

India and the Multilateral Trading System Post-Seattle: Defensive or Proactive?

Aaditya Mattoo (World Bank)
and Arvind Subramanian (Harvard University/IMF)

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ABSTRACT

Until very recently, India had disengaged from world trade. The challenges ahead are to implement policies that increase competition in domestic markets, while safeguarding public objectives. These challenges are, above all, domestic. However, this paper argues for more active multilateral engagement by India. This engagement can be helpful in facilitating and consolidating domestic reform, and in gaining access for India's exports of goods and services.

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Non-Technical Summary

This paper argues that India should engage more actively in the multilateral trading system. For four reasons.

First, engagement can facilitate domestic reform and enhance access for India's exports. India is now at a critical juncture. It is an increasingly willing reformer, but confronted by opposition to reform domestically. At the same time, market access in areas of major export interest remains impeded. Multilateral engagement pits these two elements against each other constructively. On the one hand, domestic reform would be facilitated if the government could demonstrate that there were payoffs in terms of increased access abroad. The gainers from the increased access, be they exporters of textiles, software, professional services or other products, could represent a countervailing voice to groups that resist reform. On the other hand, the need to demonstrate external payoffs to secure greater openness at home makes India a credible bargainer, and could help induce trading partners to open their own markets.

Second, engagement can serve as a commitment to good policies. The experience of unconstrained choices in Indian trade policy has not been salutary. External commitments can foster good policies in two respects: providing guarantees against reversal of current policies and credibly promising future reform. For instance, in recent years, India has reversed some of its tariff liberalization, which could have been prevented by more meaningful tariff bindings. India also failed to take advantage in sectors such as telecommunications to use multilateral commitments to lend credibility to future reform programs. Such precommitment can help strike a balance between the reluctance to unleash competition immediately and the desire not to be held hostage in perpetuity to the weakness of domestic industry or to vested interests.

Third, engagement can serve as a means of securing market access rights that have already been established. In a situation of asymmetric power, a rules-based system protects, albeit imperfectly, the weaker party. The WTO dispute settlement system thus far has enabled developing countries to enforce their rights. While this experience affords some comfort, there is increasing concern that the required elimination of quotas on textiles and clothing may not happen on time and be difficult to enforce. We argue below that in such an eventuality, India can enforce its rights by threatening to wield an effective retaliatory weapon: withdrawing its TRIPs obligations.

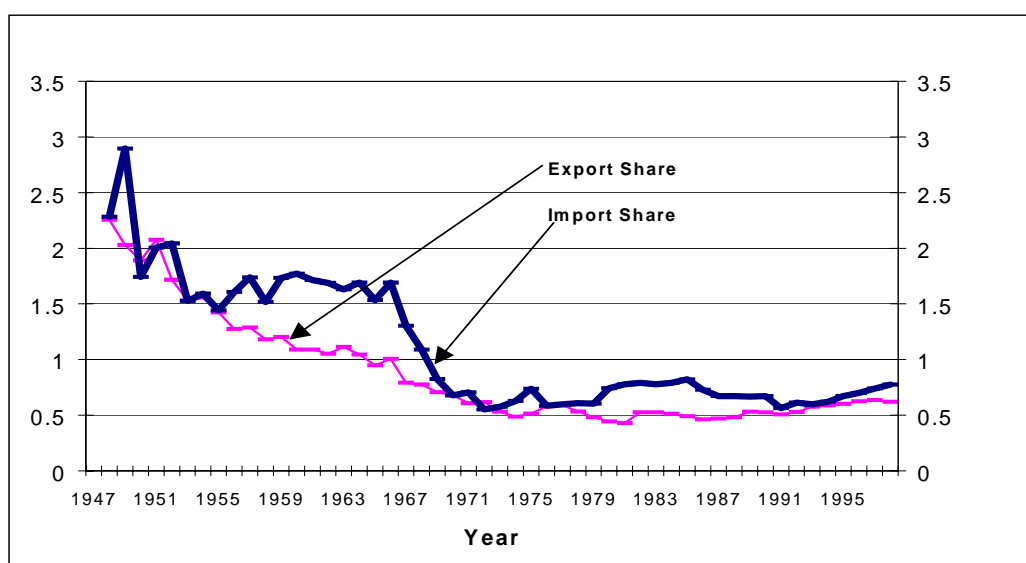
Fourth, multilateral engagement can serve as a bulwark against regionalism. The proliferation of regional agreements is having a serious if unrecognized impact on India's trade. A particularly stark example relates to the potential trade diversion consequences of NAFTA. India has a strong interest in a multilateral tariff reduction to neutralize this policy-induced disadvantage.

Overall, the value of multilateral engagement might be limited if prospects for securing increased market access are dim, and the failed Seattle negotiations heighten such negotiating pessimism. However, this pessimism needs to be credibly tested, by a willingness on India's part to open its markets in return for improved access. Success in this regard is not assured, but its chances can be improved if India were to align itself with countries that press for sound open policies.

I. Introduction

One of the more commented upon facts about the Indian economy is its small and dwindling importance in world trade. At independence, India accounted for over two percent of world exports and imports, and by the early 1990s, this share had declined to about half a percent (Chart 1 below). A plausible case can be made that India's economic fortunes have been related to this de facto international disengagement which is attributable, at least in part, to India's inward looking economic and trade policies. Protectionist policies, in turn, have shaped India's attitude to participation in the multilateral trading system, both in the old GATT and its successor, the World Trading Organization (WTO). India's stance in the GATT/WTO has always tended to be defensive, seeking freedom to use restrictive policies, which has been one of the two prongs of the so-called special and differential (S&D) treatment embraced by developing countries as a whole.¹ Since the early 1990s, India has embarked on serious trade and economic reform, without, however, a corresponding change in the nature of its multilateral engagement. This paper examines whether India should adopt a proactive role in the multilateral arena founded on its recent adoption of more open policies.

Chart 1: India's Share in World Imports and Exports



Source: IMF's International Financial Statistics

The collapse at Seattle of the negotiations to launch a new round provides time and perspective for India to reassess more carefully its attitude toward the multilateral trade system. The failed talks are both sobering and heartening in their lessons for India. Sobering because of what failure signals about the external political and negotiating environment. The hardening of partner country attitudes toward opening their own markets and the emergence of insidious forms of protectionism will make the bargaining climate less favorable for India in the future. Equally, however, Seattle demonstrates the ability of developing countries to resist successfully these

¹ The other prong was to seek preferential access for one's own exports in industrial country markets.

protectionist demands while claiming the high ground and retaining legitimacy. Few, if any, observers have ascribed the blame for the failed negotiations to developing country obstructionism.

Clearly, there are flaws in the structure of the multilateral system as well as limits to what it can deliver, an observation reinforced by the events in Seattle. But Seattle should not deflect attention from India's pressing need to reform domestically and to harness multilateralism to this end. Multilateral engagement should be measured but broadly active and supportive, rather than defensive.

Section II spells out the advantages of an active engagement strategy, while drawing attention to its limits. Section III analyzes the issues that have emerged in some of the negotiating areas in the WTO. Finally, section IV offers concrete proposals that Indian negotiators might adopt in future discussions in the WTO. Section V concludes.

II. Multilateral Engagement: Whether and How

A major challenge facing India is how to institute and sustain good economic policies. Above all this challenge is a domestic one. Good policy should be geared, first of all, to injecting competition in the domestic economy. In the area of goods, this will involve reduction in trade barriers; in services, competition requires also eliminating barriers to entry. But good policy for both goods and services also includes judicious regulation, both to remedy market failures and to achieve social objectives efficiently.

It is clear that multilateral engagement cannot be an end-in-itself. Domestic policy priorities cannot be subordinated to the needs of such engagement nor must domestic reform be held entirely hostage to external bargaining imperatives. The important question is whether multilateral engagement can be harnessed to serve the ends of good domestic policies. Can it contribute meaningfully to overall policy reform, and if so how?

Multilateral engagement and the consequent international commitments undertaken by countries necessarily entails a loss in sovereignty—the freedom that countries have to make unconstrained choices. Globalization is ultimately a process of erosion of sovereignty induced by conscious policy actions or forced by market and technological developments. But sovereignty is not an absolute, overwhelming consideration that should trump all others. It can be partially and strategically ceded to further domestic policy reform and to secure an open trading system, which India, as a large and growing trader, has some ability to shape. A number of factors argue in favor of a reassessment of its approach to sovereignty and to the terms of its multilateral engagement.

A. Engagement as facilitating domestic reform and enhancing access through credible bargaining

The GATT/WTO is a quintessentially mercantilist bargaining framework where concessions to open each other's markets are exchanged. These concessions are legally binding commitments not to make policies affecting market access more restrictive than a certain stated level. Thus, a country may commit not to raise its

tariffs on bananas above 20% or commit to allow at least 5 foreign banks to enter its market. It is important to recognize that actual conditions of access may be, and often are, more liberal than those which are legally bound – actual tariffs on bananas may be only 10% and more than 5 foreign banks may actually be allowed to enter. Traders and investors value both the actual liberalization of markets and the legal guarantee of access.

In order to see when multilateral engagement can both facilitate domestic reforms and make it possible to extract concessions from trading partners, it is useful to examine three situations.

If a country is wedded to self-sufficiency, as India and other developing countries were until recently, it cannot be a bargainer. If you are not willing to open your markets, you do not have the most obvious means of inducing your trading partners to do so. Under the so-called special and differential treatment (S&D), developing countries sought, indeed could only seek, limited preferential access as supplicants, because of their own unwillingness to liberalize, rather than genuine non-preferential access as equal partners.²

Paradoxically, if a country is credibly committed to reform and can successfully implement it, it cannot be a credible bargainer either. Partner countries can basically free-ride on the internal commitment knowing that a refusal to engage in bargaining will not alter their market access interests. The situation does not change much if a reformer proceeds with liberalization unilaterally but refuses to bind the openness under the WTO in the hope of extracting concessions. This is because the value to partner countries of a binding by a credible reformer such as Singapore or Chile is small given the low probability of policy reversal.

A third situation, and one that applies to India in the current context, arises in relation to a willing reformer whose ability to implement reform is constrained by domestic opposition. In this case, domestic reform could be facilitated if a government could demonstrate that there were payoffs, in terms of increased access abroad, to domestic opening. The gainers from the increased access, be it exporters of textiles, software, professional services or other products, could represent a countervailing voice to groups (import-competing industries) resistant to reform. How effective such a strategy could be for Indian policymakers is unclear, but selling reform domestically should be that much easier if some external payoffs can be demonstrated.

China's recent agreement with the US on its accession to the WTO illustrates this political economy at work. In fact, in China's case, the external payoff, at least in the US market, is really not *increased* access, but securing existing access as it already receives MFN status in the US.³ China considers that its task of domestic reform is easier to sell and implement by pointing merely to increased security of existing access.

² Of course, this suited the protectionist interests in industrial countries because it allowed them to procrastinate on the liberalization of the two sectors where developing countries had intrinsic comparative advantage—agriculture and textiles.

³ Of course, this is an oversimplification because in some sectors such as textiles and clothing there will arguably be increased access.

Crucially, the need for improved foreign access to facilitate domestic reform (by easing the domestic political constraints) makes a country a more credible bargainer and enables it to extract more meaningful concessions from trading partners.⁴ A country can credibly say, “if I get less, I can deliver less domestic liberalization” in a manner that neither an unwilling reformer nor a wholly credible reformer can.

We would underscore here that the possibility of bargaining does not imply that unilateral reform should be delayed or held back in order to secure market access benefits. Indeed, much of the reform is likely to be implemented unilaterally. However, this process can be facilitated by multilateral engagement, and to that extent, the latter becomes important to address.

The distinction made above between alternative situations is important because there are some who argue that India should focus on pushing domestic reform without necessarily deepening its multilateral engagement. “Liberalize tariffs and investment unilaterally but don’t necessarily bind them” is a typical line taken by such observers. To us, such a view is founded on a simplistic or overly sanguine view about the prerequisites for successful reform. It renounces the use of forces that could be harnessed to secure domestic reform. And it forsakes the possibility of credibly extracting concessions from trading partners.

B. Engagement as commitment to good policies

Of course, there is some value to multilateral engagement and ceding sovereignty even if concessions cannot be extracted from partners. Sovereignty or the freedom to choose could be the freedom to chose badly. Indian trade policy-making has been a sad testament to bad unconstrained choices, choices that might have benefited from being constrained. Such constraints foster good policies in two respects: providing guarantees against reversal of current policies and facilitating future reform.

Even without harking back to the dirigiste days of the 1960s and 1970s, there have been instances of policy reversal, which might have benefited from some loss of sovereignty via a previous commitment to good policy. Despite undertaking commitments to bind tariffs in the Uruguay Round in 1994, India availed itself of large amounts of flexibility in the form of the wedge between the bound tariff and the actual tariff, particularly in agriculture. In 1996 and 1997, the government, in the face of fiscal pressures, decided to raise tariffs and use up some of the water in the tariff. From the government’s perspective, the decision to provide for a cushion or a margin of maneuver was vindicated by its subsequent actions. But from a welfare perspective, this freedom that the government had was in fact counter-productive. Had the Uruguay Round bindings been really binding, it would have forced the government to choose a superior instrument - one that was neutral between imports and domestically produced goods - to meet its fiscal needs.⁵

⁴ The Indian experience with TRIPS illustrates this point. The fact of the considerable domestic opposition to higher patent protection brought home to trading partners the realization that without offsetting compensation it would be extremely difficult for India to accede to their TRIPs demands.

⁵ There are several other examples of benefits from binding international rules. For instance, the recent WTO rulings will lead to the elimination of quotas that India has for long and inappropriately maintained for balance of payments reasons. Even though, India’s commitments to phase out local

One reason for the reluctance of the Government to liberalize immediately is the perceived need to protect the incumbent domestic suppliers from immediate competition - either because of the infant industry type of argument or to facilitate "orderly exit". And one reason for the failure of infant industry policies in the past, and the innumerable examples of perpetual infancy, was the inability of the Government to commit itself credibly to liberalize at some future date - either because it has a stake in the national firm's continued operation, or because it is vulnerable to pressure from interest groups which benefit from protection. The WTO offers a valuable mechanism to overcome this difficulty. In the services negotiations, for instance, many governments precommitted to future liberalization, thus striking a balance between the reluctance to unleash competition immediately and the desire not to be held hostage in perpetuity to the weakness of domestic industry or to vested interests. But India failed to take advantage of this mechanism, and committed only to review its policies in basic telecommunications at specified future dates.

C. Engagement as enforcement of rights

It is a truism that in a situation of asymmetry, a rules-based system protects, albeit imperfectly, the weaker party. This is especially true when it comes to enforcement of rules that have been already established. Warts and all, the WTO dispute settlement system has lived up to this requirement in offering recourse to developing countries to enforce their rights. Table 1 tabulates the complaints that have been notified in the WTO. Developing countries account for about one-third of all the complaints and have been defendants in forty percent of the complaints. Developing countries have won all the cases that they have brought against the developed countries. India has successfully prosecuted all three cases against developed country partners. The fact that developing countries have been defendants in a lot of cases, even unsuccessful defendants, is actually reaffirmation of the usefulness of the system as a safeguard, at least insofar as it reflects reduced extra-systemic pressure. To settle disputes within the system affords greater protection to the weaker party than settling outside it.

While the experience of dispute settlement affords some comfort, it could be argued that on the really big issues, where real interests are at stake, there is still the possibility that developing countries will be ineffective at enforcing their rights. The banana and hormones disputes where compliance by larger trading partners has been delayed or absent warrant caution. More generally there is the perception that developing countries' ability to secure compliance by the larger traders is ultimately limited by the small size of developing country markets and the consequential limited impact of any retaliatory actions.

This problem acquires fresh urgency in the current international trading context because of increasing fears that the quantitative restrictions imposed on textile products by industrial countries will not be eliminated early in the next millennium as required by the Uruguay Round textiles agreement. The stakes are high for India which should, given the right domestic policy environment, stand to gain from the elimination of the quotas or stand to lose if there is backtracking by trading partners.

content requirements under the TRIMs agreement has not prevented the recent reimposition of such requirements in the automobile sector, they could be challenged by partner countries.

Do developing countries such as India have the clout to ensure compliance with commitments or must they resign themselves to ineffectiveness, believing that outcomes are beyond their ability to influence? We argue below that India can wield an effective retaliatory weapon in the form of its TRIPs obligations and should seriously consider changing its intellectual property legislation to allow for this possibility.

D. Multilateral engagement as a bulwark against regionalism

There are very few multilateral traders left in this world and India has for the most part been one of those lone battlers.⁶ Championing multilateralism is no longer a slogan because its erosion through regional agreements is having a serious if unrecognized impact on India's trade and could have similar consequences in the future. We provide a particularly stark example below in relation to NAFTA. Multilateral tariffs must come down if this policy-induced advantage is to be leveled and India therefore has a strong interest in seeking to reduce tariffs on all industrial products including textiles and clothing.

A future area of concern for multilateral traders is the proliferation of mutual recognition agreements—whereby countries choose to accept the standards of some but not all partner countries. These agreements are conceptually analogous to preferential trading arrangements with all the possible adverse impacts on those countries that are excluded from these agreements. Strengthening the provisions in goods and services on preferential trading arrangements is overdue.

E. Negotiating pessimism

It is easy to be critical of the old obstructionist approach of developing countries which was founded on a belief in self-sufficiency and inward-looking policies. But a more complex question facing developing countries now is whether the liberal policies being pursued at home need to be “multilateralized.” Naysayers highlight the continuing asymmetry of bargaining power, which affects agenda-setting and rule-making, and conclude a kind of negotiating pessimism. They accept that domestic liberalization could be used as negotiating coinage to obtain market access abroad. But they conclude that items of interest to India, such as improved market access for its services exports through movement of individuals, as well as for textiles and clothing will not be seriously addressed by trading partners. On the other hand, the agenda will be dominated by the interests of the economically powerful countries, ranging from TRIPS in the past, to labor and environmental standards, competition and investment policy, and government procurement in the future. Seattle dictates that these allegations be taken very seriously.

To some extent, this reluctance to engage more proactively is based on a certain justified diffidence to which the TRIPs experience has contributed. This fear, which can be dubbed as the thin-end-of-the-wedge syndrome, attaches a certain cost to engagement and emanates from one particular view of the negotiating process: once developing countries accede to the demand to *discuss* any of these issues, there will be an irresistible tide that developing country will not be able to control and that will

⁶ The recent initiatives in the South Asian region are an exception to India's general preference for multilateralism.

inexorably lead to an outcome inimical to their interests. In such an environment, it is argued, bargaining is simply not attractive to engage in.

On negotiating pessimism, we would make several observations. First of all, India's indiscriminately negative approach to the introduction of new issues in the negotiating agenda needs to be reconsidered. It is essential to distinguish between issues in which the negotiating outcome will inevitably be inimical to India's interests, and those in which even the worst case scenario does not imply unfavourable consequences. It was right to resist insidious protectionism in the form of higher labor and environmental standards or rent transfer mechanisms such as the TRIPs agreement. But, as we argue below, it is difficult to justify the objection to the introduction of competition policy and disciplines on government procurement, unless we accept that complete national sovereignty is to be valued above improved policy at home and improved access to foreign markets.

Second, the prospects for significant gains in market access are not as bleak as they have been hitherto. Especially, in the area of labor mobility, with labor shortages developing in the US, the environment might be more propitious than it has ever been. Moreover, negotiating pessimism is an empirical proposition that needs to be seriously tested. India has never really done so because of its own unwillingness to make concessions and open its markets. And internationally, India has aligned itself consistently with countries that have argued for closed rather than open policies. The way to test negotiating pessimism and even ameliorate it is for India to align itself with coalitions that form on a shared premise of liberal policies. Coalitions need not be fixed but could vary depending on the issue. For example, India's natural allies should be the Cairns group in agriculture, Japan and Hong Kong on antidumping, and the EU on investment and competition policies.

Of course, there is no guarantee of success in the short term. But in the longer term, good arguments and pro-liberalization coalitions can be successful. Moreover, if India is identified as a strong clear voice in favor of open competitive markets, its opposition to disguised protectionism in the form of inclusion of labor or environmental standards will be more credible. The opposition will be seen as founded on substance rather than ritual defensiveness. The success of developing countries in resisting the inclusion of labor standards in Seattle attests to the influence that can be wielded by them.

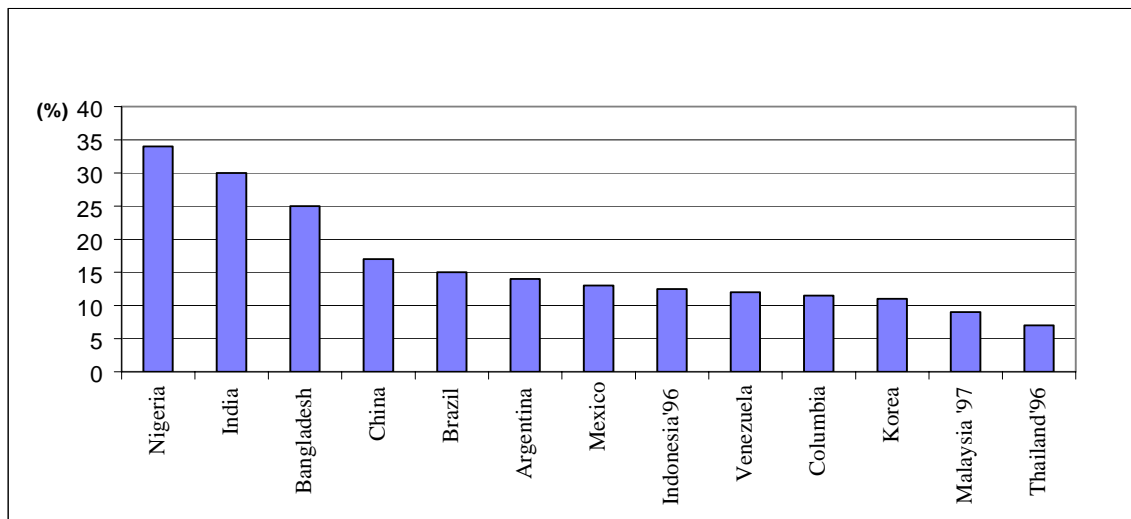
III. Issues in Selected Sectors

A. Manufacturing

India has an unambiguous interest in actively seeking negotiations to bring down tariffs on industrial products.⁷ The interest is fourfold. First, India's tariffs today, even after significant reform, remain exceptionally high and almost the highest in the world (Chart 2). Further liberalization is desirable but difficult for internal reasons and this domestic situation could yield negotiating coinage in the next round.

⁷ See Hertel and Martin (1999) for a quantification of the benefits from further global liberalization of manufacturing tariffs.

Chart 2: Cross-Country Comparison of Average Tariff Rates (1998)



Source: World Bank (forthcoming)

Second, even if the pace of further liberalization is divorced from external bargaining imperatives, India has a strong interest in reducing the level of its Uruguay Round bound tariffs. The wedge between the applied and bound remains high and creates uncertainty and lack of predictability about trade policy (Table 2). According to a recent survey domestic investors appear not to have confidence in the stability of government policies (Table 3). Bringing bound levels closer to current and future applied levels can engender confidence in the predictability of policies. Recent tariff policy increases - the special additional duty of 4 percentage points imposed in 1998-99⁸ and the surcharge equivalent to 10 percent of the basic customs duty levied in 1999-2000 - illustrate the costs of not having tighter external discipline on trade policies. Had such discipline existed in the form of bindings that “bit”, the government would have been forced to raise revenues through alternative, trade-neutral and hence less costly measures.

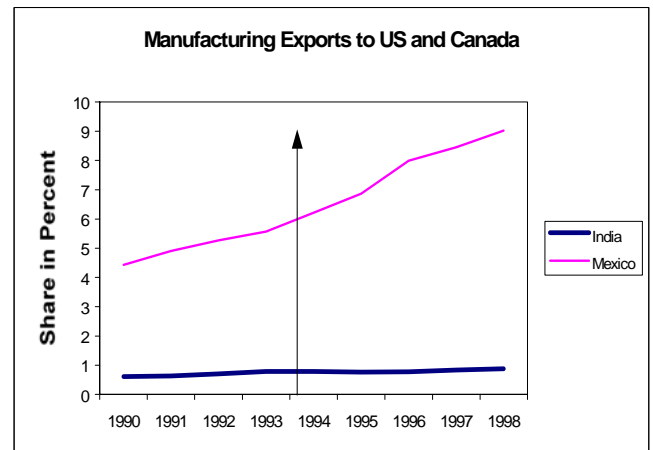
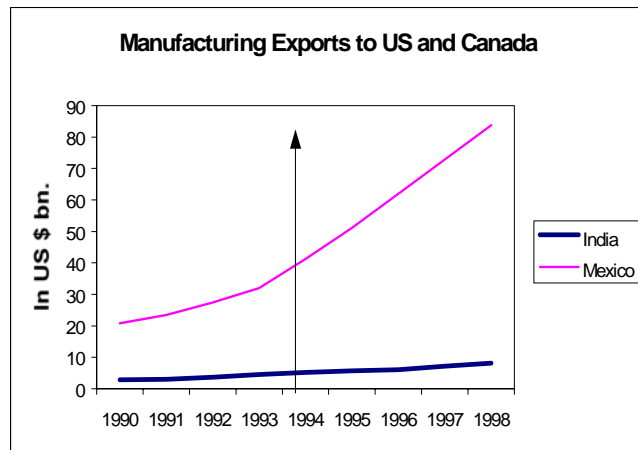
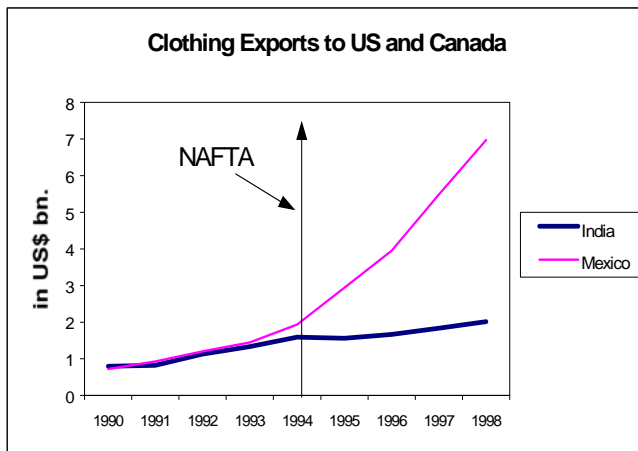
Third, reductions in tariffs by partner countries will have important market access effects for India. Further reductions, particularly in tariffs on textiles and clothing, are likely to improve India’s terms-of-trade and yield sizable welfare benefits.⁹

One particularly important aspect of these market access effects, and perhaps the most compelling reason for seeking cuts in tariffs in the textiles, clothing, and leather sectors, relates to *trade diversion*. In the current environment, such reductions are necessary to arrest the trade diversion that MFN traders such as India have suffered as a result of regional agreements. We present one example - in relation to NAFTA - which brings home starkly this impact. It is likely that there are similar effects in the EU market stemming from preferential arrangements between the EU on the one hand and Eastern European and Mediterranean countries on the other.

⁸ Although this measure was intended to rectify negative protection by imposing a tax on imported goods whose domestic counterparts already faced a 4 percent sales duty, the manner in which it was levied resulted in affording some extra protection to domestically produced goods.

⁹ See Hertel and Martin (1999).

Chart 3: Exports of India and Mexico to North American Market, 1990-1998



Source: UN COMTRADE Database

Chart 3 shows the evolution in India's and Mexico's exports to the US before and after NAFTA. Between 1990 and 1998, Mexico's manufacturing exports to the US grew by about US\$46 billion, while India registered an increase of US\$ 5 billion. In clothing where India is assured a certain absolute quantitative outcome by virtue of the MFA quotas, India's share of total US and Canadian imports declined after NAFTA: between 1994 and 1998, India's share declined by 0.5 percentage points, from 3.9 to 3.4 percent. Over the same period, Mexico's share rose from 4.7 percent to 11.8 percent, an increase of over 7 percentage points, translating into US\$ 18 billion of *additional* exports.

In the case of clothing, NAFTA opened up a preference margin for Mexico equal to the implicit tariff on India's export quotas. Even after the abolition of the MFA, when the implicit tariff comes down, the margin of preference will decline but will remain substantial, between 15 and 40 percent, depending on the product line. MFN tariffs must come down if this policy-induced advantage is to be leveled. India, therefore,

has a strong interest in seeking to reduce tariffs on all industrial products, especially textiles and clothing.

Can these trade diversion costs be offset through alternative means, for example, by disciplining the use of Article XXIV? This is unlikely for two reasons: first, there are too many large preferential traders already who are likely to resist the fundamental changes to Article XXIV that are necessary to address the trade diversion inflicted on third countries. Second, even if these changes can be effected, they will not be applied retroactively. The effects of all past regional agreements, including NAFTA and the EU-Eastern European agreements, cannot be undone through rule-making; they will have to be addressed by eliminating the trade-diverting effects of regionalism at source - the MFN tariff.

*B. Agriculture*¹⁰

Agriculture illustrates most starkly the disjunction between India's domestic policies and its external negotiating position. High tariffs for manufacturing, combined until recently with restrictions on exports of agricultural products, have led to an incentive structure that taxes rather than protects agriculture. And although manufacturing tariffs have been reduced and most export restrictions eliminated, manufacturing continues to be favored relative to agriculture. Yet, India's multilateral position is one of defensiveness seeking the freedom to protect rather than exploiting actual and potential comparative advantage by seeking an open regime internationally.

India's agricultural trade policy regime is characterized by some import QRs, many of which are likely to be eliminated as a result of WTO panel rulings on disputes between India and trading partners over India's invocation of balance of payments grounds for maintaining QRs.

India's average applied tariffs in agriculture are 26 percent while bound rates in the WTO are 94 percent, a wedge of 68 percentage points (Table 2). In about 83 percent of agricultural tariff lines, the wedge is over 50 percent (Table 4). The major items such as rice (applied tariff of 0 percent), skimmed milk (0 percent), wheat (0 percent), pulses (0 percent), sugar (25 percent), and edible oils (15 percent) are virtually fully integrated with world markets (except of course for the export QRs) even though the bound rate is extremely high.¹¹ On domestic support, total AMS tends to be negative, suggesting taxation rather than protection of agriculture. On export competition, Indian agricultural exporters do not receive any direct export subsidies. However, there is some support in the form of exemption of agricultural export profits from income tax and subsidies on freight and for certain floriculture and horticultural exports.

At the same time, India has significant actual and potential agricultural exports in rice, sugar, dairy products, cotton, and processed foods, and in the long run even in cereals. These exporting possibilities will be more fully realized as the discrimination against agriculture is fully eliminated.

¹⁰ This section draws heavily on Gulati (1999)

¹¹ However, state trading enterprises continue to influence trade in agricultural products.

This combination of a relatively unprotected domestic regime and potential comparative advantage means that India has a real interest in seeking to eliminate protection in international agricultural markets. India's sugar and dairy exporters have already expressed a serious interest in reducing barriers to their exports. As in manufacturing, India also suffers from the preferences granted to competing suppliers in sectors such as sugar. It therefore has a real interest in reducing agricultural tariffs as well.

And yet, India's position is defensive, continuing to focus on the freedom to protect to safeguard food security.¹² India should seriously consider aligning itself with the Cairns group of agricultural exporters consistent with an overall strategy of forming coalitions based on a liberalizing ideology. In this regard, many of the specific proposals in Gulati (1999), including elimination of export subsidies, elimination of tariff quotas, moving from aggregate AMS to product-specific AMS commitments, and disciplining blue box measures are worthy of consideration.

*C. Intellectual property*¹³

The main issues in TRIPs are: using TRIPs as a device for ensuring partner country compliance; developing domestic policies and institutions to offset some of the more egregious impact of TRIPs¹⁴ and harness the benefits of IP protection in other areas; and developing mechanisms for national and international protection for IP produced in India.¹⁵

TRIPs as an enforcement device

How can the commitment by industrial countries to remove all the MFA textile quotas ("walk off the cliff") come January 1 2004 be enforced? The answer seems to be that if the industrial countries renege on their commitment in textiles, developing countries should withdraw or threaten to withdraw their TRIPs obligations. In principle, cross-retaliation in TRIPs could be a weapon for developing countries, but the peculiarities of IP make it more difficult than in other areas.¹⁶ In a recent proposal (Subramanian and Wattal (2000)), it is argued that such cross-retaliation, if designed with care, can be feasible, effective, and probably legal.

The essence of the proposal is that India should alter its draft IP legislation to specify that the Indian executive retains the right to revoke some of the IP rights of foreign patent owners in the event that partner countries fail to comply with commitments that

¹² As Gulati (1999) argues, food security concerns can be adequately addressed through policies other than domestic trade protection.

¹³ This section draws heavily on Subramanian (1999).

¹⁴ The Uruguay Round TRIPs agreement did impose costs on India, particularly in the pharmaceutical sector (see Subramanian (1995)), which are likely to be felt in the early part of the next century.

¹⁵ There are a number of issues that have generated well-entrenched and occasionally extreme positions such as compulsory licensing for non-working, parallel imports, transfer of technology, and restrictive business practices. However, these issues are either not seriously important or misguided (see Subramanian (1999) for a fuller discussion). They should be spared negotiating effort and time.

¹⁶ To see why, it is important to recall that IPRs are private rights conferred through domestic legislation. While it is easy to raise tariffs in retaliation, to withdraw private rights granted through domestic legislation would be very difficult, perhaps even unconstitutional in many legal systems. Furthermore, withdrawing rights would be of little value unless alternative sources of production for the patented product can be found.

affect India's market access. Specifying that this revocation would only be pursuant to a WTO authorization to retaliate would preserve its WTO-legality. Several options present themselves in terms of the form and timing of the revocation. However, one question that needs to be considered is whether current rules that allow retaliation across sectors only as a final resort circumscribe the ability of countries to use such retaliation effectively. India should be able to argue that retaliation within goods for noncompliance by partners in goods is not "practicable." Retaliation in TRIPs has the attractive property that, if implemented, it would be welfare enhancing, and therefore credible and practicable. The ability to use TRIPs as a retaliation device would also address broader concerns about the asymmetry of the WTO dispute settlement process and the lack of retaliatory power for developing countries.¹⁷

Developing domestic policies and institutions

The two most important policy instruments available to India to mitigate some of the effects of the high levels of patent protection are compulsory licensing and competition policies. India needs therefore both to implement a new competition policy and develop the capability to use compulsory licensing effectively. The flexibility afforded by compulsory licensing comes in two forms: first, countries are virtually unrestricted in the circumstances under which they can grant compulsory licences.¹⁸ Second, while a number of conditions need to be fulfilled when these licences are granted, it is possible for national authorities to meet them and yet dilute the monopolistic impact of the proprietary protection granted in the first place (Wattal (2000)).

The advantages of deploying competition policy are twofold. First, there is some latitude in determining the optimal degree of protection that balances the need to foster innovation while ensuring technological diffusion and consumer protection. For example, what constitutes abusive pricing is a question that will admit of a wide variety of answers.

The second advantage follows from the language of the TRIPs agreement. There is even greater flexibility in the use of compulsory licences - in two key respects - when they are granted to remedy anti-competitive practices,¹⁹ which could be usefully harnessed by India.

A really crucial public policy issue that arises in relation to use of new technologies (biotechnology, including genetic modification) is how to harness their benefits while minimizing the attendant risks to consumer safety, biodiversity, health, and the environment. In India as in other countries, opposition to the use of these technologies can be vocal and sometimes extreme. But if these concerns are to be addressed, there must be a domestic regulatory body and process that makes informed

¹⁷ It is notable that Ecuador has taken similar steps in retaliating against the European Union for its failure to remedy the WTO-inconsistencies in its banana import regime.

¹⁸ The only grounds on which compulsory licences cannot be granted is non-working of the patent locally.

¹⁹ When compulsory licences are used to remedy anti-competitive practices, the TRIPs agreement provides that (i) no case needs to be made that the patentee was unwilling to license the patent on reasonable commercial terms as a precondition for granting the compulsory licence; and (ii) the principle that remuneration for the compulsory licence should be "adequate" need not be respected.

and transparent public policy choices and commands public trust. Existing institutions need to be strengthened along the lines of the FDA in the US.

Indian intellectual property: genetic resources, indigenous knowledge, and geographical indications

India and other developing countries have made sensible proposals seeking greater protection for “intellectual property” generated in these countries in the form of indigenous knowledge and geographical indications.²⁰ But a challenging agenda of research and policy lies ahead. How extensive are genetic resources and indigenous knowledge and to what uses can they be put? How important is the potential economic value of these resources? And finally, how should a proprietary right be created that is enforceable internationally, and that rewards agents, including traditional communities, to preserve and create such resources and knowledge? Similar questions arise in relation to geographical indications. How can names in the public domain be restored to proprietary protection? In these areas, a credible international negotiating position can be built if such systems of protection are instituted within India and shown to be workable.

In relation to the new technologies, India’s involuntary response seems to be to favor low levels of protection - for plant varieties and biotechnological inventions. But this is not a position that is based on underlying research. A case could be made that stronger proprietary protection in these areas could generate some dynamic benefits for India either in the form of research *by* Indians, *in* India, or *on* products and technologies of value to India. Some research on agriculture in India (Pray and Basant (1999) and Pray and Ramaswami (1999)) suggests that these dynamic benefits could be significant. More research to underpin informed policy positions is warranted.

D. Anti-dumping

The use of anti-dumping has spread significantly from the five original industrial country users (Australia, Canada, the EU, New Zealand and the US) to developing countries, including India. Since mid-1997, India has initiated 21 antidumping cases. It ranks as one of the largest users of antidumping actions (see Table 5), and the ambitions in this area are escalating, reflected in the recent upgradation of the antidumping cell into a full-fledged directorate.

At the same time, India is also a major victim of antidumping actions, in fact the worst hit if measured in terms of antidumping actions per dollar of exports (Table 6). While the loss associated with the latter resonates easily with policy makers and the public, it is the domestic use of antidumping that arguably represents the major threat.

The only justifiable use of antidumping - to correct predatory price behavior by foreigners - requires exporters to have market power. This is implausible in the Indian context because in a number of antidumping actions there were imports from 20 or more countries. In those cases where suppliers were few, discipline was present in the form of rival domestic firms (see World Bank (forthcoming)).

²⁰ On geographical indications, it might be sensible for India to seek to form an alliance with the European Union which is a major demandeur in this area.

Given the fact that the cost of protection increases at an increasing rate, antidumping by India is worse in its impact than elsewhere because it is levied on top of tariffs that are high and certainly higher than other antidumping users. Antidumping could turn out to be the nocturnal Penelope: undoing the liberalization unleashed by the tariff reductions. Further, the experience from other countries has been that antidumping actions are typically taken against the most efficient suppliers. This in turn signals other exporters to raise prices, inflicting terms of trade losses.

The serious costs of antidumping to India - both as victim and perpetrator -mean that it should push strongly for reforming antidumping provisions. The most intellectually coherent approach would be to fold antidumping into competition law provisions on predation which would provide the appropriate safeguards against protectionist use of AD. Alternatively, AD laws should be required to incorporate buyer/consumer interests and provide meaningful representation for such interests in AD proceedings. India's proposals have focussed on specific provisions and amounted to tinkering at the margin rather than in eradicating the menace altogether.

*E. Services*²¹

In services, the most important initiatives need to be taken at the domestic level. Nevertheless, there remains scope for constructive use of the multilateral trading system both in realizing credible domestic liberalization and securing market access abroad. Before we elaborate on these themes it is instructive to recall what we have learnt about services trade liberalization.

(i) There are substantial gains both from liberalization within countries, especially in key infrastructure services like telecommunications, transport and financial services, and from the elimination of barriers to their exports.

(ii) Successful liberalization requires

- Emphasis on competition more than a change of ownership
- Credibility of policy and liberalization programs
- Domestic regulations to remedy market failure and pursue legitimate social goals with economic efficiency

(iii) Effective market access requires

- Elimination of explicit restrictions
- Disciplines on implicit regulatory barriers

In India, the untrammelled freedom to chose policy in services has led to unwise policy choices. Not only have the pace and extent of liberalization been modest, its pattern has also been poorly conceived. In each of the three key infrastructure sectors, there has been a reluctance to introduce meaningful competition through unimpeded entry; limited liberalization to foreign participation has been grudgingly allowed with limitations on both equity and numbers, perpetuating imperfectly competitive

²¹ Throughout this paper, services trade will refer not only cross-border delivery, as in the case of goods, but also supply through the establishment of firms and movement of individuals.

structures; there have been significant policy reversals, for example in power and telecommunications with loss to policy credibility; and while due recognition has been accorded to domestic regulation, it has been late in coming and imperfect in operation. Moreover, the multilateral route has not been used to any significant extent to liberalize or to precommit to future liberalization.

Table 7 summarizes how the policy choices made by India in three key service sectors have impeded effective competition. In all these sectors, limited freedom of establishment coupled with restrictions on competition through alternative modes, has led to imperfectly competitive markets which has raised costs and facilitated rent appropriation by foreign firms.

Table 8 and Chart 4 depict some of the effects of these policy choices in telecommunications and transport, respectively.²² Table 8 compares the price of international calls in several countries, with the call from the United States to the country in question serving as the benchmark (since the United States is one of the most competitive markets). In the case of India, the benchmark is itself inflated because providers based in the United States are obliged to pay the Indian monopolist the settlement rate for terminating their calls, and this inflates their price. Nevertheless, we find that the price of calling from India is nearly *twice* this overstated internationally competitive price. This is significantly higher in absolute and relative terms than the price from locations such as Hong Kong and Australia where competition has been introduced, and from Singapore where call-back services have been permitted to eat away at monopolistic price margins.

Chart 4 compares the transport and insurance costs for Indian exports to the US with those for Singapore and other countries. The United States is one of the few countries which collects statistics on its imports on both a fob and cif basis. The difference provides a rough measure of *ad valorem* transport and insurance costs. Estimates of *ad valorem* nominal tariffs are also presented. Insofar as India exports lower value products than Singapore the *ad valorem* transport cost estimates for India are likely to be biased upward. Nevertheless, it is particularly striking that even though India faces lower applied tariffs than Singapore in sectors of major export interest like apparel articles and accessories, iron and steel articles, and electric machinery, its higher transport and insurance costs more than offset this advantage so that the total incidence of transport costs and tariffs is greater. The picture looks more worrying when India is compared with all other countries (which is a less efficient benchmark than Singapore). Transport and insurance costs are nearly twice as high than for all countries.

Securing market access: Natural persons

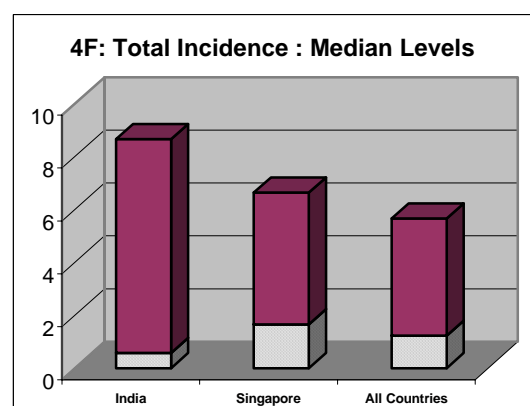
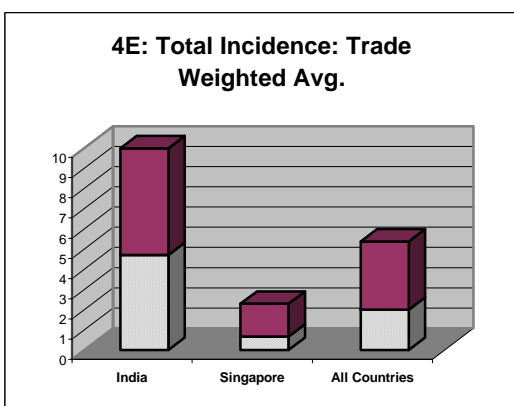
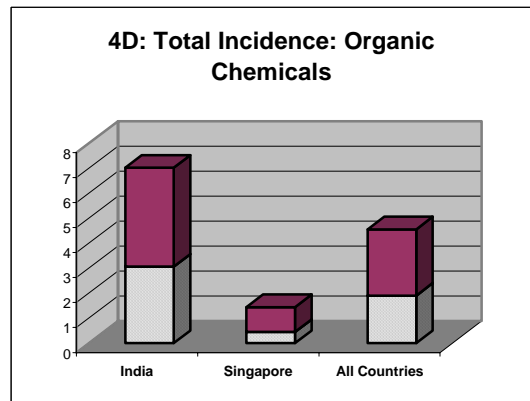
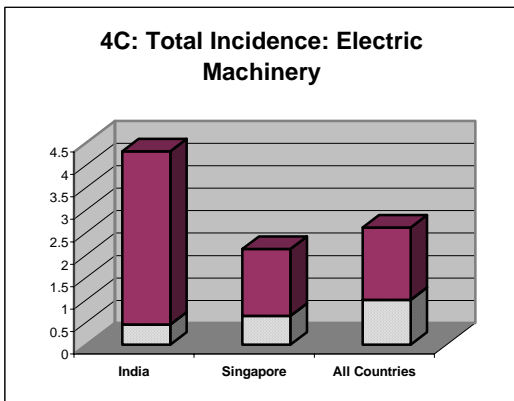
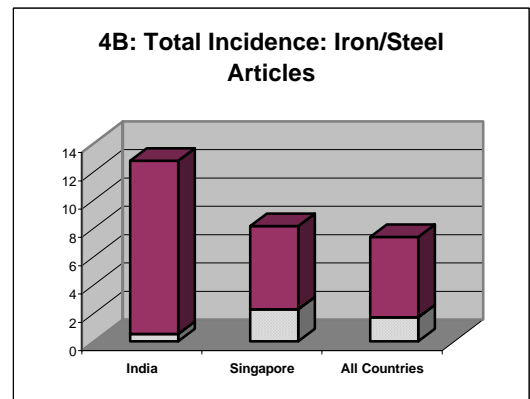
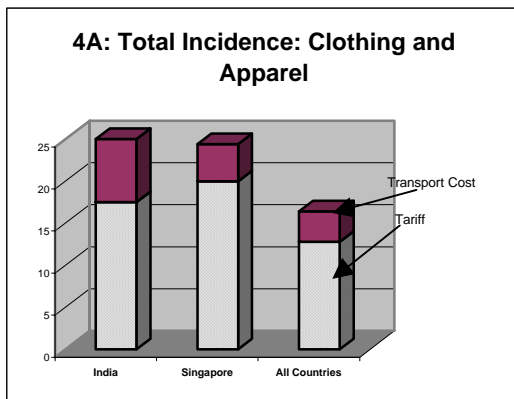
There is no doubt that the Uruguay Round outcome in services was unbalanced. The much-touted trade-off between modes of delivery simply did not take place. Although antipathy to commitments on labor mobility in partner countries was a major contributing factor, an unwillingness on the part of India to open up domestic services markets made its demands for labor mobility difficult to sustain. With India opening up its markets, that bargaining dynamic can change and the prospects for

²² See Chadha (1999) for a general equilibrium analysis of the benefits to India of liberalizing services trade.

serious inter-modal trade-offs -obtaining labor movement in return for allowing greater commercial presence for foreign service providers - must be greater now. Also, the fact of severe shortages of skilled labor in the US and the powerful constituency of high-technology companies lobbying for relaxation of visa limits makes this a propitious time to put labor mobility squarely on the negotiating agenda.²³ That India has a strong comparative advantage in some of the high-skilled

²³ The notions of the US as the unrivaled centre of technology and the role of technological progress in motoring the recent US economic expansion resonate deeply with the US public. They would therefore be loath to countenance any obstacles to this march of progress even if it involves greater imports of labor-related services.

Chart 4: Total Incidence of Transport Costs, Insurance Costs and Tariffs on Exports to the US: India and Other Countries



Note: Ad valorem transport and insurance costs are stacked above ad valorem tariff. Total Incidence is measured as the sum of these costs for each of the above mentioned categories.

Source: Research in progress by Fink and Mattoo, World Bank, 1999

labor-intensive sectors is beyond doubt and Table 9 emphasizes this point in the case of software services.

India's defensive position on services liberalization impedes the possibility of credibly advancing India's labor-related services through inter-modal trade-offs. More specifically, the resistance to the use of horizontal formulae in negotiations and the insistence on a request and offer approach may be ill-advised. Mattoo and Olarreaga (2000) have elaborated a specific proposal, based on the use of formulae, which can serve to extract meaningful commitments on the movement of individual service suppliers from trading partners.

In essence, this proposal would require a country to provide increased "foreign labour content entitlements" to their domestic firms in relation to the country's increased exports of services.²⁴ The proposal offers several advantages. First, it is internationally symmetric. All countries would be obliged to create such entitlements, though how much they are used would be determined by sound economic considerations of modal comparative advantage. The entitlements would not be bilateral, but international. Second it is based on a balance of concessions, an appealing principle in trade negotiations. Exporters of labor services would receive benefits commensurate with efforts to open up their domestic services markets. Finally, the scheme is also attractive because it generates a desirable liberalizing momentum. Conventional mercantilist negotiations on trade barriers create a holdback problem: I would rather give less to get more from you. But since the proposed scheme implies that my export possibilities are based on your actual exports, it induces me to be more open.

F. Electronic commerce

WTO Members have decided that electronic delivery of products will continue to be free from customs duties. For the moment this commitment is temporary and political, but there are proposals to make it durable and legally binding. Two aspects of the commitment are notable. First, only electronic transmissions are covered; goods ordered through electronic means but imported through normal channels are explicitly excluded. Secondly, the standstill/prohibition applies only to customs duties; there is no mention of other forms of restrictions.

Fortunately most electronic commerce is already free of barriers (except of course those created by differences in standards), and so the objective is really to bind this existing openness to preclude the introduction of new barriers. But is duty-free electronic commerce the appropriate route?

India was initially opposed to the decision on duty free treatment for electronic commerce,²⁵ concerned that it would hurt tariff revenue. But more recently, there has

²⁴ In a way Bill Gates' recent testimony before congress arguing for the need to allow more software engineers to enter to maintain international competitiveness is not far-removed from the suggested scheme.

²⁵ In principle, all types of products can be advertised and purchased over electronic networks, the potential for electronic delivery, and the scope of the WTO decision not to impose duties is more limited. It requires that a final product be presented as digitalized information and transmitted electronically, typically over the Internet. The bulk of the products that can be supplied in this manner are services, financial, legal, customized software, etc. Some information and entertainment products

been a change in position. Perhaps thanks to the growing importance of software exports, India has now joined the many countries that are in support of the existing political decision on duty-free treatment for electronic commerce to be made legally binding. We would argue that the initial inhibitions and the current enthusiasm are both misplaced and do not further India's real commercial interests.

The initial inhibitions were founded on fears of revenue loss. Mattoo and Schuknecht (1999) estimated the tariff revenue countries collected from these products.²⁶ Even if all delivery of digitizable media products moved online – an unlikely prospect – the revenue loss would be minimal. India would lose 0.4 per cent of tariff revenue and 0.1 per cent of total revenue.

Equally, the current enthusiasm is also misplaced as the value of liberating e-commerce from duties is either superfluous or virtually devoid of value. Since the bulk of such commerce concerns services, the relevant regime is that established by the GATS regime on cross-border trade. This Agreement allows countries to decide whether to commit to market access, i.e. not to impose quotas, and to national treatment, i.e. not to discriminate in any way against foreign services and suppliers. If a country has already made such a commitment, then any further promise not to impose duties is superfluous because customs duties inherently discriminate against foreign services. If a country has not made such a commitment, then the promise not to impose customs duties is worth little, because a country remains free to impede access through discriminatory internal taxation – which has been carefully excluded from the scope of the decision. Worse the prohibition of such duties, may induce recourse to quotas which are ironically still permissible in spite of being economically inferior instruments.

Hence, the focus on duty-free treatment is misplaced. The objective for countries like India should rather be to push trading partners into making deeper and wider commitments under the GATS on cross-border trade regarding market access (which would preclude quantitative restrictions) and national treatment (which would preclude all forms of discriminatory taxation).

Table 10 summarizes the current state of commitments on cross-border supply in some of the areas in which developing countries have an export interest. In software implementation and data processing, of the total WTO Membership of over 130, only 56 and 54 Members, respectively, have made commitments; and only around half of these commitments guarantee unrestricted market access, and a similar proportion guarantee unqualified national treatment. In all professional services, there are commitments from 74 Members, but less than a fifth assure unrestricted market

typically characterized as goods, such as books, standardized software, music and videos embody digitalized information that can also be supplied electronically over the Internet.

²⁶ Services are not subject to customs duties as far as we know. So we need concern ourselves only with the fiscal implications if international trade in digitizable products currently classified as goods shifts to the Internet, and if no tariffs are levied on such products. The estimates are reasonably reliable for the most important categories where trade and tariff data were available for the most important countries. A few data problems persist as volume data for some products facing specific tariffs were not available, sometimes the tariff rate was not provided, and applied tariff rates for some of the smaller countries were not available.

access and national treatment, respectively. There clearly remains considerable scope for widening and deepening commitments.

G. Government procurement

There are many good reasons to liberalise government procurement. Some benefits are analogous to those arising from the liberalisation of trade, but to these must be added the budgetary benefits of efficient procurement and significant reductions in rent-seeking which is rampant in procurement. Thus, both the consumer and the taxpayer will benefit. But WTO experience shows that most countries (developed and developing) are reluctant to immediately accept full liberalisation of procurement.

For India, Srivastava (1999) estimates that the total value of purchases by the central and state governments and public enterprises, which could in principle be subject to international government procurement rules, varies between 3.4 and 5.7 percent of GDP. For certain procurement contracts, a price preference of 15 per cent is given to indigenous equipment suppliers, requiring that at least 20 per cent value must be added in India. In the shipping sector, price preferences up to 30 per cent apply to Indian bidders on procurement contracts. If more efficient procurement practices can be implemented domestically, Srivastava (1999) calculates that the total savings could be as much as 1.7 percent of GDP or about US\$ 8 billion. Even if only a fraction of the estimated savings is realized, the gain can be substantial.

It is clear once again that India has exercised the freedom to choose in ways that are probably very costly for consumers and taxpayers. Even if it had chosen wisely, it is reasonable to ask whether a multilateral agreement can add to national legislation which often contains similar provisions to mitigate agency problems? One of the biggest problems in procurement is that of moral hazard on the part of the procurer. For instance, a recent survey conducted by the Confederation of Indian Industries shows that procurement contracts frequently involve corruption. The significant benefit of a multilateral agreement is in helping to overcome national agency problems in procurement by creating mechanisms for reciprocal international monitoring supported by multilateral enforcement. It achieves this by shifting the legal scope for monitoring from dispersed taxpayers, who may have little interest in monitoring individual procurement decisions, to the bidders for contracts who have a significant stake.

Two elements of a possible multilateral agreement are crucial in this context. First, the agency problem is mitigated by creating obligations on the procurer to be transparent. Secondly, foreign suppliers are given the opportunity to challenge the decisions of the procurer before national courts or independent and impartial review bodies. As a starting point, it would seem both desirable and feasible for India to be open to commitments on increased transparency and strengthened enforcement.²⁷ This is in fact the *raison d'être* of the Working Group on Transparency in Government Procurement.

²⁷ It has also been suggested that countries could continue to maintain preference margins, but agree to bind them and make them subject to unilateral or negotiated reductions - in a manner analogous to tariffs.

In addition to improved domestic policy, government procurement offers the potential for making negotiating linkages. Foreign suppliers can only effectively contest the market for government procurement if they are not unduly handicapped by restrictive trade measures. Hence, the creation of genuine international competition for procurement contracts depends crucially on the liberalisation of trade. It would, therefore, be natural for developing countries to make their willingness to accept disciplines on government procurement depend on future negotiations on market access for goods and under the GATS on measures affecting trade in services.

For instance, one of the most important services sectors in the context of government procurement is construction. Yet in the GATS, Members have usually not bound themselves to grant market access to the supply of construction services through the presence of natural persons, except for certain limited categories of intra-corporate transferees. The assurance that workers can be temporarily moved to construction sites would greatly increase the benefit of non-discriminatory government procurement for developing countries. The same applies to procurement of other services such as software and transport.

H. Standards and related domestic regulations

Effective market access for both goods and services requires the elimination not only of explicit restrictions, but also of the implicit barriers created by standards and other domestic regulations. In goods, environmental standards (for shrimp) and safety standards (for certain types of apparel) have both impacted on Indian exports. In services, trade-restrictive effects have arisen from a variety of qualification and licensing requirements in professional and numerous other services.²⁸

There are in principle three international routes to dealing with such barriers: harmonization of national regulations (leading possibly to the creation of international standards); mutual recognition, and strengthening multilateral disciplines on national standards. These need to be complemented by upgradation of domestic standards.

Harmonization

In both goods and services, where countries have varying preferences for quality, including in relation to safety and the environment, harmonization is probably not desirable (see Bhagwati and Hudec (1996)). In the case of services, the difficulty of harmonization is revealed by the absence of widely accepted international standards. Where such standards exist, as in banking or maritime transport, meeting them is seen as a first step towards acceptability, rather than as a sufficient condition for market access.

MRAs

²⁸ The requirement of registration with, or membership of, professional organisations can also constitute an obstacle for a person wishing to provide the service on a temporary basis. For instance, in the United States requirements to practice medicine for foreign-qualified doctors vary from state to state. Candidates must also pass the qualifying examination of the Educational Commission for Foreign Medical Graduates, and then undergo a period of graduate medical education at a hospital in the United States.

India's concern about MRAs is justified, because they are like sector-specific preferential arrangements. If regulatory barriers are prohibitively high, i.e. if you start from autarky, then recognition can only be trade creating. But if they are not, then selective recognition can have discriminatory effects and lead to trade-diversion away from those who are left out of MRAs. However, India's attempt to address the problem by requiring that developing countries be allowed to join MRAs is not tenable and ignores a basic fact: MRAs are voluntary, they cannot be made to happen. A multilateral agreement cannot oblige countries to conclude MRAs – just as any provision such as Article V of GATS or Article XXIV of GATT cannot make regional integration happen.

So what is to be done? Multilateral disciplines must be used to ensure that MRAs are not used as a means of discrimination and exclusion. These disciplines operate at two levels: the general rules on preferential arrangements (Article XXIV of the GATT for goods and Article V of the GATS) and the specific rules for MRAs (in the Agreement on Technical Barriers to Trade for goods and Article VII of the GATS). Both sets of rules need to be strengthened and enforced. It would seem that Article XXIV, which disallows discrimination between countries in regard to domestic measures (including standards and regulation), would not allow MRAs to be justified as elements of integration agreements. However, the Agreement on Technical Barriers to Trade, which encourages the conclusion of MRAs, should not be interpreted as permitting discrimination through MRAs. A clarification of this point is essential.

In services, Article V on integration agreements does not explicitly preclude MRAs, and several countries have chosen to notify their MRAs under this provision. However, Article VII of the GATS dealing specifically with recognition, strikes a delicate balance by allowing such agreements, provided they are not used as a means of discrimination and third countries have the opportunity to accede or demonstrate equivalence. It should be clarified that this provision, with its desirable non-discriminatory and open-ended nature, overrides Article V of the GATS as far as MRAs are concerned.

Multilateral disciplines based on “necessity” test

In our view, the most important strategy for addressing barriers is to strengthen multilateral disciplines on standards per se. The trade-inhibiting effect of the entire class of domestic regulations can be disciplined by complementing the national treatment obligation with a generalization of the so-called "necessity" test. This test essentially leaves governments free to deal with economic and social problems provided that any measures taken are not more trade restrictive than necessary to achieve the relevant objective.

This test is already part of the Uruguay Round Agreement for goods and the recently established disciplines in the accountancy sector. It would seem desirable to use the test to create a presumption in favor of economically efficient choice of policy in remedying market failure and in pursuing non-economic objectives.²⁹ For instance, in the case of professionals like doctors, a requirement to requalify would be judged unnecessary, since the basic problem, inadequate information about whether they

²⁹ This argument is developed in Mattoo and Subramanian (1998).

possess the required skills, could be remedied by a less burdensome test of competence.

This test could also be applied to situations where a country is contemplating trade-restrictive measures on the grounds that environmental or labour standards in a partner country are too “low.” The necessity test would not seek to deny a country’s right to be concerned about environmental and labour problems in other countries, but subject the instruments it chooses to critical scrutiny. The question would be posed as to whether trade restrictions were the best instrument to address the relevant problem, and whether alternatives to the trade restriction, say compensation or international negotiation, would be more efficient in attaining the country’s objectives.

Upgradation of domestic standards

Finally, India must upgrade its standards and related institutions consistent with domestic preferences for quality. This would strengthen the case for obtaining foreign recognition and also allow foreign technical barriers to be credibly challenged. For instance, the poor standards of a few professional colleges in the country and their willingness to award certificates without adequate examinations, penalizes all members of the profession seeking to work abroad by legitimizing the imposition of elaborate requalification requirements.

I. Competition policy

India has relied for decades on the Monopolies and Restrictive Trade Practices Act, and there is now a strong need for a modern competition policy.³⁰ One reason, discussed above in the context of the TRIPs agreement, is that competition policy, coupled with compulsory licensing, offers one avenue for mitigating some of its most egregious effects. More fundamental domestic reasons, such as the concentration of production in several sectors sometimes associated with the entry of foreign investors, also dictate the adoption of a new competition policy. But does this mean that India should embrace efforts to have multilateral disciplines on competition policies?

A negative response could be based on the fear that multilateral disciplines will constrain the design or implementation of India’s own competition policy or on the view that multilateralism can add little to national efforts. On the first point, it should be noted that any future rules are likely to be very general and probably not very ambitious. Competition policy standards, practices, and institutions are divergent enough between industrial countries as to militate against very detailed and specific multilateral rule-making.

On the second point, there are a number of cases where multilateral engagement on competition policy can bring about outcomes that could benefit India. Reform of anti-dumping to bring it within the fold of competition policy is one case in point, but unfortunately the prospects of this happening in the near future are dim given the opposition of the United States and the European Union. The most coherent multilateral case for a competition policy rests on the possibility of negative spillovers across markets that need cooperation to ensure an outcome that maximizes global

³⁰ See Bhattacharjea, “Trade and Competition Policy in a Developing Country Context,” (1999).

welfare. Several examples of potential interest to India can be found. In the shipping market, international cartelization inflicts terms of trade losses on India. Excessively high levels of IP protection can inhibit transfer of technology. Foreign export cartels may charge excessively high prices. In all these cases, although domestic competition policy could attempt to redress the anti-competitive impact, it may be relatively ineffective because of jurisdictional problems or because remedial measures (for example, refusing foreign IPR owners or foreign suppliers of essential products access to domestic markets) may not be credible. Enforcement can be more effective when taken at source, involving the cooperation of partner countries.

On balance, it would seem that the most substantial gains for India would arise from the creation of an effective domestic competition policy. Multilateral rules on competition policy are likely to provide net benefits, albeit small in magnitude, especially if the prospects of addressing the menace of anti-dumping are slim. It is, therefore, difficult to understand the strong opposition that India tends to express on this issue.

J. Investment

The strongest analytical case for multilateral rules on FDI stems from the proliferation of investment incentives which creates policy-induced distortions in FDI flows without augmenting their aggregate size. In view of the superior ability of richer countries to grant such incentives, multilateral rule-making on investment could be unambiguously beneficial for developing countries such as India. Given the widespread use of these incentives by industrial countries (not just at federal but also at sub-federal levels), the prospects for disciplining them are likely to be slim.

Thus, if multilateral discipline on investment incentives are ruled out, can a case still be made for multilateral agreement on investment? It would be generally acknowledged that clear benefits derive from a liberal domestic regime for foreign domestic investment. In the case of India, despite considerable liberalization, FDI continues to be regulated and in an ad hoc manner, imposing serious costs³¹. The issue is whether multilateral rules on investment are necessary and desirable or whether FDI regimes should be determined unilaterally. Even strong advocates for multilateral disciplines on tariffs, tend to be less enthusiastic about such disciplines on FDI.

It is puzzling as to why the case for multilateral rules on FDI is different from that for conventional trade policy or for trade in services, which after all involves opening domestic markets to FDI. Theoretically, should countries have greater flexibility in designing an FDI regime for cars and electronics than for banks and telecommunications? If anything, the need for regulation which is so intrinsic to services, and which qualifies to some extent the nature and pace of opening up to FDI, is less strong in the case of FDI in goods.

The arguments in favor of multilateral engagement made above - facilitating domestic reform and providing a means of precommitment to good domestic policies - seem to be no less relevant to FDI in goods than to conventional trade policy. Moreover,

³¹ See Das (1999).

under a new competition policy, India can, like all other countries, prevent the acquisition and abuse of market power by, and regulate other anti-competitive practices of, foreign (and domestic) firms. The interesting question then is whether there is need for additional discretion to regulate FDI and whether this will be unduly circumscribed by multilateral rules. One example would seem to be measures designed to ensure the transfer of technology and training of local workers.³² There is undoubtedly need for more research on whether other safeguards need to be built into an investment agreement to preserve the freedom to pursue national objectives. But again blanket opposition to any investment agreement is not easy to comprehend.

IV. Concrete Proposals

We now present a set of concrete proposals that India could consider in the ongoing trade negotiations. These are summarized in Table 11.

Industrial tariffs: It is in India's interest to reduce its bound and actual tariffs and to seek to reduce tariffs in industrial countries, especially in textiles, clothing and footwear. The latter is particularly urgent in view of the large trade diversion costs imposed on India consequent upon preferential arrangements such as NAFTA. Reforms to Article XXIV, even if feasible, will not compensate for the trade diversion from existing preferential agreements.

Agricultural reform: Given India's actual and potential comparative advantage in agriculture, and the policy regime, which for the most part taxes rather than protects the sector, there is good reason for a change in India's negotiating position. Defensiveness should cede decisively to active advocacy of global free trade in agriculture. India should consider joining the Cairns group in supporting full liberalization of international agricultural markets.

Services: Although the most serious challenges are domestic - enhancing domestic competition and improving the regulatory framework - India should be open to multilateral disciplines on services liberalization. This openness could serve as the basis for creating credible negotiating linkages through a formula approach, trading domestic liberalization for increased mobility of individual service providers. At the same time, India should press for strengthened multilateral disciplines under the GATS on domestic regulations, to address implicit barriers posed by qualification and licensing requirements.

Electronic commerce: While supporting the current limited initiatives to liberalize ecommerce, India should push actively for commitments under the GATS on cross-border services trade to secure market access (by prohibiting quantitative restrictions) and preclude all forms of discrimination (by guaranteeing national treatment). Again, India should support strengthened disciplines on regulatory barriers to services trade.

TRIPs: India should change its draft IP legislation to ensure that TRIPs benefits can be withdrawn in the event of noncompliance by partners with commitments that affect India's exports. Simultaneously, it should seek to clarify WTO dispute settlement

³² It is relevant that India has reserved the right to impose these requirements on foreign investment under the GATS, on which any investment agreement is likely to be modelled.

procedures to prevent the within-sector retaliation rule from becoming an obstacle to such action. Domestically, it should institute workable systems for protecting intellectual property in order credibly to seek their replication internationally. A new competition policy, combined with judicious use of compulsory licensing, can help to mitigate the most egregious impacts of the TRIPs agreement.

Preferential agreements: The real problem with Article XXIV of the GATT and Article V of GATS is the lack of compensation for third parties adversely affected by trade diversion. Such compensation should be incorporated into the rules. Further, there should be a clear reaffirmation that mutual recognition agreements cannot be used as a means of discrimination.

Competition policy: Domestically, India should enact a new competition policy and be willing to discuss multilateral disciplines on competition policy. These disciplines should include outlawing practices that involve negative international spillovers such as export cartels (as in shipping), and bringing anti-dumping within the ambit of competition policy.

Standards: India should ensure that mutual recognition agreements are not used as a means of discrimination. To this end, the Agreement on TBT would need to be clarified, as would the relationship between Articles V and VII of the GATS to establish primacy of the latter. At the same time, it should push for multilateral disciplines on domestic regulations in goods and services based on the necessity test. On labor standards, India should be proactive in the ILO to ensure universal adherence to the basic ILO conventions while resisting attempts to bring the issue into the WTO.

Government procurement: Given the potential gains from more efficient and transparent government procurement, India should be willing to undertake multilateral disciplines on government procurement. At the same time, it should seek to create natural linkages with the elimination of barriers to trade in goods and services, so that it can meaningfully contest foreign procurement contracts in areas of its comparative advantage, such as labor services.

Investment: Liberalization of India's FDI regulations will yield substantial benefits. If a new domestic competition policy can regulate anti-competitive behavior of foreign (and domestic) firms, a case against multilateral rules on FDI must hinge on the need for additional discretion to regulate FDI consistent with desirable domestic objectives. This case needs to be clearly elaborated.

V. Conclusion

Trade can be an engine for growth. In the past, this engine has sputtered, owing to policies rather than geography. The challenges ahead for India now lie in implementing sound domestic policies that increase competition in, and improve the contestability of, domestic markets. These challenges are, above all, domestic. However, active multilateral engagement can be incrementally helpful in facilitating domestic reform and gaining access for India's exports of goods and labor services.

In the short run, the value of such engagement might be limited if prospects for securing increased market access are dim, and the failed Seattle negotiations heighten such negotiating pessimism. However, this pessimism needs to be credibly tested, by a willingness on India's part to open its markets in return for improved access. Success in this regard is not assured, but its chances can be improved if India were to align itself with countries that coalesce on a shared premise of sound open policies. Liberalization-based coalition/coalitions (which can differ across issues) can be an effective force for reform internationally with beneficial internal consequences. The success in Seattle of developing countries such as India in resisting demands for the inclusion of backdoor protectionism is testimony to this possibility. In the long run, the power of good arguments, buttressed by India's growing economic weight, should not be underestimated.

Table 1: Summary Indicators of WTO Disputes

All Complaint			
Complainant	Defendant		
	Developed	Developing	Total
Developed	63	42	105
Developing	21	11	32
Total	84	53	137

Completed Panels 1/			
Complainant	Defendant		
	Developed	Developing	Total
Developed	9 (7)	7 (7)	16 (14)
Developing	8 (8)	2 (0)	10 (8)
Total	17 (2)	9 (2)	26 (22)

Source: World Trade Organization

1/ Figures in brackets refer to number of cases in which complainants were successful.

Table 2 : Bound Tariff Rates and Effective Rates of Duty

	Effective rate of duty 1993/94 ³³	Effective rate of duty ³⁴ 1997/98	Bound rate of duty ³⁵ by year 2005
<u>Average unweighed tariff (per cent)</u>			
Agriculture (ISIC 1)	43	26 (16)	94 (33)
Mining (ISIC 2)	70	25 (13)	36 (9)
Manufacturing (ISIC 3, includes food processing)	73	36 (10)	52 (41)
Whole economy	71	35 (15)	54 (42)
<u>Average unweighed tariff by stage of processing (per cent)</u>			
Unprocessed	50	25 (16)	74 (40)
Semi-processed	75	35 (9)	44 (23)
Processed	73	37 (17)	56 (51)

³³ Following reform package contained in the 1993-94 Budget. The auxiliary duty was merged with the basic customs duty in the 1993-94 Budget.

³⁴ Effective m.f.n. rate, i.e., actual rates applied where basic rates have been reduced by exempt rates. However, many exempt rates can not be incorporated such as where the exempt rate applies to only a part of the HS six-digit tariff line. The effective rate also excludes specific exemptions.

³⁵ Includes only items bound during the Uruguay Round. The bound rates do not include the commitments under the Information Technology Agreement.

Note: Standard deviation is provided in parentheses. Tariff averages consider only those tariff lines with *ad valorem* rates. Year beginning 1 April.

Source: UNCTAD, the World Bank, Government of India, and selected GATT Secretariat estimates.

Table 3: Predictability, Responses and Availability of Rules and Regulations*(Percentage of respondent ratings under different categories)*

	Strongly agree	Agree	Slightly agree	Slightly disagree	Disagree	Strongly disagree	Avg score 1999
Score	6	5	4	3	2	1	
Predictability of government rules and regulations	2	7	46	29	12	4	3.46
Predictability of policy changes in the annual central budget	2	3	45	33	9	8	3.32
Advance information to firms about the changes affecting them	0	18	11	35	25	11	3.00

Source: World Bank – CII survey of 210 private sector firms, 1999

Table 4: Indicators of Indian Agricultural Trade

**4.A: Difference in UR final bound rates and MFN tariff rates:
Number of Lines by different range groups**

Range (UR-TR)	No. of Lines
UR-TR \geq 75	401
50 \leq UR-TR $<$ 75	155
25 \leq UR-TR $<$ 50	29
10 \leq UR-TR $<$ 25	39
0 \leq UR-TR $<$ 10	41
UR-TR $<$ 0	8
TOTAL	673

TR = MFN Tariff Rate (BCD) as announced in G.O.I., Budget 1999/2000.

UR = Uruguay Round final bound rates.

- Notes:*
- 1) Tariff Lines at 6-digit HS or sub-groups of 6-digit HS.
 - 2) Includes only agricultural products.

4.B: Aggregate Measure of Support to Indian Agriculture (selected crops)

Year	Product Specific Support <i>(as % of value of agricultural output)</i> <i>(selected crops)</i>	Non-Product Specific Support <i>(as % of value of agricultural output)</i> <i>(selected crops)</i>	Total AMS <i>(as % of value of agricultural output)</i> <i>(selected crops)</i>
	1986	-34.29	2.25
1987	-32.08	3.2	-28.88
1988	-35.54	3.32	-32.22
1989	-36.97	3.39	-33.58
1990	-31.78	3.36	-28.42
1991	-62.23	3.6	-58.63
1992	-69.31	3.46	-65.85
1993	-54.75	3.14	-51.61
1994	-43.27	3.4	-39.87
1995	-44.09	3.9	-40.19
1996	-45.84	3.62	-42.22
1997	-32.16	4.12	-28.04
1998	-41.89	3.49	-38.4

Source: Gulati (1999)

Table 5: Antidumping Initiations by Economy Taking Action

Economy	Number of antidumping initiations		Index of antidumping initiations 1995-98 per dollar of imports, USA=100 ^{a/}
	1991-94	1995-98	
Developed Economies			
Australia	213	77	1096
Canada	84	39	199
EU	135	122	210
US	226	94	100
All developed economies	678	353	74
Developing Economies			
Argentina	59	72	2627
Brazil	59	54	871
India	15	78	1875
Korea	14	34	204
Mexico	127	31	275
South Africa	16	72 ^{b/}	2324
All developing economies	394	509	313

Notes:

^{a/} Based on numbers of antidumping initiations 1995-98 and values of merchandise imports for 1996.

^{b/} 1995-97 figure.

Source: WTO Secretariat, Rules Division; Antidumping Measures Database

Table 6: Antidumping Initiations by Exporting Economy

Economy	Number of antidumping initiations		Index of antidumping initiations per dollar of exports, USA=100
	1992-94	1995-97	
Developed economies			
France	26	8	34
Germany	35	30	70
Italy	16	16	77
Japan	32	23	67
UK	20	16	74
US	70	48	100
Developing economies			
Brazil	50	23	585
China	115	94	751
India	24	21	779
Korea	50	40	385
Taiwan	31	30	323
Thailand	26	21	451

Source: WTO Secretariat, Rules Division; Antidumping Measures Database

Table 7: Impediments to competition in the provision of infrastructure services

Sector	Impediments on establishment	Impediments on cross-border delivery
Basic telecommunications ³⁶	Restrictions on number of firms (two for each geographically-defined circle); foreign equity participation up to 49% allowed	Restrictions on call-back services; high accounting rates and no-bypass of monopolist allowed
Financial services ³⁷	Restrictions on number of new banks and branches of foreign banks (15 per year); foreign subsidiaries not allowed	Non-convertibility of rupee limits scope for cross-border delivery
Maritime transport	No restrictions in bulk but number of shipping lines fixed (3): new entry only on routes where existing lines do not operate; foreign ownership up to 74 per cent allowed automatically	Bulk: use of foreign ships only if Indian ships not available on “comparable” rates; Liner: progressively increasing quotas on specified routes.

³⁶ In basic telecommunications, competition has been allowed to a limited extent in recent years in the local, intra-circle national long distance, and mobile segments but international telephony is still monopolized. Furthermore, the approach has meant limited planned competition duopolies in fixed telephony and in cellular mobile. At the same time, one key form of cross-border delivery, call back services are not permitted by law, and probably not much used in practice because of the difficulty of making payments in foreign currency.

³⁷ Even though the scope for competition in the banking sector has been enhanced by allowing new private sector banks since 1993 and local area banking by the private sector since 1996, the RBI fixes the number of licenses for new banks and expansion by existing foreign banks on an annual basis. This number has been fixed at 15 per annum in recent years. The monopoly in insurance may only now be broken. The scope for cross-border delivery of financial services is limited by the non-convertibility of the rupee on capital account.

Table 8: Comparison of International Long Distance Tariffs (Telecom) , 1999

<i>Country</i>	<i>From US</i>	<i>To US</i>	<i>Acc. Rate</i>	<i>Degree of Market Liberalization in Int'l Long Distance</i>	<i>Call Back</i>	<i>% of Foreign Ownership Allowed</i>
Australia	\$0.25	\$0.14	\$0.42	Competition	Yes	na
Hong Kong	\$0.31	\$0.24	\$0.80	Competition	na	na
India	\$0.66	\$1.27	\$1.28	Monopoly	No	49
Singapore	\$0.35	\$0.51	\$0.85	Monopoly	Yes	49
Peru	\$0.55	\$0.71	\$1.13	Monopoly ends in 99	No	100

Note:

1. Tariffs are per minute charges in the residential international long distance market and are subject to change. "From US" tariffs refer to the unweighted average of international calling plan rates offered by Sprint, MCIWorldCom, and AT&T (monthly fees are not considered). "To US" tariffs represent the rate charged by the foreign monopolist or, in case of competition, refer to the average tariff charged by a random sample of foreign operators. In case of peak/off-peak tariff discrimination, the time-weighted average tariff was used. Foreign operators' tariffs were converted into US dollars using market exchange rates as published by the Financial Times.

2. Accounting rates are from the US Federal Communications Commission.

3. Information on the remaining variables comes from the ITU.

Source: Research in progress by Fink and Mattoo, World Bank, 1999

Table 9: Cross-Country Comparisons of Costs of Software Services

Country	Cost per line of code (US\$)		Average salary of programmer (US\$)	
	Development	Support	Development	Support
United States	18	1.1	46,550	43,395
Canada	10	0.6	35,156	33,846
Australia	NA	NA	34,940	30,644
Japan	21	1.2	NA	NA
Austria	NA	NA	33,000	33,000
Denmark	19	1.1	NA	NA
England	11	0.7	38,785	38,179
France	13	0.8	36,750	41,250
Germany	22	1.3	42,058	34,848
Greece	6	0.4	NA	NA
Ireland	10	0.6	NA	NA
Italy	10	0.6	17,655	17,655
Netherlands	NA	NA	33,994	47,069
Scotland	NA	NA	24,842	NA
Switzerland	27	1.6	48,869	48,869
Israel	11	0.6	NA	NA
Estonia	NA	NA	12,000	8,000
Brazil	NA	NA	20,032	20,032
Colombia	NA	NA	NA	16,000
Mexico	NA	NA	10,843	13,292
Rep. of China	NA	NA	28,266	16,366
<u>INDIA</u>	<u>5</u>	<u>0.3</u>	<u>3,638</u>	<u>4,316</u>

Note: Data refer to 1996-98 averages.

Source: Adapted from Rubin (1999).

Table 10: GATS Commitments on Mode 1 and 2 in Selected Service Sectors

Sector/Subsector	Number of Countries	Market Access			National Treatment		
		Cross-Border Supply (%)			Cross-Border Supply (%)		
		Full ¹	Part ¹	No ¹	Full ¹	Part ¹	No ¹
PROFESSIONAL SERVICES	74	19	17	64	14	10	76
COMPUTER AND RELATED SERVICES							
a. Consultancy service related to the installation of computer hardware	51	57	20	24	51	22	27
b. Software implementation	56	54	27	20	48	29	23
c. Data processing	54	54	26	20	46	31	22

1 Full: full commitment; Part: partial commitment; No: no commitment.

Note: Percentage may not add up to 100 due to rounding.

Table 11: Current and Recommended Negotiating and Domestic Policy Positions

Issue	Current position	Recommended strategy
Industrial tariffs	Reluctant but willing to accept negotiations	Reduce own bound and actual tariffs and seek to reduce tariffs in other countries, especially in textiles, clothing and footwear.
Agriculture	Seeking the flexibility to protect domestic agriculture while pushing for liberalization abroad	End policies which discriminate against agriculture. Push for liberalization on a global basis and consider joining Cairns group.
Services	Defensive position in relation to opening domestic services markets, while pushing for increased mobility for individual service suppliers	Further domestic liberalization, emphasizing competition more than a change of ownership, and greater use of GATS to precommit to future liberalization. Create inter-modal negotiating linkages to enhance access for individual service suppliers. Strengthen domestic regulations and push for stronger multilateral disciplines on regulatory barriers to trade.
Electronic commerce	Initially opposed but now willing to support decision not to impose customs duties.	Current decision has little meaning since quotas and discriminatory internal taxation are still permitted in many cases. Therefore, widen and deepen scope of cross-border supply commitments under GATS on market access (prohibiting quotas) and national treatment (prohibiting discriminatory taxation) to ensure current openness continues in areas of export interest like software and database services.
TRIPs	Seeking general provisions on transfer of technology and increased protection for traditional knowledge and bioresources.	Change draft IP legislation to ensure that TRIPs benefits can be withdrawn in the event of noncompliance by partners with commitments that affect India's exports. Institute workable systems for protecting traditional knowledge domestically in order to seek their replication internationally. Use new competition policy, and judicious use of compulsory licensing, to mitigate the egregious impacts of the TRIPs agreement.
Preferential agreements	In favor of strengthening rules	Argue for inclusion of compensation provision for third countries adversely affected by trade-diversion.
Competition policy	Opposed	Strengthen domestic competition policy and be open to the development of meaningful multilateral disciplines, which ideally would also cover anti-dumping
Standards	Pushing for inclusion in MRAs Opposed to labour standards	Strengthen disciplines on MRAs to ensure that they are non-discriminatory. Push for multilateral disciplines on domestic regulations in goods and services based on the necessity test. Improve domestic standards. And on labor standards, be proactive in the ILO while resisting attempts to bring the issue into the WTO.
Government procurement	Opposed	Be open to creation of multilateral disciplines, but link to the elimination of barriers to trade in goods and services, so that foreign procurement contracts can be contested in areas of comparative advantage, such as labor services.
Investment	Opposed	Be willing to discuss multilateral disciplines, but examine case for preserving discretion beyond that provided by strengthened competition policy.
Anti-dumping	Seeking to limit scope for foreign action.	Curtail domestic use of anti-dumping. Argue for drastic reform of multilateral anti-dumping rules to eliminate current protectionist use, ideally by subjecting them to competition policy.

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