THE WTO, SAFEGUARDS, AND TEMPORARY PROTECTION FROM IMPORTS

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INTRODUCTORY CHAPTER

I. An Introduction to Safeguards in the GATT/WTO System

Temporary protection from fairly traded imports under the World Trade Organization (WTO) typically refers to a national government’s use of a “safeguard” tariff, quota or tariff rate quota.¹ The founders of the WTO’s predecessor – the 1947 General Agreement on Tariffs and Trade (GATT) - placed such an escape clause provision squarely into the original text through the treaty’s Article XIX.² Since the WTO’s 1995 inception, the Agreement on Safeguards has taken the place of Article XIX to cover temporary import protection for trade in goods covered under the traditional agreement.³

Safeguard provisions are the primary mechanism through which a WTO member’s national government is authorized to establish a statute describing the conditions which permit it to investigate whether a domestic industry is injured because of fairly traded, but imported goods; and then impose a temporary unilateral import restriction that would otherwise be in violation of market access commitments implied by its explicit Article II tariff bindings.⁴ The safeguard provisions may also provide guidance on the form of the trade policy being imposed – whether a tariff, quota or demands to voluntarily restrain exports; whether applied selectively or against imports from all countries; the duration over which it may last before requiring removal; and finally, the terms of any compensation to adversely affected exporting countries.

While the safeguard exception to liberal trade has long been an element central to the architecture of the GATT/WTO system, its use has only periodically garnered attention outside of

¹ To clarify, this volume focuses on the re-application of temporary trade barriers that had previously been removed. It does not address temporary protection for “infant” industries, though there is some overlap between the insights of the two research literatures. This volume also does not examine application of (temporal or permanent) trade barriers against unfairly traded imports, i.e., through antidumping or countervailing duty measures, though we will discuss the substitutability between the policy instruments below. For an explicit and focused discussion of antidumping, see the volumes by Nelson and Vandenbussche (forthcoming) in this series.
² Under the GATT, in addition to Article XIX, Contracting Parties could also seek trade policy flexibility under Article XXVIII (for permanent import protection), on the grounds of national security or other general exceptions (Articles XX and XXI), under unusual circumstances when granted a waiver (Article XXV), or when suffering balance-of-payments crises under Articles XII or XVIII:B. For a discussion see Finger (1998, 2002).
³ Bown (2002a) describes many of the fundamental reforms embodied in the WTO’s Agreement on Safeguards in comparison to the GATT’s Article XIX.
⁴ A tariff “binding” is a negotiated limit or maximum tariff rate that a country is permitted to impose under its GATT/WTO obligations.
GATT/WTO circles. One such occasion was March 2002, when a substantial international political outcry and media attention accompanied the United States use of its safeguard statute to erect a massive set of tariff and quota barriers on steel product categories that had covered $5.5 billion in imports the previous year. At the time, six other WTO members quickly followed the US policy by imposing import-restricting safeguards on similar steel products, and at least two more countries initiated procedures to investigate whether to do the same. Furthermore, nine WTO members filed formal dispute settlement proceedings challenging the US steel safeguard under the WTO’s Dispute Settlement Understanding (DSU). A combination of domestic and international political pressure associated with the WTO dispute eventually culminated in the US removing the steel safeguard in December 2003, making more temporary (20 months) an import-restricting policy that the US had indicated would be fairly temporary (36 months) even from the date of the original policy announcement.

Despite a lack of much publicity, scholarly researchers have developed a thorough literature examining the structure and use of such temporary import protection programs. Furthermore, understanding the effectiveness and limitations of such policies is increasingly important with the proliferation of new safeguard regimes, proposals and provisions across many different subtexts of the WTO agreements. In addition to the authorized use of temporary trade restrictions under the Agreement on Safeguards reported to the WTO’s Committee on Safeguards (WTO, various issues), the WTO’s 1995 inception added safeguard provisions covering areas of trade newly integrated into the system. Examples of new safeguards are found in the Agreement on Agriculture’s Article 5, the General Agreement on Trade in Services’ (GATS) Article X, as well as a China-specific safeguard associated with its 2001 WTO accession.\(^5\) Furthermore, during the 1995-2004 period of the WTO’s Agreement on Apparel, Textiles and Clothing (ATC), which transitioned such trade from outside of GATT rules under the Multi-Fibre Arrangement (MFA) system to trade fully covered by WTO rules and disciplines, there was also a separate, ATC-specific transitional safeguard regime in place under that Agreement’s Article 6.\(^6\)

While the GATT’s Article XIX escape clause provision was only invoked in 150 instances between 1947 and 1994 (WTO, 1995), temporary restrictions under the Agreement on Safeguards have already been imposed upwards of 75 times between 1995 and 2004 (WTO,

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\(^6\) For a discussion of the use of safeguards under the WTO’s temporary Agreement on Apparel, Textiles and Clothing, see Kim, Reinert and Rodrigo (2002).
various issues). Furthermore, safeguard trade restrictions under the separate provisions on agriculture and textiles have been the subject of hundreds more trade restrictions. Finally, WTO members have formally challenged upwards of 25 different safeguard actions through formal dispute settlement proceedings at the DSU, further raising the policy’s profile and generating questions associated with the “appropriate” conditions and evidence necessary for its WTO-consistent use. While much of this relative increase in safeguard use is certainly associated with the dramatic expansion in WTO membership to over 140 countries, relative to the GATT’s original 23 Contracting Parties, as well as an increase in global trade covered under the agreements, the safeguard policy instrument has nevertheless taken on increased visibility, and political demands for its use may increase going forward.

This volume presents a collection of scholarly research from the economics of international trade policy and law that examines a number of fundamental questions regarding the design and use of temporary import restricting regimes. The first and foremost question confronting researchers is, why include such a safeguard clause into trade agreements in the first place, as it is otherwise antithetical to the liberal market access framework of the GATT/WTO system? Why allow for it ex ante if, ex post, national governments use it to impose barriers against fairly traded imports that lead to well-known economic inefficiencies, distortions and welfare losses to the overall economy? Second, what are the consequences of various potential forms of the safeguard policy – i.e., tariff, quota or voluntary export restraint; nondiscriminatory or country-specific protection; temporary or permanent measures; compensation or no compensation to adversely affected countries? Third, how do the changing economic conditions generated by a safeguard affect the adjustment incentives facing workers, firms and industries? Fourth, what factors determine how a safeguard law is used and/or abused by domestic actors in the political-economy process? Fifth, what are the actual economic conditions under which a safeguard can legally be used under WTO rules? Finally, how does safeguard use interact with related WTO provisions such as antidumping and the dispute settlement procedures?

The research in this volume is emblematic of a growing theoretical, empirical and policy literature on the topic of temporary protection from imports. In a limited collection there are important contributions that must be omitted, thus we do not attempt here to provide a comprehensive assessment of the subject. Furthermore, there is still much to the use and structure of temporary protection from imports that is the topic of ongoing and future research endeavors.

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After a discussion of the papers and topics included in the volume in the next section, I return to unresolved questions in the conclusion.

II. The Literature on Temporary Protection from imports

A. History and Institutions

The first three papers in the volume present historical and institutional perspectives on safeguards under the GATT/WTO system. The chapter by John H. Jackson (1997) presents an accessible description of the institutional and legal framework written by one of the GATT/WTO’s foremost legal scholars and historical participants in the formulation of the evolving system. The second paper by Alan V. Deardorff (1987) uses Corden’s (1974) conservative social welfare function framework to describe one income maintenance rationale for using such protection from imports. Finally, the chapter by J. Michael Finger (2002) describes how the use of safeguards has changed over time, and how the policy fits in with the use of substitutable policy instruments to achieve similar trade-restricting outcomes in the GATT/WTO system.

B. Economic Theory: Difficulties to Making the Case for Import-Restricting Safeguard Policies

Before motivating the use, existence or design of safeguard and adjustment policies, it is worthwhile to discuss a second set of papers whose purpose is to describe some of the fundamental problems arising with the existence of such policy availability. First is a paper by Jagdish Bhagwati (1976) that considers the phenomenon of a “market disruption” along with a safeguard threat by the importing country. This paper focuses on the endogenous impact on the exporting country’s own trade policy, as well as GATT rules in existence at the time for dealing with these phenomena.

The contribution by Michael Mussa (1978) describes the basic efficiency case against activist adjustment policies when expectations are rational and there are no distortions in the underlying economy under examination. One implication of the Mussa result was to highlight the

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8 Bown and Crowley (2005) provided an additional survey treatment of the research literature on safeguards.

9 See also the discussion in Sykes (1991) which presents a view of the safeguard as import protection and whose use generates the standard economic efficiency problems.

10 The theory behind the ideas expressed in the paper (and presented succinctly in the appendix) is more formally developed in Bhagwati and Srinivasan (1976).
demand that future research undertake modeling clarity so as to identify either what market distortions are present that can lead to an efficiency-enhancing role for an adjustment policy such as a safeguard, and/or how such a temporary restriction from imports may be a second-best policy due to the unavailability of a first-best policy instrument.

Finally, suppose the purpose of the GATT/WTO agreements is to provide an external enforcement device allowing a domestic government to commit its private sector to a reform program of trade liberalization. In a third paper, Robert W. Staiger and Guido Tabellini (1987) develop a model to illustrate how the presence of a safeguard clause in such a trade agreement can make even an optimal policy of liberal trade a time-inconsistent policy.

B. Economic Theory: Safeguard Provisions and Design

A second set of theoretical papers in the volume examines questions such as: why include such a clause into the original negotiated agreement; and, if included, how should such a clause be designed? In their political-economic text on the WTO system, Hoekman and Kostecki (2001, chapter 9) characterize inclusion of a safeguard clause as having two potential roles with respect to the underlying agreement – as “insurance” and as a “safety valve.”

The “safety valve” rationale for a safeguard provision is that governments may desire a temporary escape from the agreement in the presence of heightened political or economic pressure. The idea is that governments would like the option to temporarily suspend certain elements of the agreement when the appropriate set of circumstances arise, without having to fear that the entire agreement will fall apart and that countries will resort to non-cooperative behavior. A theoretical paper in the collection by Kyle Bagwell and Robert W. Staiger (1990) shows how, in a self-enforcing agreement and in the presence of terms-of-trade shocks, such a safeguard provision can preserve the integrity of the overall agreement by allowing countries to deal with temporary surges in trade volumes by cooperatively raising import protection.

On the other hand, the “insurance” motive relates to the idea that, when the policymakers are signing the original agreement, they would like to hedge against the possibility that certain unforeseen events may occur. Ronald D. Fischer and Thomas J. Prusa (2003) develop this idea in a model in which a safeguard clause can act as insurance for import-competing sectors affected by adverse price shocks. Under the assumption of incomplete markets so that agents cannot privately contract insurance, they show that sector-specific contingent protection, such as a resort to a safeguard, is a superior policy option to uniform tariffs.

Furthermore, Bagwell and Staiger (2005) consider the efficiency properties associated with including a safeguard provision within a self-enforcing trade agreement between
governments that acquire private information over time.\textsuperscript{11} Their model also provides an interpretation of a key feature of the WTO’s Agreement on Safeguards, which is the limited duration of the temporary trade restriction that prevents it from being re-imposed by the same industry.

C. Economic Theory: Safeguards and “Adjustment”

The language surrounding use of the safeguard policy in practice is frequently tied to the loose and ambiguous topic of “adjustment” – whether the adjustment is at the level of the individual worker, firm, or industry that has been affected by increased import competition.\textsuperscript{12} There are numerous theoretical papers that examine how safeguard policies affect the “adjustment” response of economic agents. This research documents that a temporary import-restricting policy might operate on many margins, and thus it identifies the need to identify the intended purpose of the policy ex ante. We return to this issue in the concluding section where we present a discussion of the failure of policymakers to adhere to this principle when implementing trade-restricting safeguard policies in practice.

One potential purpose for a safeguard policy is to give the domestic industry the opportunity to adjust to increased competition in order to increase its “competitiveness.” For example, Kaz Miyagiwa and Yuka Ohno (1995) explore the impact of different forms of import protection on firm-level adoption of new technology that is required in order for it to “catch-up” with foreign rivals. One important result of their paper is that temporary contingent protection, i.e., the tariffs or quotas that remain in place until the firm adopts a new technology, always delay the timing of the firm’s technology adoption decision. Other papers and results from this literature explore how such incentives change with the form of protection – i.e., tariffs versus quantitative restrictions, nondiscriminatory policies versus country-specific policies, etc.\textsuperscript{13}

On the other hand, a number of papers use economic theory to examine how a safeguard provision may provide a declining domestic industry with a more efficient adjustment out of the marketplace through exit. The article in the collection by Arye L. Hillman (1982) illustrates how, in a political economy model, a government may use a safeguard trade policy to slow the decline

\textsuperscript{11} Another paper in this spirit is Rosendorff and Milner (2001)

\textsuperscript{12} The preamble to the WTO’s Agreement on Safeguards states, “Recognizing the importance of structural adjustment and the need to enhance rather than limit competition in international markets…”

\textsuperscript{13} Other papers in the literature include Matsuyama (1990), Miyagiwa and Ohno (1999), and Crowley (2002).
of an industry for purely selfish (political support) motives. In a later paper, S. Lael Brainard and Thierry Verdier (1997) use the interaction between industry adjustment, lobbying, and the political response to explain the persistence of import protection.\textsuperscript{14} Their political-economic model illustrates how the process of current adjustment diminishes future lobbying intensity. The insight from the perspective of a safeguard policy is that import protection reduces adjustment which leads to the failure to diminish future lobbying intensity; i.e., current import protection raises future protection. Their model has interesting dynamic properties in that declining industries contract more slowly over time in the presence of a safeguard policy and never fully adjust.

Carl Davidson and Steven Matusz (2004), furthermore, examine the impact of temporary import protection on labor market activity.\textsuperscript{15} They consider a two-sector overlapping-generations model in which workers trade off the potentially higher wage that the export sector has to offer with a lower job acquisition rate in that sector. The lower acquisition rate is due to the assumption of congestion externalities that arise in the export sector as the pool of potential workers increases. They show how temporary protection can smooth out the adjustment process following an unexpected, permanent improvement in a country’s terms of trade. From the perspective of the safeguard policy’s “purpose,” this paper is aligned with questions concerning the efficient facilitation of resources out of an industry (e.g., the Brainard and Verdier/Hillman line of research), as opposed to “technological catch-up” and inducing additional resource investment in an industry (e.g., the Miyagiwa and Ohno approach).

\section*{D. Empirical Analysis of Safeguard Use}

Much like other areas of international trade research, the empirical literature examining the economic implications of safeguard use is much less developed than the theory. This stems from a number of reasons, including the relative historical infrequency of the policy’s use. Another important factor is that researchers have only recently gained access to the product- or industry-level international trade data necessary to assess critical elements of such policies. With few exceptions, the empirical literature that has evolved thus far has focused almost exclusively on United States use of its Section 201 safeguard law. This is explained by the fact that Section 201 has been used with some frequency, its use has been relatively transparent and easy to document,

\textsuperscript{14} See also Brainard (1994), Brainard and Verdier (1994), Kohler and Moore (2001), and Magee (2002).

\textsuperscript{15} See also Gaisford and Leger (2000).
and there exists a relatively long time series of high-quality, product-level US trade data that has been made publicly available to researchers.

The first two empirical papers in the volume examine the impact of US temporary import protection policies on key indicators of domestic economic performance. First, while the US International Trade Commission did investigate a 1980 safeguard petition for import protection filed by Ford and the United Auto Workers (UAW) union, it failed to find a causal link between any injury to the domestic automobile industry and imports. Nevertheless, in 1981 the US government implemented a temporary trade restriction on automobiles by negotiating a voluntary export restraint with the Japanese automobile manufacturers. Steven Berry, James Levinsohn, and Ariel Pakes (1999) rigorously examine the effect of this policy on the US economy through an analysis of its impact on consumer welfare, firm profits, and foregone tariff revenue. James Hartigan, Philip R. Perry and Sreenivas Kamma (1986) provide an alternative approach to examining the impact of a temporary trade restriction on economic activity by using the event study methodology to assess whether safeguard protection decisions in the United States between 1975 and 1980 affected capital markets and stock prices.16

The next two papers examine the US use of its safeguard policy in relation to other, substitutable policies of contingent import protection – its antidumping and countervailing duty provisions. The first paper by Robert E. Baldwin and Jeffrey W. Steagall (1994) examines determinants of the US International Trade Commission’s decisions on whether or not to find injury in administered protection investigations.17 Another paper using the data on US actions by Wendy L. Hansen and Prusa (1995) examines the differential requirements for obtaining protection across these laws as well as the impact of these alternative US laws on the product-level import flows subject to the trade restrictions.

The article by Chad P. Bown (2004a) takes the perspective of alternative policy instruments one step further by examining data on international use of safeguards under Article XIX over the 1973-1994 period. The paper investigates determinants of a country’s use of a GATT-legal safeguard versus a GATT-illegal import restriction that resulted in a trade dispute.18 The analysis provides evidence in support of the theory that, when a government imposed an

16 See Dohlman (2001) for an additional discussion of the capital markets approach.

17 See also the discussions in Finger, Hall and Nelson (1982), Takacs (1981), Baldwin (1985) and Hansen (1990).

18 Bown (2002b) develops the theory behind this question.
import-restriction, it was more likely to utilize a GATT-consistent safeguard when it sought to
shield itself from the retaliation capacity of exporters adversely affected by the proposed policy.

The empirical paper by Staiger and Tabellini (1999) tests a key proposition of their
theoretical paper (Staiger and Tabellini, 1987) in the volume. They use an empirical analysis to
examine whether GATT rules help a national government make trade policy commitments to a
domestic industry that it could not have made in the absence of these rules. To test this behavior
they examine the United States use of its safeguard policy, where it did not have access to such
GATT rules to help it commit, in comparison to the US governments’ determination of sectoral
exclusions in the Tokyo Round of GATT negotiations.

Finally, Bown and Rachel McCulloch (2004) assess the discriminatory nature of various
safeguard policies applied since the WTO’s 1995 inception. While the WTO provisions mandate
that a country is to apply a nondiscriminatory safeguard on all imports, irrespective of their
source, the evidence is that explicit and implicit nuances to the safeguard rules allow
governments to undertake substantial discretion in how they apply the policy. The results indicate
that such discretion can lead to quite discriminatory application of safeguard measures in
practice.19

E. Policy Use, Legal Process and Dispute Settlement

Finally, there are a number of additional questions related to how the WTO’s Agreement on
Safeguards allows for temporary protection from imports in practice. Researchers have written a
number of papers providing policymakers with economic frameworks to ascertain from a
petitioning domestic industry whether it has truly been “injured” from imports in a way that is
consistent with the textual agreement.

A paper by Douglas A. Irwin (2003) in this volume describes and applies one such
approach developed originally by Kelly (1988). The basic idea is to use minimal data and prior
information on market elasticities to examine whether changes in equilibrium conditions in the
domestic market are consistent with the domestic industry’s injury being caused by imports. This
approach is useful as either a low-cost, first pass at the question, or an alternative to a more
rigorous econometric approach that may be mandated because of data limitations. Irwin also
illustrates the approach by applying it to public data from a number of recent US safeguard
investigations that were formally challenged through dispute settlement at the WTO. In each case
WTO panels found the US safeguard to be inconsistent with its WTO obligations, largely because

19 See also the presentation of Bown and McCulloch (2003).
the US policymakers did not provide sufficient evidence attributing the domestic industry’s injury to imports, as they could have done by following the Kelly, or an alternative, approach.\textsuperscript{20} Finally, Alan O. Sykes (2003) combines cogent legal and economic analysis in a paper that is part of a growing literature examining WTO jurisprudence on dispute settlement decisions related to safeguard use.\textsuperscript{21} Sykes provides an important critique of the lack of guidance being provided by WTO panel and Appellate Body decisions, as well as the potential implications of such failure for the overall agreement. His analysis suggests that such decisions have failed to clarify to national governments how they can legally utilize the Agreement on Safeguards.

III. Conclusions

This volume contains a collection of theoretical and empirical research papers that have contributed to understanding the challenges associated with the temporary imposition of import protection – i.e., the use of safeguards – in the WTO system. While the existing literature addresses a number of important questions and provides a template for examining this trade policy, there is still much about the impact of such policies that is unknown.

First, the theory on temporary import protection has far outpaced empirical work on the subject. More empirical research is required to inform on the relevance of the existing competing and complementary theories. There is evolving empirical research examining questions associated with safeguards use in practice, including recent papers examining the 2002 steel safeguards. Such research empirically evaluates whether an effect of the policy wasn’t simply to raise the costs of domestic (in addition to foreign) rivals within the US steel industry, as well as to mimic the discriminatory nature of earlier implementation of antidumping measures, despite the nondiscriminatory requirements of the safeguard statute and provisions.\textsuperscript{22} Required are additional

\textsuperscript{20} When there is sufficient, high quality data available, it may be preferable to use an econometric approach to investigate the causal link between imports and injury. Such an approach is beneficial if it can hold the impact of other factors that may also be affecting injury constant. Actual econometric approaches to doing so in the safeguard context, as well as applications to specific cases include Grossman (1986), as well as Pindyck and Rotemberg (1987). See also the similarities for simultaneous equation regressions used in antidumping investigations described in Prusa and Sharp (2001). WTO (2005) details how such evidence has been utilized by formal DSU panels examining the WTO-consistency of safeguards use.

\textsuperscript{21} See also Horn and Mavroidis (2003), Bagwell and Sykes (2004), Sykes (2004) and Grossman and Mavroidis (2005).

\textsuperscript{22} See empirical papers on the US steel safeguard such as Durling and Prusa (2003) and Bown (2004b).
industry-level studies addressing the safeguard policy’s impact on firm-level productivity, resource allocation and adjustment.\textsuperscript{23}

An additional question is whether the substantial textual ambiguity within the safeguard provisions gives policymakers too much discretion, thus eroding the effectiveness of any “adjustment” policies\textsuperscript{24}. As the discussion in section C above attempted to illustrate, a domestic industry’s “adjustment” to increased import competition could mean one of two diametrically opposed outcomes that a policymaker could be attempting to target: 1) generating an environment conducive to encouraging competitiveness of the domestic industry and technological catch-up with foreign rivals; versus the polar opposite of 2) creating incentives to facilitate the rational and efficient exit of resources out of an industry that cannot compete with foreign rivals. The insight from the targeting principle (Bhagwati and Ramaswami, 1963) suggests that it is not possible for a single trade restricting safeguard policy to be the most efficient instrument at inducing both resource exit and resource entry (i.e., investment).

The research literature also lacks a more critical assessment of those safeguard policies that have been implemented, as well as appraisals of policy performance relative to the policies’ stated goals. For example, have policymakers implied that a policy intention was to facilitate resource exit from an industry, and yet imposed policies that discourage exit and encourage the status quo? The ambiguity of the ex ante meaning of “adjustment” makes it increasingly important to hold policymakers accountable for matching policy rhetoric with policy choices.

Finally, there is no empirical analysis investigating how the use of a safeguard import restriction as an “adjustment” policy fits into the broader adjustment policy environment. I.e., governments have many alternative (domestic) policy instruments with which they might target different facets of the adjustment process. How do countries with differential access to the non-trade policy instruments that more effectively target adjustment – i.e., the flexibility/rigidity of domestic labor laws, trade adjustment assistance programs, bankruptcy laws, subsidy and industrial policies, etc. – adjust differently when safeguards are imposed? What are the implications of these differences for safeguard design and rules for its use?

As globalization continues, comparative advantages shift, domestic industries decline, preferences are eroded, technologies improve and consumer preferences change - economies face increasing adjustment pressure and political demands to use the safeguard and related policy instruments. As new safeguard provisions are proposed as required political components of new

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\textsuperscript{23} One paper that has begun to address these questions from the perspective of antidumping (and not safeguards) protection is Konings and Vandenbussche (2005).

\textsuperscript{24} See the discussions found in Bown and McCulloch (2005a, b).
agreements, their appropriate design is essential. As safeguard laws are adopted and used by developed and developing countries alike, an improved understanding of the policy’s role in the trading system, as well as its limitations, is increasingly critical.

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