

Trade and Subsidies

Undermining the trading system with public funds

An IISD Commentary

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Despite the official optimism at the World Trade Organization, it is hard to hide the serious malaise that has taken grip of the multilateral trading system. Efforts to winch the Doha Round out of the ditch are proving much more strenuous than anticipated, and the feeling is spreading that there might be something more profoundly wrong with the system than we initially feared; or if not with the system, then certainly with our approach to expanding and consolidating it.

Ironically, this malaise strikes at a time when visible progress on concluding a trade deal could play an important role in helping put the world economy back on its feet. In fact, the loss of confidence in the trading system comes at the worst possible time. Trade offers a promising way for countries to grow their way out of the recession, and it offers to pay dividends faster than many of the other measures included in economic stimulus packages. Instead, there are ominous signs of resurgent protectionism. So far, most protectionist measures have been combated successfully, but no one is sure how long the tide can be held off.

Surely, given both the dangers of protectionist escalation, and the role that robust trade could play in combating the recession, concluding the Doha Round and thereby rebuilding confidence in the trading system must be a high priority. But here is the paradox: there is broad agreement that expanding trade would be of great benefit at this time of economic downturn. It is generally agreed that it makes sense to complete the Doha Round and that the concessions required are not beyond the reach of enlightened leadership. Most agree that a final failure to secure a reasonable Doha package would not only weaken the WTO but that it would land a body blow on multilateralism in general. And, finally, trade economists worldwide share a sense of danger on observing the proliferating signs of protectionism. So why can't we move forward?

Solving this situation is not simply a matter of all sides showing marginal flexibility. It is not a matter of stumbling across the ingenious formula that everyone has missed in their haste. It is not a matter of cutting a few bilateral deals in the corridors and forcing a consensus on the more recalcitrant WTO members. Instead, it requires recognizing that, in many ways, the current organization of both national and global economies seriously undermines the goals that trade liberalization is intended to serve, and recognition that we must retool the trading system to confront these issues.

Nothing illustrates this challenge better than current patterns of subsidy use. The fact that gigantic sums are deployed in ways that distort trade and undermine the development of mutually-beneficial trading relationships is nothing short of a scandal, both in the dimensions of public money deployed and in the impact on trade and sustainable development. While the subsidies involved range from those that are marginally useful or

neutral to those that are outrageously destructive, there is little doubt that a significant majority of these subsidies undermine progress towards sustainable development. Agricultural subsidies approach \$1 billion a day. Subsidies to water provide incentives to waste a commodity that is not only growing more scarce but that is fundamental to agricultural and industrial production and, indeed, to life itself. Subsidies to fisheries have contributed to the depletion of one fish stock after another, pushing them over the brink so that they never recover. Subsidies to fossil energy reward behaviour that flies in the face of global efforts to combat catastrophic climate change, warping markets in ways that perpetuate wasteful and environmentally-destructive energy practices.

Current subsidy budgets vastly outstrip the funding needed to address the world's major development challenges. Subsidies to agriculture, energy, water and transport annually total some 15 times the sums needed fully to implement the Millennium Development Goals by 2015. They are an order of magnitude higher than the amounts needed to attain the goal—set back in 1966—of devoting 0.7 per cent of GDP in OECD countries to development assistance. They represent over eight times the amount once calculated as being needed fully to implement Agenda 21—the world's most ambitious plan to bring about sustainable development. Finally, if the public funds currently invested in energy subsidies were to be invested instead in the fight against climate change, they would largely suffice to meet the target that Lord Stern calculates is needed to stabilize greenhouse gases below the levels at which they risk causing irreversible damage.

These examples are deliberately chosen to shock. The simple fact is that public money is not only being mis-spent, it is being mis-spent in titanic proportions. It is being mis-spent in ways that undermine the credibility of the trading system and that sap the confidence developing countries have in trade as a potential solution to their development problems. As such it is preventing recovery of the world economy, and virtually guaranteeing that action on climate change will be too little, too late.

Wait, isn't WTO able to combat subsidies, provided they are trade distorting? Of course it is—and at least the agricultural subsidies are on the negotiating table. The trouble is WTO members do a poor job of notifying the subsidies they use and, when they do so, the reporting is patchy, out-of-date and generates non-comparable data. In fact, there is no incentive for members to notify subsidies, since there is no price to be paid for failing to do so, whereas notifying their subsidies could leave them open to challenge.

So we have a situation where we are trying to urge countries to extend the multilateral trading system in the interest of re-launching the world economy. To do so requires raising the confidence of members—and especially the developing countries—that their concerns will be met. And yet we systematically refuse to address seriously one of the most massive,

most damaging and most central of the reasons for the low level of confidence. Subsidies are a defiant slap in the face to developing countries that can't afford them, that can't compete because of them, and that see them as a monument to a system that is unbalanced, unfair and hopelessly stacked against them. They underline as hypocritical the endless political statements at the G8 and elsewhere that action against climate change is the most urgent problem of humanity, or that alleviating poverty in Africa must take precedence over any other development challenge. And they cement the mistrust with which the developing countries regard institutions like the World Bank or WTO that are dominated by the rich and powerful.

If we are serious about trade, we must get serious about how we use precious public funds. We must resolve that they should no longer be used in ways that undermine equitable, sustainable development and instead insist that they should only be used in ways that advance and protect the global public good. Where is the leader who will take us down that path?

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