



# **ENERGY, TRADE AND GLOBAL GOVERNANCE**

**22 October 2009**

**at a conference organised by the Centre for Trade and Economic  
Integration (CTEI) at the Graduate Institute of International and  
Development Studies, Geneva**

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I am pleased to welcome you here and to have this opportunity to share with you some thoughts on energy and its relationship to trade and to trade governance. These are indeed complex questions of rising importance in international economic relations.

The first time I publicly entered the debate on energy and trade was in a speech two years ago to the World Energy Congress in Rome. In that speech I discussed some of the reasons why energy had not featured prominently so far in the GATT/WTO, notwithstanding the fact that many of the principles underlying our trading rules were applicable in key ways to international commerce in energy and energy services. I also argued that for a range of reasons the time might be ripe to consider these issues more closely. Two years on, I believe that this is even truer than it was then. It is for this reason that I welcome the initiative taken by the organizers of this conference.

***Key energy products display special features***

As we all know, energy as a product embodies a number of special characteristics that render its treatment in policy terms different from that of many other products in sectors such as manufacturing and agriculture.

Markets clearly play a part in the economics of energy supply and demand, but in a rather more complicated way than what a standard textbook would tell us about the workings of markets and the role of international trade.

Let us briefly consider some of the reasons for this.

First, much of today's energy supply – particularly fossil fuels and natural gas – is geographically concentrated, fixed in terms of location, and prominent in the production and trade of the countries that possess the resource. Thus, trade patterns on the supply side are largely pre-determined and change only slowly, in contrast to the shifting comparative advantage we associate with economies that are less resource-endowed in this way.

But compared to the geographical concentration that characterizes the supply side of energy markets, demand is very widely spread because we all need energy to run our economies. This relationship between supply and demand has important implications for the economic and political conditions under which trade takes place.

A second feature of today's key energy products is that they are scarce and non-renewable. Combined with their fixed and concentrated location, this makes for less direct competition in production and the presence of significant economic rents.

Thirdly, natural resource sectors tend to display a high degree of price volatility. While no leading economic model explains the causes of such volatility, contributing factors include supply uncertainties, inelastic demand due to the lack in the short run of substitutes for traditional energy products, and the role of speculation and political uncertainty in some producing countries.

*Trade and the traditional WTO focus on particular trade rules do not play their “standard” role in many energy markets – but trade and trade rules are still relevant*

This combination of circumstances means that trade does not enhance competition and adjust resource allocation in the standard "Ricardian" manner to say, that we think of in relation to trade in manufactures, agriculture and services.

Hence the view that the GATT/WTO's traditional focus on the instruments of trade policy, such as tariffs and quotas, is less applicable in energy markets. Indeed, there is a sense in which it is “markets” rather than “trade” that inform the core of policy concerns in the field of energy. Such policy concerns – relating among other things to competition and access to supplies have not really been the core focus of the GATT/WTO's work over the years.

On a purely practical level, there is also the reality that many of the suppliers of traditional energy products are either recent entrants into the WTO, or are still in the process of negotiating their accession. Let me just mention a few of those knocking at the WTO door to illustrate this point: Russia, Kazakhstan, Azerbaijan, Algeria, Lybia, Iran, Irak, Sudan to name but a few.

In addition, regardless of where traditional sources of energy are located, sovereignty and strategic concerns figure much more prominently in this sector, making for a greater reluctance to enter into internationally binding agreements.

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Let me be clear, however. I am not arguing, either normatively or positively, that the WTO and the world of energy are parallel universes and should forever remain so. Far from it. The culture of international trade cooperation that defines the WTO – and many of the rules underpinning it – is actually and potentially relevant to energy in several sorts of ways that I shall return to in a minute.

### ***Realities in energy markets are changing***

Before that, though, I would like to take note of some significant changes that are occurring in energy markets, and which some argue fortify the case for closer attention on the part of the WTO to the energy sector. Over time, a larger number of players have entered the field on the supply side. In no small part

this is the result of technological advances and the diversification of energy sources. Fossil fuels and natural gas increasingly compete with alternative energy sources such as nuclear power and renewables, including bio-fuels, wind, water and solar power.

The trend towards embracing renewable sources of energy will only continue as concerns about global warming intensify. Climate change, and how we can secure international cooperation to combat it, has become a central preoccupation of the global policy community. This carries significant implications for energy markets.

I am not suggesting that the structure of the energy market will change overnight, or that technology will not work its wonders in the traditional energy sector as well as in new areas, such as through the development of carbon capture and storage techniques.

But I am arguing that the panorama is changing and that this reinforces the case for examining how an institution like the WTO might contribute to an orderly and mutually beneficial framework for cooperation in the energy field.

### ***Issues actually and potentially relevant to the WTO***

I have already said that the purpose of the WTO, its existing structure and the content of some of its rules are directly relevant to the energy sector. I

would also argue that natural extensions of existing rules could be relevant to the sector.

Let us briefly examine these propositions more closely.

For all the reasons already discussed, the WTO does not address energy as a distinct sector. But in a broad sense, the purpose and framework of the WTO is applicable to all trade. Non-discrimination, transparency, an explicit structure of rules that provides predictability and reduces uncertainties, greater openness over time and a mechanism for settling disputes constitute the foundations of the system.

This is the starting point. After that, a number of specific rules are particularly relevant. Just like any sector where trade is feasible, obstacles to trade are equally feasible.

Among the energy related issues that come to mind are subsidies that distort trade, state trading disciplines, transit rights for transporting energy, and export restrictions. As has been discussed in one of your previous sessions today, the WTO has something to say on each of these.

In the field of services, the WTO has established a framework of cooperation that includes services incidental to the extraction of oil and gas, services incidental to energy distribution and pipeline transportation of fuels. Indeed, the current negotiations on energy services cover a broad range of

activities relevant for energy suppliers and traders, encompassing all energy sources, including renewables. Governments are seeking commitments from one another in services areas such as drilling, engineering, technical testing, pipeline construction, and distribution.

Many of these issues are being negotiated in the on-going Doha Round: energy services, transit rules, subsidies or climate friendly goods and services.

But there are obvious questions which remain to be answered. More and more questions in the area of energy relate to competition and investment policy, on which the WTO has presently little to no say. There are also no disciplines on export taxes, for the moment.

And as climate change concerns loom larger, the WTO becomes relevant in relation to the possible use of trade measures to manage leakage or competitiveness concerns arising from the costs of carbon constraints on production. The potential development of international trade in carbon emission permits and the establishment of carbon offset arrangements which could be considered as "subsidization" may also involve a WTO angle.

### ***Concluding observations***

I have not attempted to present an exhaustive account of the interface between energy and the WTO. But the links are clear enough. There is a core

question that I think we need to ask ourselves, based on three “givens” that I have already discussed:

- that energy is of fundamental importance to every economy in the world,
- that the energy sector embodies particular characteristics affecting the nature and content of international cooperation,
- and that the sector is changing rapidly in quite fundamental ways.

The core question I refer to is whether we need a new, more comprehensive global governance in energy. Following from this, if the answer is affirmative, is what the form and content of such governance should be and in what institutional setting. Finally, what would be the WTO role in this new energy governance? For instance, should the WTO adapt its existing rules or define specific rules to energy?

I regard these as questions that need to be explored. I hope that a conference such as this one will help to disentangle the complex set of issues involved and start to direct us towards research-based answers. I look forward to learning of the results of your deliberations.

You have had a long day and I shall stop here. As usual, I welcome any comments and questions.

Thank you.