



THE TRANSFORMATION OF GLOBAL GOVERNANCE PROJECT

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THE GOVERNANCE OF INTERNATIONAL TRADE: RESHAPE OR DEMISE?

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- 1. The geopolitics of trade have changed.** Whilst free trade was once meant to create bonds, trade policy is now used confrontationally in a power struggle between the US and China with spillover effects for the rest of the world. Because of its enforceability, trade policy is increasingly used as a substitute for the lack of other instruments to promote issues that have little to do with it. There is danger in these developments.
- 2. Widespread dissatisfaction with the global trade system pre-dates Trump.** Most US grievances (about dispute resolution, the abuse of developing country status, weak rules for subsidies, China) pre-date the Trump administration. It's not only the US: there is widespread dissatisfaction with the outcome of past multilateral negotiations and the functioning of the world trading system. Sentiment of being treated unfairly is shared in both developed and developing countries.
Dissatisfaction stems from:
 - In advanced countries, the rapid erosion of technology rents that benefitted all, including relatively unskilled employees (aggregate factor), and the lack of appropriate policies that could have tilted the sharing of trade gains between producers and consumers (distributional factor);
 - Developing countries worry that manufacturing relocation away from advanced countries has benefitted a handful of EMs only and that insufficient market opening in advanced countries has prevented food-producing countries from benefitting;
 - China feels it has been subject to discriminatory rules by advanced countries.Future outcomes will hinge on:
 - Whether, in advanced countries, the growing current challenge to the positive-sum game nature of international trade can be reversed or complemented with policies which convince (and compensate) an increasingly sceptical electorate;
 - Whether, in certain developing countries, the values underpinning international trade can coexist with increasingly politically illiberal regimes.
- 3. Trade principles are sound but trade rules and institutions are outdated.** The nature of international trade has changed fundamentally with the development of global value chains (GVCs) and the blurring of the distinction between goods and services. It is bound to change further as a consequence of the digital revolution. Multilateralism, national treatment and the most favoured nation principle remain essential. But the trade negotiation architecture is increasingly outdated:
 - GVCs challenge traditional specialisations and trading interests;
 - The categorisation of participants in global trade on the basis of development level is at odds with growing heterogeneity within countries;
 - Increasingly important 'behind the border' issues (regulation, competition, taxes, intellectual property protection) are not properly addressed.
- 4. Clubs are the way forward, provided they abide by a set of strong principles.** Plurilateral agreements and critical mass agreements are nimble instruments that can be used in an open, non-discriminatory way. They can serve to fight the abuse of consensus and tackle the diversity in degrees/patterns of integration and national preferences/priorities. Their purpose remains ambiguous: Are they temporary patches, flexibility instruments, conduits for gradual emergence of new forms of multilateralisation or a basis for alternatives to existing multilateral arrangements? It is highly desirable that variable-geometry agreements be rooted in strong multilateral principles and be regarded as complements rather than substitutes to the multilateral order.
- 5. Trade is shifting to digital and trade policy and is increasingly linked to other policies.** As the economy and trade are increasingly digitalised, traditional trade governance norms and instruments have become increasingly ineffectual or irrelevant. With this trend set to continue, future governance outcomes will depend on the current system's ability to develop tools and governance formats which are more in tune with these new digital trade patterns and characteristics. The long-standing debate on

whether trade issues should be treated in isolation, or understood instead in conjunction with other policy areas (trade *and* environment, trade *and* labour standards,...) has decidedly shifted in favour of the latter. This is due both to the structural transformation of trade patterns but also to an understanding that this may be tactically the only way to save an open trade regime. The remaining question is whether this trade-*plus* policy stance will act to further destabilise open trade or instead help save it.

6. **The EU should address the Trump and China challenges simultaneously.** The EU shares some of the US grievances towards China but opposes its transactional approach. It should voice its concerns to both partners. It should position itself as an active proponent and, alongside the US and China, as one of the key potential architect of a reformed trade system. A “WTO 2.0” hinges on China-EU-US cooperation. The battle will be a hard-fought one as China and the US may share an interest in a purely transactional management of their rivalry.

Future outcomes will hinge on:

- whether the US will go “all the way” in rejecting the multilateral system of rules, or instead will stay within it, all the while challenging its individual tenets and pushing for reforms;
- whether the EU will be willing or able to assume the mantle of the main defender of this system, or be bogged down by its internal contradictions and weaknesses;
- whether China will be convinced to “play by the rules”, or instead veer towards an illiberal regional and confrontational solution;
- whether the WTO membership will support and implement reform efforts, or instead the WTO will be pushed to irrelevance.

7. **Broadly speaking, there are three ways forward for trade governance:**

- Attempting to **salvage the multilateral system**, by rewriting some rules, buttressing its institutions, and generating political support for it. In the current circumstances, this not only seems like an unlikely outcome, but also one at odds with the structural transformation of international trade under way.
- **Further breakdown**, with countries increasingly opting for unilateral action or pursuing bilateral deals, in essence destroying the current system in all but name. This is currently perhaps the most realistic scenario, but also one with the most downside for trade, growth and more generally the future of global governance.
- **A new plurilateral system** which draws and builds on the characteristics of the current multilateral system, but also recognises the need to amend and complement it in way that reflects the diversity of trade patterns and actors. This would be by far the most desirable – and probably also relatively likely – outcome; as a hybrid however, much will depend on its specific characteristics, i.e. on how far it will deviate from current multilateral rules.