CHAPTER - I

INTRODUCTION
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1.1 THE PROBLEM:

The international trading system, which refers to the rules, institutions and practices governing transborder flows of goods and services, is a precondition for the smooth functioning and expansion of international trade. It provides a framework and institutional support which facilitate exchange of goods and services among countries and sustain sound economic growth.

From 1870 to 1913 economic relations between rich countries and developing countries were characterized by far-reaching liberalization of international trade. The pattern of international trade was the typical colonial in which developing countries exported primary products to the rich industrialized countries and industrialized countries exported finished manufactured goods to the developing countries. During two world wars and the Great Depression in the 1930s, the 'beggar-thy-neighbour' policies in which each country tried to transfer its economic problems to other countries by deprecating its own currency and imposing high tariffs, led to an almost complete collapse of the international trade system. Partly as a result of this, the volume of world trade fell off, and investment in developing countries decreased drastically. Economic growth stagnated both in rich countries and the developing countries most involved in international trade. During the World War II, it was feared that the depressed economic conditions of the 1930s may return after the
recession of War as nations, like in the past, would attempt to return to balanced budget. This would create problems for international trade. Therefore, plans for reform in international trading system began to take shape during the war. As the war ended, the allied powers met in Bretton Woods, New Hampshire in 1944 to set some guidelines for the operation of the world economy in the post war years.

The International Monetary Fund (IMF) to deal with the BOPs problems and promote international monetary cooperation and trade and the International Bank for Reconstruction and Development (IBRD) to finance economic reconstruction and development were conceived at this conference. This conference also generated plans for the establishment of an International Trade Organization (ITO) to frame rules, eliminate restrictions and settle disputes relating to international trade. The first two were set up but the ITO failed to take shape due to non-approval of its Charter by the U.S. Congress. Therefore, U.K., US and few other countries agreed to adopt as treaty obligations a set of rules for conducting international trade among themselves. This treaty was called the General Agreement on Tariffs and Trade (GATT). The GATT was signed in 1947 at Geneva by 23 countries including India and became effective from January 1, 1948.

The GATT became the cornerstone ground on which the multilateral trading system was built. Its guiding principles included:

(i) Trade on non-discriminatory basis;
(ii) Protection of Domestic industry by means of customs, tariffs and not through others commercial measures;

(iii) Consultations among members to avoid damage to their interests; and

(iv) GATT to serve as a forum within which negotiations could be held to reduce tariff and other trade barriers.¹

The GATT framed rules for conduct of international trade among member nations and provided forum for multilateral negotiations on issues relating to it. Its members agreed to abide by the principle of non-discrimination embodied in the Most-Favoured Nation (MFN) clause and national treatment. They committed to protect their domestic industry by tariffs only and bind the tariff levels negotiated among themselves. The GATT also established a framework for settlement of trade disputes.

Over the years, the GATT pursued trade liberalization by sponsoring a series of negotiations or rounds and achieved remarkable success in reducing tariffs all around the globe especially in the developed countries. Continued reductions in tariffs helped spur on unprecedented expansion in world trade surpassing the rate of growth of world output. But despite these achievements, grievances against the working of the GATT appeared in the early 1980s.

The developing countries raised their voice against its weak institutional structure and defective dispute settlement system. They strongly protested against the bias of the GATT favoring the developed countries and demanded that an ITO be set up. The members of the GATT wanted it to be
improved to absorb the complexities of world trade, encompass additional areas of trade and address increasingly the concerns of developing countries.

These and other realizations convinced GATT members that a new effort to reinforce and extend the multilateral system was needed. The efforts resulted in the Uruguay Round (UR), the Marrakesh Declaration, and the creation of WTO.

The UR commenced in September 1986 and was concluded in 1994. It covered many new areas such as agriculture, textile, technology, intellectual property rights (IPRs), trade related investment measures (TRIMs), services etc.² It included in its scope of liberalization, non-tariff barriers (NTBs), along with tariffs, and conceived many new norms and disciplines such as sanitary and phytosanitary measures, anti-dumping measures, dispute settlement procedures, safeguard measures etc. with a view to ensuring liberalized effective market access and rule based trade.

The conclusion of the UR saw the transformation of the GATT into a more formal organization called the World Trade Organisation (WTO) in 1995.

The WTO like the GATT stands for the principle of non-discrimination and calls for progressive liberalization of World trade by reduction and binding of tariffs, elimination of quotas and NTBs. But it is distinct from the GATT in certain respects. It has an institutional set up and a wider coverage. It is equipped with powers to enforce commitments, rules and norms of discipline in international trade among its members.
It has an improved dispute settlement system. It is a responsible for overseeing the implementation of all agreements that were negotiated before it came into existence and those that will be negotiated in future. Thus in short the WTO seeks to promote both trade and the multilateral trading system to face the needs of the future.

The WTO has brought agriculture and textiles more fully under International trade rules. Prior to the setting up of this organization, these two sectors were heavily protected in most of the developed countries and trade was distorted. For industrial goods, the main provisions of the WTO include the reduction in tariffs, expansion of duty free access and expansion of bindings by the developed countries.

Thus, the establishment of the WTO has brought in significant changes in the world trading system and placed additional demands on developing countries in respect of their effective participation. First, the WTO covers a variety of new areas – such as services sector, IPR in which new rules governing the conduct of international trade have been agreed and whole implementation requires additional institutional capacity on the part of the member governments. Second, the WTO negotiation on liberalization of various sectors require continuous participation by the members. Third, the new WTO Dispute Settlement Mechanism (DSM) enables developing countries to address their grievances, but it also poses tremendous challenges because of their very limited institutional capacity to initiate action against developed countries.
No doubt, trade can be good for development of those countries which engage in trade with other countries. But how much trade will be beneficial depends upon the trade policy and the trade liberalization policy. Trade liberalization opens foreign markets, expands the demand for domestic firms goods and enable them to serve a large market and realize gains from economies of scale. Trade liberalization may make available a range of inputs at lower prices by lowering cost of production. Liberalization may also introduce more competition from foreign firms to the domestic firms which may result in improvements in efficiency of local production. Finally trade liberalization may, through various channels, affect the rate of economic growth.

The standard argument in favour of trade liberalization is that it improves the average efficiency in a country. Import from foreign producers may destroy some inefficient local industries, but competitive local industries are supposed to be able to absorb the shock as they expand their export to foreign markets. In this way trade liberalization is supposed to allow resources to be deployed from low productivity protected sectors into high productivity export sector. But that argument assumes that resources will be fully employed in the first place, whereas in most developing countries unemployment is persistently high. One does not need to redeploys resources to put more resources into the export sector, one simply needs to employ hitherto unused resources. In practice trade liberalization often harms competing local import
industries, while local exporters may not automatically have the necessary supply capacity to expand. So liberalization often seems to result in labour temporarily going from low productivity protected sectors to zero productivity unemployment. Unfortunately, most of the models which attempt to address question of welfare gain from trade liberalization assume full employment and therefore provide no answer to this key question: the impact of liberalization in economies with underemployed resources. But the issue of unemployment is not just a theoretical problem. Concern that trade liberalization will lead to increased unemployment is perhaps the most important source of opposite to liberalization.

Trade liberalization will also affect inequality. Opening up to trade does not make everyone in a country better off. Instead it changes the distribution of income and creates winners and losers. The standard economic argument is that the net gains from trade liberalization are positive so the gainers can compensate the loser and leave the country better off overall.³

Most of the economic theory of trade liberalization has focused on static welfare gains, the long-run effects of trade liberalization are determined by its effect on the economy’s rate of growth. Recent models of indigenous growth have important implications for the theoretical relationship between free trade and economic growth, although their results are not fully understood, and their policy consequences remain to be thoroughly established.
Theory and empirical evidence indicate that trade liberalization can be a positive force for development in poor countries, but that these benefits depend on others, concomitant factors. The factors which are responsible to failure to the trade liberalization is the market failure. Developing countries should attempt to promote development by correcting these market failure through policy interventions, including trade policies, if and only if they are the best available instruments. Developed countries must do their parts. They can help to integrate developing countries into world trading system and ensure that they benefit from it.

The WTO membership is expected to bring in the major benefits in terms of greater and secured market access abroad for exports, freedom of transit, resolution of the disputes through Dispute Settlement Mechanism, and greater discipline at home that brings more transparency and accountability for the sound economic policy.

The market access is assured by GATT Article 1 and Article 111. While Article 1 ensure that each member countries provide Most Favoured Nation (MFN) treatment to each other, Article 111 talks about National treatment. The MFN means getting access to market of a member nation without discrimination. The member countries are abolished to reduce the bound tariff rates. This makes the MFN treatment more meaningful and functional. The ‘national treatment’ means that a foreign supplier is treated at par with national supplier without discrimination. The GATT Article V assured
freedom of transit for commodities treated by one WTO member through the territory of another member. The member countries obliged to provide passage through most convenient route for international transit. In case of a dispute or member countries feel being discriminated, the defaulting countries can be brought into the dispute settlement mechanism to resolve it or get compensation for the loss. Further, the WTO membership brings more discipline in domestic economic management as several rules would apply to the country’s own policies.

There are two other specific benefits though temporary in nature, accorded to developing and least developed countries. These are special and differential treatment (SDT) and technical assistance. The SDT is designed to provide essential breathing space to the least developed countries enabling them to adjust and come up to the required standards. The WTO endorsed technical assistance programme which the developing and least developed countries may receive from various international agencies including WTO towards basic capacity building, and towards raising their ability to get improved preferential access to international market\(^5\).

The new trading system under the WTO has been in operation for more than a decade and it is appropriate to assess the impact of this system on trade performance of developing countries like India.
1.2 OBJECTIVES OF THE STUDY:

In the light of the above, our objective in this study is primarily to examine the role of world trading system under the WTO in promoting international trade of developing countries in general and that of India in particular. Within the framework of this broad objective, the specific objectives set out for the study are as follows:

1. To discuss the implementation of WTO agreements and commitments by its different member countries.

2. To assess the impact of the WTO provisions on India’s foreign trade to reflect on the country’s success in realizing her expectations of its membership of this organization.

3. To suggest ways and means as to how India can maximize the gain and minimize the losses from its membership of the world trade organization.

India is one of the founder members of the WTO. India’s joining the WTO family was motivated by the expectation to strengthen her trade under the strengthened multilateral trading system. India had initiated economic reforms programme in July 1991 with liberalization of foreign trade as an important part of the programme. Measures were taken to create an environment for rapid increase in exports, raise the country’s share in world exports and make trade an engine for achieving higher economic growth. India’s membership of the WTO was expected to accelerate this drive for expansion of exports and bring higher growth leading to a better earnings and
living for the ‘average citizen of India’. A study that seeks to explore whether India’s foreign trade has undergone noticeable changes during the post-WTO period may be considered significant from the point of view of developing countries in general and for India in particular. To the extent that India’s experience in this respect is any guide, this study will also be helpful to the similarly placed countries.

1.3 DATABASE AND METHODOLOGY:

The study has as its period of reference the post-WTO period which is also compared with the pre-WTO period. The study is based on secondary sources of data which have been collected from various sources. Due acknowledgement has been given to their at appropriate places.

The methodology used is simple and analytical. Tabular analysis has been used to analyse the data and results have been interpreted accordingly.

1.4 PLAN OF THE STUDY:

The whole study is divided into six chapters.

Chapter two is devoted to review of literature. This is followed in chapter three by a brief discussion of the framework of the world trading system and their features.

Chapter four investigates the implications of WTO for developing countries.
In the fifth chapter the performance of the Indian trade has been considered in the era of WTO rule.

Finally Chapter six summarizes the findings of the present study and tries to offer a few suggestions for improving the trade benefits of India.
References:


