger (2016) argue

the former, that is, that there has been judicial learning, and rule clarification, by the courts. They find that the probability of a new dispute or a ruling is related to the accumulation of article-specific, directed-dyad-specific, and complainant-specific rulings. But while they find that the specificity of rulings matter, they find only weak empirical evidence of what they call general-scope learning (the impact of the total number of rulings regardless of issue area and disputant characteristics is only weakly supported). The lack of a general finding casts some doubt on the argument that governments are getting "smarter" about the DSM process.

The other explanation, that decline is evidence of more compliance, is also problematic, according to a recent paper by Kucik and Pelc (2016). In this study, these authors look directly at trade policy choices, focusing on behavior during the Great Recession, 2008-2011. Their conclusion is that the more rigorous and ambitious the nation's accession agreement, the more likely it was to be shirked during this period. Countries, in hard times, took "action to protect the interests of domestic producers, in spite of their stated commitments to liberalise" (393). Their data suggests that leaders do respond to domestic political and economic pressures, even in the shadow of a binding dispute system. And as such, it may be that some nations, here, those who recently acceded to the WTO, may worry less about another country taking them to court than the domestic pressures that emanate from an economic shock. While not undermining what we know about the institutionalization of the WTO court procedures, it does suggest that we need a deeper understanding of when and why the courts, and the general membership, are more forgiving of nations' inability to comply with obligations.

Some General Conclusions

Alan Blinder inked a blog post in 2016 noting that, "this [is] an unpropitious time for rational discourse" on the subject of international trade (The Wall Street Journal). Trade in general, regional trade agreements and the WTO, are all being blamed for a host of economic problems, most of which have little to do with the agreements. A Washington Post-ABC News Poll (May 16-19) taken not long after the Blinder post found that 53% of respondents believed that trade took away jobs; two months earlier, 65% had responded that US trade policy should be more restrictive in order to protect jobs (Bloomberg Politics Poll, March 19-22). European public opinion is equally as negative. Even though the job "churn" is rarely a result of a trade agreement, the public's perception is that trade and job prospects are interconnected. While those that benefit from globalization, the more educated, continue to support open borders, the shift in the labor market that has resulted from technological innovations and declining productivity are more often seen as a result of some external public policy (For ex. of trade attitudes see: Hiscox 2002; Scheve and Slaughter 2004; Mayda and Rodrik 2005; Pandya 2010). One important explanation for legislative inactivity by the WTO is this shift in domestic public opinion in many of the member states. But while public attitudes may be the most visible of the constraints on trade policymaking, this is not the only problem that confronts the WTO. Three other constraints are suggested from this review.

First, the inability to legislate may be tied to the growth of international law. Gilligan et al. (2010) have provided a logic for courts benefiting from increased

precision of international law and a number of scholars have argued that states are more likely to sign and abide by agreements when they think their partners will challenge them if they do not (Davis 2012). But whether or not the current WTO dispute settlement system allows efficient breach remains an open question. To the extent that nations feel constrained by existing law, they will fear any new obligations. And as Kucik and Pelc (2016) illustrate, in hard economic times, nations fail to adhere to promises made when their economy was booming. More generally, the Kucik and Pelc (2016) finding of rule violations suggests two possible interpretations of the relationships between the courts and the legislative impasse today. By one interpretation, the ability of nations to escape a rule in hard economic times is evidence that nations are not overly bound by WTO obligations. The DSM is allowing efficient breach. The other interpretation, however, is that post-WTO, nations have increasingly recognized that economic shocks do require reneging and as such, continue to fear the potential of DSM punishment. In either case, nations would be wary of any new obligations given uncertainty about the level of acceptable breach.

A second stumbling block to new legislation may be the norms of the regime and in particular, the norms that regulate internal decision making. Steinberg (2002) argues that the original choice of the GATT founders to grant each member "sovereign equality" is a substantial impediment to the legislative process. Reviewing the history of past Rounds, he concludes that the rule has always been understood to be impractical and historically, legislating in the GATT/WTO depended upon joint action between the US and Europe and not a more general

agreement among members. The transatlantic partnership, he finds, created an "invisible weighting"; cooperation depended upon agreement between Brussels and Washington (354-355).

Steinberg is not alone in arguing that the one member one vote consensus system is problematic. Leading up to the creation of the WTO, there was a reform effort, which would have institutionalized the authority of a smaller group of influential nations (then known as the CG18). The proposal failed for fear that the three or four most powerful nations would have too much influence in the organization. But the then status quo, which was sometimes labeled the "concentric circles" model, was not very different (Blackhurst 1998). Here, power remained informal but just as relevant. For any policy, there would be an inner circle of nations that would reach consensus on a set of rules. That decision would then be sent to a larger number of nations and upward until there was a general consensus. Explaining the benefits of the system, Blackhurst who ran the research division for many years explained that, "the concentric-circle model … enables delegations to adopt a position of not opposing the consensus without actually having to cast an affirmative vote" (50). This system, later decried as the "green room" was fundamentally rejected after 1999 by the developing world.

The absence of reform in decision making may explain the failure of the most recent Doha Round of negotiations. As the interests of the developed and developing countries have diverged and the shared sense of purpose that facilitated consensus in the early years of the GATT has eroded, the organization has found consensus an illusive goal.

A third set of scholars focus less on the courts or the voting system and instead, focus on the expansion of the agenda. The first fifty years of the trade regime focused on the binding and reduction of tariffs. With success, the WTO turned its attention to a set of nontariff barriers. But the problems they now seek to solve are of a different nature; they are behind the border and are more likely to elicit attention from domestic audiences. The new issues range from FDI, to the environment to competition policy. All require domestic actors to change their regulatory regimes in a manner that is fundamentally disruptive to politics at home. Making those changes was difficult, more so because simultaneous with a push for deeper liberalization through regulatory reform came the demand for more inclusive and transparent negotiations. Not surprisingly, transparency has made cooperation even more problematic by increasing the number of domestic veto players.

As a most general conclusion, it would be wrong to assume that the popular malaise about the virtues of trade is a function of something the WTO did or did not accomplish. The current fear of deeper liberalization may well reflect the success of the multilateral system, not its failure. The GATT/WTO has been extremely efficacious in facilitating the transnational opening of borders to the movement of goods and services. Few international organizations can claim credit for having influenced the policies of member states to this degree. Whether or not there will be more Rounds and a greater harmonization of trading rules is an open question. It is possible that the future gains will be insufficient to balance potential disruptions.

But even if so, history will record the 20th and perhaps the 21st centuries as ones in which GATT/WTO system was profoundly important.

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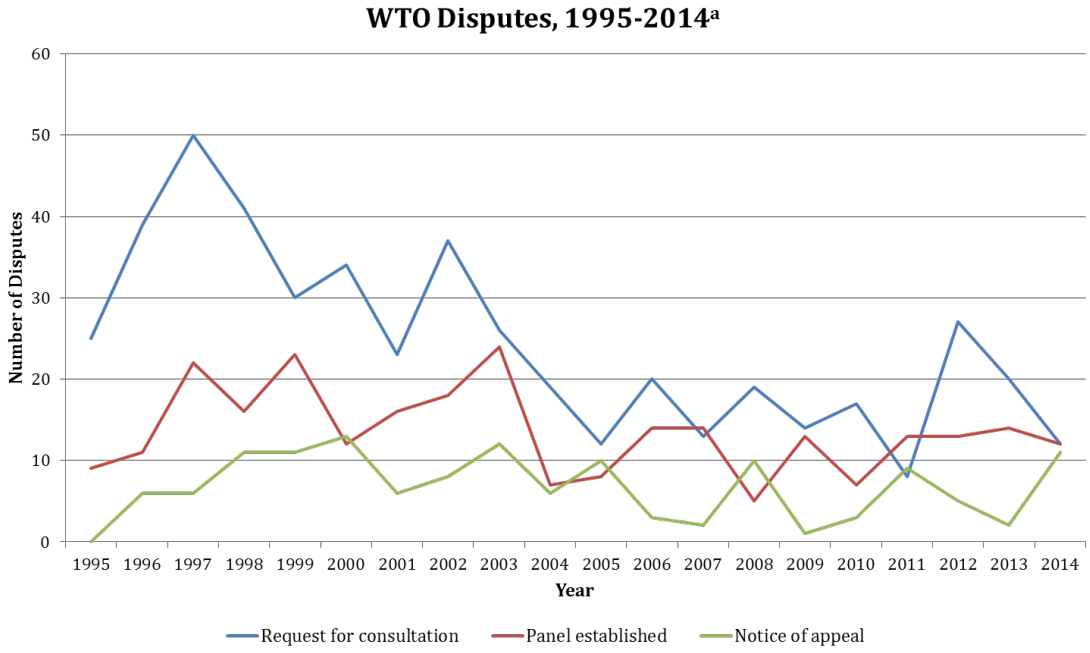
Table 1: Tariff levels, 2012

WTO member economy	MFN applied rate, simple average[a,b]	Binding coverage[a,c]
G20 High-income		
Australia	2.7	97.1
Canada	4.3	99.7
European Union	5.5	100.0
Japan	4.6	99.7
Saudi Arabia	5.1	100.0
South Korea	13.3	94.6
United States	3.4	100.0
G20 Emerging		
Argentina	12.5	100.0
Brazil	13.5	100.0
China (2011)[d]	9.6	100.0
India	13.7	73.8
Indonesia	7.0	96.6
Mexico	7.8	100.0
Russia	10.0	100.0
South Africa	7.6	96.4
Turkey	9.6	50.3
Developing, other[e]		
Bangladesh (2011)[d]	14.4	15.5
Burma	5.6	17.6
DR of the Congo	[f]	100.0
Egypt	16.8	99.4
Ethiopia[g]	17.3	[h]
Iran (2011)[d,g]	26.6	[h]
Nigeria (2011)[d]	11.7	19.1
Pakistan	13.5	98.7
Philippines	6.2	67.0
Thailand	9.8	75.0
Vietnam	9.5	100.0

[a]Computed from Bagwell, Bown, and Staiger (2015)
[b]Ad valorem rate
[c]Share of import products
[d]Data availability for 2011
[e]Developing countries with 2012 populations greater than 50 million
[f]Not available
[g]Observer only; non-WTO member
[h]Countries without bound rates

Figure 1.



[a]Sources: Overview of the State of Play of WTO Disputes - Annual Report 2014 and WTO Dispute Settlement Website (https://www.wto.org/english/tratop_e/dispu_e/dispu_current_status_e.htm). Disputes are from January 1, 1995 to October 31, 2014.