

Economic Policy Program

International Trade

SUMMARY: As ministers gather around the WTO negotiating table the week of July 21 in Geneva, there are troubling questions about whether the deal that is at hand is really worth doing and whether it is even possible to conclude an agreement at present, given the political constraints—especially those associated with a U.S. presidential election year.

This opinion brief argues that Doha skeptics are missing the critical importance of a WTO agreement in terms of imposing new disciplines and binding current practice in trade in agriculture, industrial goods, and services, and that there are large benefits to be had from an agreement on trade facilitation and from ensuring the continuing trade relevance of Aid for Trade. Waiting is not a good option, as upcoming elections around the world suggest that the political calendar for Doha will become more not less unforgiving.

If Not Now, Then When?

The urgent need for a Doha deal

by Joe Guinan and Courtney Phillips-Youman*

Trade ministers gathering in Geneva the week of July 21 have one last window of opportunity to make critical progress in the Doha Round of multilateral trade negotiations at the World Trade Organization (WTO). If they fail to reach an agreement on modalities for liberalization in agriculture and industrial products at the July 2008 WTO Ministerial, then there will be no further serious effort this year.

WTO Director General Pascal Lamy has made a gamble in calling ministers together, believing the chances of a breakthrough are greater than 50-50. However, if ministers fail to hammer out their differences, the odds point to a complete failure of the round. If that happens, the prospects for future WTO agreements, for the world trading system, and for the global economy as a whole begin to look increasingly uncertain.

Even with stakes as high as these, a number of shadows are being cast over the deliberations. As ministers gather around the negotiating table, two questions in particular are being voiced in the trade community.

The first is whether the deal that is at hand is really worth doing. A survey

of the recent literature indicates that this question rests upon mistaken perceptions about the value of what is on the table. Perhaps more importantly, it also ignores the consequences of not getting an agreement.

The second question is about timing, and about whether it is even possible to conclude an agreement at present, given the political constraints—especially those associated with a U.S. presidential election year. While these constraints are real, there are precedents that suggest they are far from insurmountable. And waiting is not a good option. Negotiating fatigue is setting in, and nothing qualitatively different will be put on the table by further dragging out the talks along current lines. Upcoming elections in key countries around the world suggest that the political calendar will become, if anything, even more unforgiving.

A deal on Doha would provide a much-needed shot in the arm for today's faltering global economy, which is struggling with financial market volatility, the inflationary effects of high energy and commodity prices, and a mounting food crisis. But if the Doha Round were to fail, the outlook for the global economy would be

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bleak indeed.

A deal worth doing

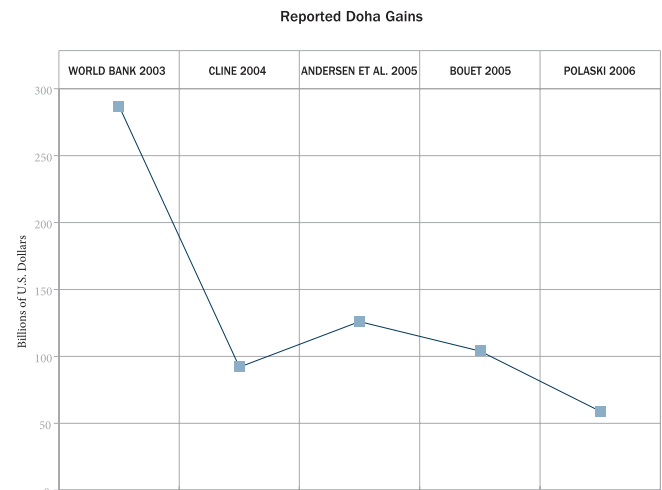
The idea that there is little on the table in the Doha Round has been growing for some time. As a result, key constituencies who could have been expected to push for a deal—especially the U.S. and European business communities—are contemplating withholding their support for an agreement at current levels of ambition. This creates another major stumbling block, particularly given the cold political wind that has already been blowing on trade over the past several years.

Feeding the problem is the perception of the “incredible shrinking gains” from trade. The Doha Round negotiations have been accompanied by an unprecedented degree of economic modeling and analysis aimed at quantifying the expected welfare gains and their distribution across countries and sectors. Compared to previous rounds, when negotiators complained about “negotiating in the dark,” this wealth of data has been invaluable. However, early inflated numbers on the gains from both global free trade and a Doha agreement proved unhelpful because they came to be seen as exaggerated and lacking in credibility.

In the past six years, there have been almost 20 assessments of full trade liberalization using computable general equilibrium (CGE) models, and at least nine assessments of a Doha Round agreement. Estimates of the welfare increase from global free trade ranged from 3.1 percent to 0.2 percent of world gross domestic product (GDP)—a difference of a factor of 15—with the numbers trending steadily downward. Similarly, the number of people lifted out of poverty as a consequence have been projected to be anywhere between 440 million and 72 million.¹ Estimates of gains from the Doha Round—only ever expected to move the world part of the way toward global free trade—have followed the same trajectory.

Trade critics have used these downward revisions to hint at some sinister plot, but the truth is far simpler. As noted trade modeler Antoine Bouët has explained, experiments with trade models have become ever-more sophisticated and now take into account preferential trade

¹ Antoine Bouët, *The Expected Benefits of Trade Liberalization for World Income and Development: Opening the “Black Box” of Global Trade Modeling* (Washington, DC: International Food Policy Research Institute, 2008), pp. 55-87.



Source: The German Marshall Fund of the United States, 2008.

arrangements and free trade agreements (FTAs), among other things, which lower previous assessments of existing trade protection and therefore of the gains from liberalization. In addition, results vary according to the trade elasticities and other assumptions that are adopted. Simply allowing for a relationship between trade openness and factor productivity—widely recognized due to effects such as the accelerated transmission of technology, but difficult to isolate and model—causes welfare gains to jump by up to 80 percent.

“Gains from the Doha Round would be at least \$43 billion a year, or \$73 billion if a modest liberalization of services is included. These are underestimates.”

The latest credible modeling numbers regarding the gains on the table in the Doha Round, based on the May 2008 draft texts in agriculture and non-agricultural market access (NAMA), converge at around \$43 billion a year.² One of these exercises, by Yvan Decreux and Lionel Fontagné, manages to incorporate a liberalization of trade in services (at 10 percent, a conservative estimate) to produce a further \$30 billion in gains, for a total of \$73 billion a year. All regions of the world would enjoy boosts in their GDP. These are not trivial numbers. And they are underesti-

² Yvan Decreux and Lionel Fontagné, “An Assessment of May 2008 Proposals for the DDA,” draft paper, Centre d’Etudes Prospectives et d’Informations Internationales, Paris, June 30, 2008; Antoine Bouët, David Laborde, and Simon Mevel, “What Can the Least Developed Countries Really Expect from the Doha Development Agenda?” draft paper, International Food Policy Research Institute, Washington, DC, July 2008.

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mates—probably dramatically so. They do not include the full benefits of services liberalization, an agreement on trade facilitation, additional gains from the Aid for Trade initiative, and other dynamic gains that cannot be captured by CGE trade models.

Nor do these numbers adequately reflect the inverse of a deal. There is an idea, a mistaken one, that in the absence of a Doha Round agreement the alternative is the *status quo ante*. It is not. As Crawford Falconer, New Zealand’s ambassador to the WTO and chair of the agriculture negotiations, has warned, if the Doha Round fails it will represent “the first broken window in the neighborhood” of globalization. The WTO would not collapse overnight, but failure could ultimately compromise the integrity of the multilateral trading system—with all the huge embedded value it represents to consumers, businesses, and governments around the world—and diminish opportunities for global economic reform. The weakest WTO members, those least able to defend their interests outside of a rules-based trading system, would then suffer most of all.

Agriculture

Agriculture has been the principal stumbling-block for much of the Doha Round, but negotiators have made important progress in recent months. Current high food prices have decreased the levels of countercyclical trade-distorting support to farmers and may therefore be obscuring some of the medium-term benefits of what is on the table in the agriculture negotiations. Binding commitments that do not affect applied protection today will have real bite if the current unusual situation in world agricultural markets reverts to a pattern that has held true since the 1950s: declining terms of trade and price volatility.

A recent assessment of the draft modalities on agriculture concludes that a Doha Round agreement would represent “substantial progress in strengthening the reforms started in the Uruguay Round,” leading to a “substantial and worthwhile outcome...even if some of the headline reduction numbers in the modalities were closer to the bottom end of the range.”³ For developed countries—whose protectionist farm policies have been a central focus of the Doha Round negotiations—all export subsidies would be abolished; overall trade-distorting

domestic support would be reduced by 50-85 percent; and agricultural tariffs would be reduced by 50-73 percent, with greater reductions for higher tariffs. The introduction of a minimum average tariff cut and of new disciplines on commodity-specific trade-distorting domestic support are valuable additions.

In the face of rising protectionist sentiments, a Doha Round agreement would lock-in recent agricultural policy reforms and give impetus to further such reforms in the future. Policy processes underway in the European Union regarding the future of the Common Agricultural Policy (CAP) would certainly benefit from pressure from the WTO, as would any future re-opening of the 2008 Farm Bill via the budget reconciliation process in the U.S. Congress.

Non-agricultural market access (NAMA)

The early emphasis on agriculture in the negotiations recently gave way to wrangling over manufactured products. Modeling of the NAMA modalities commissioned by the German Marshall Fund of the United States found that the ranges of non-agricultural goods tariff reductions for developed and developing countries, combined with the exceptions to the general tariff formula for some countries, would result in only modest increases in exports and national income.⁴ Industrialists in Europe and the United States have been vocal in their complaints about such small gains.

“A huge share of existing trade is living on borrowed time, with manufacturers simply taking for granted that industrial tariffs will remain at their current low applied levels.”

Once again, this is not an adequate appreciation of what is at stake. Renowned trade economist Patrick Messerlin has warned that the world trade regime in manufacturing is sleepwalking on a tightrope above an abyss.⁵ A huge share of existing trade is living on borrowed time, with manufacturers simply taking for granted that industrial tariffs

³ Mike Gifford and Raul Montemayor, “An Overview Assessment of the Revised Draft WTO Modalities for Agriculture,” International Centre for Trade and Sustainable Development, International Food and Agricultural Trade Policy Council, International Food Policy Research Institute, Geneva, June 2008, p. 8.

⁴ Joseph Francois, Laura Baughman, Martina Brockmeier, and Rainer Klepper, “A Quantification of the Economic Effects of the February 2008 Draft NAMA Text: Summary of Results,” draft paper, German Marshall Fund of the United States, Washington, May 14, 2008.

⁵ Patrick A. Messerlin, *Walking a Tightrope: World Trade in Manufacturing and the Benefits of Binding*, GMF Policy Brief, Washington, June 2008.

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will remain at their current low applied levels. The real benefits of a Doha Round agreement for these exporters lie in the elimination of the danger that emerging economies could raise their applied tariffs by as much as three-and-a-half times on average at any moment and without compensation.

Foolhardy observers eager to dismiss this scenario as unlikely would do well to contemplate the reactions of governments to the recent food crisis, with 28 countries rushing to impose export bans in spite of the fact that such a trade panic hurts their own interests. Industrial tariffs in countries like Brazil have already begun to edge up in recent months.

Finally, cuts in bound tariffs—even when they only cut tariff “water” and do not reduce applied tariff levels—generate additional economic activity of a kind that cannot be captured in modeling analysis. This is simple common sense. If there are large differences between bound and applied tariff rates, companies with global supply chains must significantly increase their risk premiums when they assess the viability of new projects.

A Doha Round agreement that amounts to a “binding round” in manufacturing should not be sniffed at. It would consolidate the considerable liberalization that has taken place since the Uruguay Round and provide businesses with much-needed predictability in uncertain economic times.

Services

Services are probably the most important aspect of the Doha Round negotiations. Accounting for two-thirds of global economic output, services remain a disappointingly small share of world trade—\$2.8 trillion in 2007, or 20 percent. The economic benefits of services liberalization would far surpass those associated with the liberalization of goods. However, it is difficult to quantify the exact benefits since transactions in the services sector are often intangible, with no physical crossing of borders. Many studies struggle to capture the positive welfare effects and dynamic gains that accompany all modes of service supply.

Be that as it may, an agreement in services is clearly more important now than ever before. Even more than in industrial goods, the status quo is not acceptable. Since the Uruguay Round, trade in services has been governed by a “positive list” approach, which means that countries only have bindings in areas that were explicitly identified

in 1993 or subsequently under one of the GATS protocols. New services that didn’t exist when countries made their binding commitments in the Uruguay Round but have since come into being are not covered by WTO disciplines.

Once again, there is a strong case for binding current market access and national treatment. Many countries already exceed their commitments in terms of applied regulations and market access. But, as with binding manufacturing tariffs, locking in current practice in services would provide certainty and legal predictability and remove the risk of rollback. It is also worth noting that, with developments such as the rise of just-in-time production, the biggest consumers of services are manufacturers.

Trade facilitation

Inefficient border clearance processes may be an even greater obstacle to international trade than traditional market access barriers. Annex D of the July 2004 Framework Agreement provides the mandate for the Doha negotiations on trade facilitation whose aim is “further expediting the movement, release, and clearance of goods, including goods in transit” by reducing unnecessary delays, cutting red tape, and increasing transparency at the border.

An agreement on trade facilitation is well within reach. Negotiations have been proceeding in a generous spirit and are on course to produce benefits that could dwarf those from the rest of the round. On average, customs and inspections procedures account for 75 percent of the total time it takes to import goods. According to the World Bank, each additional day a product is tied up in customs procedures has the effect of reducing trade by more than one percent, the equivalent of moving a country a further 70 km away from its trading partners.⁶ In a world in which time is money, the gains from expediting these processes would be enormous.

A trade facilitation agreement would also be significant in terms of the distribution of welfare gains from the Doha Round. Developing countries suffer from comparatively greater inefficiency at their borders, and for this reason they stand to gain the most from reform. Furthermore, the potential gains from trade facilitation are not proportional to the size of the firm. Transaction costs amount to a greater share of total costs for small and medium enterprises

⁶ Simeon Djankov, Caroline Freund and Cong S. Pham, *Trading on Time*, World Bank Policy Research Working Paper 3909, May 2006.

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“Trade facilitation would be significant in terms of the distribution of welfare gains from the Doha Round. Developing countries stand to reap greater benefits.”

(SMEs), which stand to reap larger relative gains from trade facilitation than do larger firms.

It has been estimated that bringing countries whose trade facilitation capacity is below average even halfway up to the average could increase overall trade by some \$377 billion annually.⁷ Because of these “win-win” gains, trade facilitation may end up being the real prize of the Doha Round.

Aid for Trade

The positive role that international trade can play in economic development and poverty alleviation is well understood, and led to the promise that the Doha Round would be a “development round.” However, in the case of developing countries—in particular, Least Developed Countries (LDCs)—the ability to capture the gains from increased market access are hindered by supply-side, administrative, and institutional constraints. An IFPRI study demonstrated the correlation between infrastructure and trade flows, showing, for example, the impact of greater phone density in Africa: “a one percent increase in phone density is likely to increase exports by more than 0.35 percent.”⁸

Studies like these make the need for trade capacity building assistance for developing countries increasingly apparent, but in the original Doha mandate there was no WTO mechanism to provide this assistance. Thus, the WTO Ministerial Conference in Hong Kong in December 2005 introduced the Aid for Trade initiative. At this ministerial, donors made significant commitments of Aid for Trade funds to support trade-related infrastructure projects in developing countries. Japan pledged \$10 billion over three years, the U.S. pledged \$2.7 billion a year by 2010, and the EU pledged €2 billion a year by 2010.

As the Aid for Trade initiative does not fall under the single undertaking, aid will still flow to developing countries

regardless of the outcome of Doha. However, the full benefits for poor countries will not be realized without the new trade opportunities resulting from a successful round. Absent a Doha agreement, Aid for Trade could be fated to lose its trade relevance and become just another stand-alone aid package.

The political calendar

Even convinced supporters of a Doha Round agreement can become discouraged when they look at the political calendar. The past several years of negotiations—a sorry story of missed deadlines, growing frustration, and intermittent crises—were seemingly conducted with one eye on the imperatives of U.S. domestic politics. The unraveling of bipartisan support for trade, the diminishing political capital available to the Bush Administration, the Democratic takeover of Congress in the 2006 mid-term elections, the expiration of the executive’s trade negotiating authority in June 2007, and the negative rhetoric on trade on the presidential primary campaign trail have all raised doubts about the ability of the United States to ratify a Doha deal. These concerns are real. But to the question of whether it might be better to wait, and resume serious negotiations with a new U.S. administration and a new Congress next year, there are two rejoinders that point in the opposite direction.

The first is that, even in terms of U.S. political considerations, there are good arguments, backed by historical precedent, for pressing ahead now so that the timing of the election and the changeover of administrations can be turned to an advantage. We are way past the point where the round can be completed by the end of the current administration’s term of office. But given the need for eventual Congressional support, it is probably better to have the parentage of two administrations than be stuck trying to sell “George Bush’s deal.” In many ways, the timing is reminiscent of the end of the Uruguay Round, when senior-level negotiations continued through the 1992 election and even through the lame duck period. The handover was accomplished, and the final Uruguay Round package was put together less than a year into the Clinton administration.

How might the changeover of administrations play out as part of the Doha Round endgame?⁹

⁷ *Global Economic Prospects: Realizing the Development Promise of the Doha Agenda*, (Washington: World Bank, 2004), pp. 24-25.

⁸ Antoine Bouët, Santosh Mishra, Devesh Roy, *Does Africa Trade Less than it Should, and If So, Why?*, IFPRI Discussion Paper, Washington, May 2008.

⁹ We would like to thank John Weekes of Sidley Austin LLP, Canadian Ambassador to the GATT during the Uruguay Round, for walking us through the historical parallels and timelines.

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First, the tough political nut to crack is agreement on modalities, which needs to happen this month. This would allow for revised services offers by the end of September (or shortly thereafter), allowing for draft schedules and a final draft negotiating text on rules by the end of November—*after* the U.S. elections. This timing is helpful because identifying exactly which domestic constituencies will or will not be protected by limited flexibilities is politically explosive in an election season. It can be somewhat depoliticized afterwards.

Second, Democratic presidential candidate Barack Obama has caused consternation by saying that he will closely review any WTO agreement reached by the Bush administration. But the truth is that any incoming administration is always going to want to put its stamp on an agreement in some fashion. The scenario stemming from a deal on modalities this month would accommodate this as part of the continuing negotiations over schedules, while still allowing for a completion of the round by the end of 2009. The current administration would then be able to claim the credit for laying the groundwork, while the new administration claims credit for concluding the deal.

The first rejoinder, then, to the argument that it may be better to wait is that it is critical to give the new administration a solid place from which to start. Otherwise, it will take years for them to conduct their own assessment of how to re-start negotiations (or launch new negotiations) and on what terms, which would inevitably involve extensive outreach to Congress and the private sector. Once in Geneva, working out how to re-launch the round or start a new round with a new mandate at the multilateral level would also take time, and the resulting negotiations would take another four or five years at a minimum. Failure to reach an agreement this month might thus mean that a new WTO agreement may not be in place until as late as 2020! Until then, and despite continuing rapid changes in the global economy, the world trading system will be expected to function under a system of rules agreed back in 1993!

The second rejoinder is that upcoming elections in other key countries around the world suggest that the political calendar for Doha will become more not less unforgiving. If a constant refrain has been that the Doha Round is suffering from a “lack of political leadership,” then this is not just directed at the United States. The kind of global political leadership that was once central to the GATT system is not evident anywhere, and may have gone for good, falling victim to the exigencies of the political cycle

and to the seemingly worldwide trend toward increasingly narrow margins of electoral victory.¹⁰ In developed and developing countries alike there are increased political sensitivities associated with trade, and governments are much less able to take their electorates for granted.

To take just the other three members of the G-4—India, Brazil, and the European Union—each will see important elections or political changes over the next couple of years that could impact their ability to reach agreement at the WTO.

India has been a critical player in the Doha Round negotiations. Kamal Nath, India’s trade minister, has had to walk a very fine line given the sprawling coalition of political parties that has been necessary to sustain the Congress Party-led government of Prime Minister Manmohan Singh. India has significant defensive interests in agriculture, and the rural vote was critical to the ouster of the previous BJP-led government. As of this writing, the government faces a critical confidence vote in the Indian Parliament on July 22, but its chances of survival are fair. Should the government command a majority on July 22, the rules of the Indian parliamentary system will protect the ruling coalition from any further confidence votes for six months, even in the face of additional defections.

Based on the May draft texts on agriculture and NAMA, close observers think that the way is now open for India to do a deal at the WTO. The government would then have six months in which to take the heat domestically and absorb any political fallout. However, in May 2009 there will be new elections in India. Only a clairvoyant would attempt to predict the outcome, which will be dependent on India’s kaleidoscopic coalition politics and the hard arithmetic of the election result. What will be the impact on future Indian trade policy is an open question.

Brazil too is headed toward important elections and political changes. Since taking office in January 2003, President Luiz Inácio Lula da Silva has pursued an aggressive trade liberalization agenda driven by agribusiness, the fastest-growing sector of the Brazilian economy. But the lowering of levels of ambition in agriculture at the WTO, combined with the fact that Brazilian agricultural exporters are already reaping the benefits of high world market prices, may result in a rebalancing of Brazil’s trade strategy under pressure from

¹⁰ Patrick Messerlin has made this argument convincingly: see Patrick A. Messerlin, *A Long Term View on the Doha Round and the WTO* (Washington: The German Marshall Fund of the United States, 2007).

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protectionist interest groups such as the auto workers. Elections in Brazil in 2010 are a real unknown in this regard.

In the European Union, there will be elections to the European Parliament in June 2009 and a new College of Commissioners is set to take office in November 2009. European Trade Commissioner Peter Mandelson already has his mandate to negotiate the Doha Round, but he will soon be a lame duck. In the meantime he is coming under intense pressure over agriculture from EU member states, led by France.

French criticism of Mandelson may be a way of signaling to Europe's trading partners that the European Union is "hurting" and that there is something substantial on the table at the WTO. It may also herald a re-run of the melodrama at the very end of the Uruguay Round, when Prime Minister Édouard Balladur attacked then-Trade Commissioner Leon Brittan over the "GATT diktat" in order to extract concessions from within the European Union on agriculture. He then turned around and signed the deal to a standing ovation in the French Parliament. French President Nicolas Sarkozy was Balladur's budget minister and a close political ally at the time—and may have been paying close attention.¹¹

However, it is far from certain that France would not seize upon a failure in Geneva to attempt to chart a new and less trade-friendly course on agriculture. At a press conference in March, French Agriculture Minister Michel Barnier remarked that "from a personal point of view, the question I ask myself is, is the WTO really the place to discuss questions on agriculture and food?"

Thirty-four economies, taken together, represent 95 percent of world trade. The United States, India, Brazil, and the European Union have already been addressed. Of the remaining 30, elections of some kind will be held between now and 2011 in all of the following: Mexico, Australia, Indonesia, Norway, South Africa, Thailand, Venezuela, Chile, Columbia, Singapore, Israel, the Philippines, Nigeria, Egypt, New Zealand, Peru, and Bangladesh. With the prospect of so much political change in key WTO member countries around the world, and in the context of an uncertain global economic future, the time has come to do a deal on Doha—before it becomes too late.

The time is now

The world trading system is still operating on a contractual basis that was agreed back in 1993, at the end of the Uruguay Round. Fifteen years on, with all the seismic changes that have taken place in the global economy, it is time to update the system of rules governing global trade. For the multilateral trading system—a global public good and one of the jewels of the post-war economic order—to remain effective and durable and to command the respect of governments, its rules must keep pace with developments in the world economy. In contrast to the scant coverage offered by proliferating FTAs, the Doha Round negotiations cover a massive 97.5 percent of world trade.¹² This regime must not be put at risk. Rather than waiting another decade before a new WTO agreement can come into force, it is time to harvest and consolidate all the additional trade liberalization that has taken place since the Uruguay Round and to move on to the new set of challenges confronting the world trading system.

"We know the lineaments of the deal.

Ministers need to show the political will to close the remaining gaps. The time to do it is now."

One way or another, we are in the endgame. Or the "red zone," as Lamy has called it. Just as turbulence on an airplane is at its worst right before landing, there are clear difficulties that have yet to be overcome. But it can be done. The credibility of the WTO is at stake.

We know the lineaments of the deal. Ministers need to show the political will to close the remaining gaps. The time to do it is now.

¹¹ We are indebted to Patrick Messerlin for this recollection.

¹² Progressive Policy Institute, "The Doha Round Covers 97.5 Percent of World Trade," PPI Trade Fact of the Week, June 28, 2006.

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