MULTILATERAL TRADE IN A TIME OF CRISIS

-Dr. Donatella Alessandrini[1]

The decline of world trade has attracted a lot of attention in the past three years. After an initial recovery in 2010, due in large part to rising import and exports in emerging and developing economies, the World Trade Organization (WTO) has revised downwards the prospects of world trade in October 2011. Warning that 'we have now moved from a financial to a growth crisis' and that 'multilateralism is a precarious position', Deputy Director-General Ruhwabiza calls upon WTO Members to successfully conclude the Doha Round and extend the remit of the WTO to Non-Tariff Barriers (NTBs) and more generally to the regulatory environmental of trade (including technical standards, competition policy and investment rules).[2] Whether these responses are adequate to deal with the current challenges, including the decline of world trade and growth, depends very much on our understanding of the processes that have led to the current crisis.

Previous financial crises such as the ones in Mexico, South East Asia, Russia and Argentina were thought to be limited to certain regions in terms of both their effects and causes. Indeed the cause was often attributed to the improper implementation on the part of these countries of policies whose rationale was hardly ever called into question. This crisis however strikes at the heart of a system, the Anglo-American one, which has been promoted as the example of progress and stability throughout the world.3 This is why alongside calls for reforming the international financial system, serious questions began also to be raised about the international economic system, in particular its role in promoting the process of financialisation of the economy (i.e. the exponential increase of investment and financial assets) and the impact this has had on the real economy (i.e. the realm within which goods and services are produced). In this context, inequality has provided an important lens trough which to examine the relationship between the so called financial and real spheres of the economy.

The inequality explanation has brought to light the connections between three interrelated processes.[4] Firstly, the rise of unequal income distribution which has led, since the 1990s, to insufficient demand at the global level: the argument is that while profits have been increasing, the share of national income going to workers in the USA, Europe and sub-Saharan Africa, the Middle East, Latin America and

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2 WTO, DDG Rugwabiza warns protectionism will hurt global growth. WTO: news items. 4 November 2011 http://www.wto.org/english/news_e/news11_e/ddg_04nov11_e.htm

3 P. Gowan (2009) 'Crisis in the Heartland: Consequences of the New Wall Street System', 55 New Left Review, 5-29.

4 The inequality explanation can be found not only in critical economic and legal scholarship but also in international policy making reports until 2010 (See for instance D. Perrons and A. Plomien (2010) Why socio-economic inequalities increase?: facts and policy responses in Europe. European Union, Brussels, Belgium). What is striking is that four years on the crisis has become, particularly in Europe, a fiscal one and the richness of this debate has been reduced to the question of the extent to which public spending needs to be cut in order to regain the confidence of financial investors. Fiscal imperatives have come to replace earlier reformist agendas and questions about the role finance has played in the crisis have been removed from public debate.

the Caribbean has decreased.[5] Second, as a result of the wage compression that has led to insufficient demand, household debt in the US and UK has increased to support otherwise unsustainable standards of living. Recourse to debt has therefore become a mechanism through which demand has been kept up and this has been actively supported by governments until 2007 when the subprime crisis erupted. Finally investments in financial assets have also increased noticeably and recent research on the demand side of the securitisation process has shown how the wealth amassed by hedge funds, in particular by their 'net worth' investors, has been the driving force behind the proliferation of these risky financial instruments.[6] The inequality lens therefore clearly shows that the present situation requires not only proper regulation of the international financial system but also, and especially, redressing the unequal and unsustainable international economic system of production and distribution to which the former is linked.

A related question in this respect is the extent to which we can speak of a global crisis. Many developing and middle income countries have been hit less hard than the US and Europe despite the decline in the demand for manufactured and commodity exports - this is particularly the case for countries reliant on export earnings - and a likely drop in tourist expenditures and remittances.[7] This is not to say these transmission channels are not important. Indeed the crisis has brought to light the degree of interconnectedness of the international economy. However, the fact that this crisis derives from a particular model of growth and development fostered by the countries of the so-called North needs to be kept in mind when thinking of responses to the current state of affairs. At the same time the complex connections that have resulted from thirty years of policies based on such model and implemented at the international level need to be carefully traced rather than simply assumed.

One such connection is the one deriving from the complex international web of demand, trade and finance. This consists of the flow of demand from countries in structural deficit, such as the US, to countries in structural surplus, such as China and Japan, a process which has been mirrored by the investment of the latter's surplus in the purchase of treasury bills issued by the countries in deficit. These reciprocal flows are today threatened by the fact that US consumers are saving much more than they did in the past when recourse to debt was actively supported and encouraged (demand for private credit has decreased by 13% in the US).[8] The collapse of private spending, and therefore demand, is likely to occur in Europe too as a result of austerity measures that will generate job losses and a consequent drop of income. Thus, as Marazzi has pointed out, this crisis has interrupted the very mechanism which has allowed the international economy to grow, although in an unequal way, over the last three decades.

5 S. Seguino (2010) 'The Global Economic Crisis, its gender and ethnic implications, and policy responses', 18:2 Gender and Development, 186-193

6 S. Seguino (2010) 'The Global Economic Crisis, its gender and ethnic implications, and policy responses', 18:2 Gender and Development, 186-193

7 See Pinto, 307 and Seguino, note 4.

8 C. Marazzi (2010) The Violence of Financial Capitalism (London: The MIT Press), 15

From this angle the important question is not how to remove NTBs to promote a more efficient environment for trade and better integration but how to stimulate demand without having recourse to debt. Indeed the fact that the decline of trade is outpacing that of GDP is less worrying than the fact that consumers in the US and Europe are not spending and consequently not generating demand. The fact that trade is declining faster than global GDP, or a recent Report by The International Economy has put it 'faster than at any time since the Great Depression', is attributable to many factors but an important one is the role played by global supply chains.[9] The intra-firm trade that started at the end of the 1970s, when the shift away from the Keynesian consensus towards neo-liberal policies of privatisation, liberalisation and de-regulation took place in the US and Europe, created new market opportunities for private actors to invest around the world, thanks also to technological innovations which facilitated companies' horizontal as well as vertical integration. This shift has meant that trade no longer involves simple transactions between two countries as companies have created global supply chains, making use of facilities in different countries for different stages of the production process. The implication of this is that, while GDP is counted on a value added basis, intra firm trade is counted several times as it crosses borders.

This is not to say that trade is not slowing down but that its movements are magnified in comparison to movements in output. Since the latter is therefore much more significant than the former, efforts should concentrate on how to stimulate demand and therefore production of output, rather than on how to remove NTBs and extend the remit of the WTO as argued by Deputy Director-General Ruhwabiza.[10] How can demand be stimulated? As already mentioned this is unlikely to happen in Europe and the US unless the current emphasis on austerity and deficit reduction is abandoned and the trend towards inequality resulting from further wage compression reversed through massive investment in the economy. This requires a political will of which there is no sign at the moment. The repercussions of this drop in demand will be felt especially by emerging economies and developing countries whose growth has been export oriented, particularly when exports have been oriented towards European and North American markets. As it stands now it seems unlikely that these countries will be able to compensate for the drop in demand. However a different chapter in the history of world trade could be written by taking into account the increasing relevance of southern trade, as evidenced by the fact that of the total exports of emerging countries, which amounted to 35% of GDP over the last 5 years, only 20% were made to developed countries while 15% resulted from South-South trade, that is trade between emerging economies.[11]

South-South trade was indeed what temporarily accounted for faster growth in the first half of 2010 according to the WTO, even though this recovery has been challenged in the second half. As Marazzi observes, for these countries (China, India, Russia and South American countries in particular)to be

9 The International Economy, Collapse in World Trade: A symposium of Views, Spring 2009 at http://www.international-economy.com/TIE_Sp09_WorldTrade.pdf

10 WTO, note 1.

11 See Marazzi, note 7.

able to stimulate global demand they would need to raise internal wages and make greater investments in the local economy than the ones they have made until now so to create a vibrant domestic market. This however implies that their savings would no longer be directed towards Northern countries but towards internal demand, which would consequently deprive the international monetary and financial system of the same mechanism that has allowed the global economy to function the way it has until now. As far as the economies of Northern countries are concerned, this will likely introduce profound changes in production and consumption patterns. The present power geometry would certainly be altered by such a shift although how this can play out remains to be seen. However, given the current situation such a scenario cannot be easily discarded.

Should the conditions for such transformation emerge, the WTO will be confronted with demands for more policy autonomy than currently allowed by its rules in order for states to enact industrial policies. I have argued elsewhere that the combined effect of the WTO agreements, especially the GATS, TRIMs and TRIPs, together with the rules on subsidies, has been that of restricting the regulatory autonomy of its members, particularly its developing country members.[12] Although Special and Differential Treatment is still formally part of the WTO apparatus, this has been reconceptualised to allow for longer transition periods and technical assistance in order to assist countries with implementing the various agreements. However substantial reciprocity has been reintroduced within the multilateral trade regime and the Single Undertaking Approach to the WTO negotiations is one important manifestation of this: in a round supposed to be about development, developing countries will have to further liberalise services under the GATS and accept greater commitments under Non Agricultural Market access (NAMA) in order to benefit from substantial reduction of distortions in agricultural trade, the birth defect of the GATT which the WTO agreement failed to adequately redress . In the meanwhile the demand of developing countries that Special and Differential Treatment provisions be revised and made more effective and operational – a demand which is part of the Doha negotiating agenda - has received little attention and made no significant progress after ten years. The Doha Development Round has therefore ended up being much more about market access for northern countries than about development: these countries, and the US and EU in particular, have continued the practice started under GATT of protecting their markets by pursuing selective trade liberalisation while ensuring that the means of industrial policies they once used would be restricted for developing countries. This is the practice Ha-Joon Chang has famously referred to as 'kicking away the ladder'.[13]

Such a practice has always been challenged by developing countries and indeed the ascendancy of emerging economies is in no small part attributable to the fact that trade liberalisation and market integration have always been accompanied by tailored government intervention. As strategic trade theory has demonstrated so called comparative advantage is actively shaped and cultivated rather than

12 D. Alessandrini (2010) Developing Countries and the Multilateral Trade Regime: The Failure and Promise of the WTO's Development Mission (Oxford: Hart Publishing)

13 H.J Chang (2002) Kicking Away the Ladder: Development Strategy in Historical Perspective: Policies and Institutions for Economic Development in Historical Perspective (London: Anthem Press).

being determined by natural endowments. The implication of this is that countries can actively pursue, and indeed have pursued, innovations in certain sectors of the economy through targeted intervention.

The demand for greater flexibility from WTO rules is likely to increase in the foreseeable future if countries decide to pursue industrial policies so to stimulate internal demand. This is the crucial challenge the WTO will face: it can either hold on to the narrative of free trade v. protectionism and continue to uphold the normative case for uniform trade liberalisation; or it can recognise that states and markets are always in dynamic interaction (embodying different combinations of liberalisation and intervention at different times) and support the case for greater flexibility, thereby rejecting the one size fits all liberalisation model. This is both a theoretical and political challenge and the way in which it will be taken up will tell whether or not the WTO, as well as the case for multilateralism, is still relevant or has become redundant.