

# INTRODUCTION

## THE INTERNATIONAL TRADING SYSTEM PROSTRATED?

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**J**ust as the WTO Doha Round reached its tenth anniversary in 2011, the Yale Center for the Study of Globalization convened a group of distinguished trade policy experts with a twofold purpose: one, to celebrate the admirable career of Patrick Messerlin as he was retiring from his long-held tenure as professor of international economics at Sciences Po in Paris; two, to undertake that celebration by deliberating about several critical issues and circumstances faced by the international trading system.

Notwithstanding our enthusiasm to acknowledge Patrick's numerous and valuable contributions to our common subject of interest, the mood prevailing throughout our discussions was rather somber.<sup>1</sup> After all, it was the tenth anniversary of the launching of the Doha Round of international trade talks whose successful conclusion was still nowhere in sight, despite many attempts, including the solemn commitment that the G-20 leaders had made at their September 2010 Pittsburgh summit, to get it done at the latest by the end of 2011, a promise clearly already broken when our group gathered at Yale in December.

We were equally concerned about the fragmentation of the trading system caused by the proliferation of regional trade agreements over the previous decade. We were also taking seriously the submission by one of our colleagues, Simon Evenett, that despite pledges made by the G-20 to reject

protectionism and boost world trade, the world was actually enduring “creeping protectionism,” as evidenced in the regular reports on additional trade-restrictive actions across the globe produced by the admirable independent online monitor, the Global Trade Alert, that had been organized under his leadership in 2009.

Ironically, notwithstanding the rather grim prospects for international trade prevailing as our group met in New Haven in late 2011, in the early summer of 2020 it is tempting to look back with nostalgia at what were then our chief concerns about the rules-based trading system. Essentially, we were worried about the consequences—the lost economic opportunities of failing to reform and strengthen the system.

None of us could seriously entertain an imminent existential threat to the trading system. Indeed, some of our participants, despite the inauspicious circumstances, even envisioned a liberal international trading system that would continue to advance, as Michael Finger, a highly regarded trade expert, expressed in 2015 (and included as chapter 16 of this volume). Inspired by his study of the evolution of trade policy in Latin America, Mike was less worried about the lack of agreement within the WTO to further liberalize trade and update its governance rules than several other members of the group were at the time. His death in the summer of 2018 deprives us from knowing whether he would still hold an optimistic view about the likely evolution of the trading system considering recent events.

It was those recent events that motivated us to reactivate the group that had met back in 2011 and request updated versions of their original contributions to our 2011 discussion. As we began reading the new versions our colleagues sent in, our worry about the trading system being subject to stresses of a magnitude unprecedented since the 1930s was reaffirmed. Several of us, in the good company of many other trade scholars, are not shy to submit that the international trading system is under an existential threat. We argue here that this threat stems most directly and urgently from the protectionist US trade policies that have been piling up since early 2017. But as noted by Simon Evenett in chapter 6 of this volume, the trade policy trends have been negative since 2008. Pre-Trump there was already a steady buildup of trade discrimination, with many G-20 members putting in place both trade-restrictive and potentially competition-distorting export-promoting measures.

The Global Trade Alert data document that, notwithstanding the loose proclivity to use tariffs by some of the major trading countries, higher import tariffs are not yet the central feature of global trade policy dynamics. More than half of the measures that have been put in place are subsidies of some sort. This is not to say that tariffs and other traditional types of trade policies do not matter. As discussed by Chad Bown in chapter 2, emerging economies have been active users as well as targets of instruments such as antidumping actions—a policy tool used intensively by the European Union (EU), the United States, and other member nations of the Organization for Economic Cooperation and Development (OECD) in the 1980s to restrain import competition.<sup>2</sup>

Many of the chapters in this volume highlight both long-standing sources of international spillovers created by domestic policies such as agriculture (chapter 8 by Anne Krueger) and subsidies (chapter 9 by Bernard Hoekman and Douglas Nelson), and new challenges such as digital trade (chapter 10 by Erik van der Marel) and policy areas where global collective action is urgently needed, notably climate change and the role trade policy can play in greening economies (chapter 11 by Patrick Low). Moving forward on these important subjects calls for multilateral cooperation. It is pertinent to recall that in the 1980s, the complex web of import restrictions put in place to manage competition from East Asian countries and interest in expanding the trading system to include protection of intellectual property and trade in services resulted in the agreement to launch the Uruguay Round of multilateral trade negotiations.

Until recently, whether a similar dynamic would emerge or, instead, the world economy would splinter into regional arrangements centered on the United States, the EU, and countries in the Asia-Pacific, seemed to be the relevant concern. As noted by Alan Winters in chapter 4, the prospects for both multilateral cooperation in the World Trade Organization (WTO) and the implications of stronger regional bloc formation depend importantly on what China would do and the approach taken by the major OECD countries toward China. At present, however, the most relevant question is how deep and lasting the dramatic shift that has taken place in the trade policy of the United States will be, purportedly to better pursue its own national interest. The latter being a legitimate objective, it is essential to inquire whether the trade actions taken by the US government are truly consistent with the country's economic and geopolitical interests.

## THE MYSTERY OF THE TPP WITHDRAWAL

On the third day of his administration in 2017, President Donald Trump signed an executive order to withdraw the United States from the successfully concluded Trans-Pacific Partnership (TPP) agreement. This action can be considered emblematic of the new administration's trade policy if only because it is impossible to find any economic or geopolitical justification for it or any meaningful domestic political reason that could override the benefits the country was bound to derive from its TPP membership.

It is not an exaggeration to say that the TPP was constructed to satisfy the interests and demands, as well as the standards and practices, of the United States to a much greater extent than any other previous trade agreement.<sup>3</sup> The American negotiators found the arguments and, perhaps more important, the leverage to make their TPP counterparts accept conditions that from the US perspective unquestionably improved upon previous regional and multilateral agreements. The US representatives pushed hard and got the most ambitious commitments to trade liberalization and related disciplines ever agreed in a trade deal. This is a highly significant fact because, among other reasons, the accord was made by a rather heterogeneous group of countries—with significant variance in both the level of income (absolute and per capita) and the structure of gross domestic product (GDP).

The TPP required fast elimination of most tariffs with few exceptions, even in agriculture, a sector historically resistant to serious trade liberalization. Progress was also achieved in other areas traditionally excluded from trade agreements or subject to only weak disciplines, including subsidies and government procurement. One such area was state-owned enterprises (SOEs) where several key provisions were adopted to ensure a level playing field between SOEs and private enterprises (foreign and domestic).

The TPP covered investment as well as trade policies. It improved on existing bilateral investment agreements as it extended and reinforced obligations to provide nondiscriminatory treatment to foreign investors. These investment policy commitments were particularly important for services, where the market opening provided by the TPP was less ambitious. Investors in service activities, where foreign investment is allowed, were provided with both security and non-discriminatory treatment under the TPP, which also established an investor-state dispute settlement mechanism, an instrument aligned with the interests of US companies. The in-

vestment provisions were further complemented by disciplines on competition, which were more stringent than in previous preferential trade agreements (PTAs) signed by the United States.

The agreement went significantly beyond existing WTO and PTA provisions on the crucial issues of labor and environment, at least for political economy purposes. Less popular among some American constituencies was the clear win achieved by the US private sector in the protection of intellectual property rights, where the pharmaceutical industry got protections that considerably surpass those in the WTO.

Interestingly, the TPP prohibited signatories from having exchange rate misalignments and undertaking competitive devaluations—a demand put forward repeatedly by US officials. Furthermore, the agreement, for all practical purposes, got rid of the long-standing special and differential treatment in favor of developing countries, which although contained in other trade treaties including those of the WTO, is now much vilified by US officials.

Mysteriously, the TPP, patently crafted to accommodate US demands, proved to be too much of a good thing for the Trump administration, which proceeded to discard it and thus caused the United States to incur not only a meaningful economic cost but also a substantial loss in geopolitical influence in a critical part of the world.<sup>4</sup> After the US withdrawal, the eleven remaining TPP signatories slightly modified the agreement and signed it in Chile in March 2018 under the name Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP). The decision to undertake this accord without the involvement of the United States may well prove to be a template for action in a world with American self-exclusion.

### **THE MYSTERY OF NEGLECTING ESSENTIAL ECONOMIC PRINCIPLES**

Other than claiming that the withdrawal from the TPP was a great thing for the American worker because it was a terrible deal and a potential disaster for the country, the Trump administration never really provided any economic rationale for that action, which makes it practically impossible to inquire seriously into the validity of the decision. However, there is more information about the purported reasons for other trade policy actions by the Trump administration and therefore some grounds on which to check their soundness.

In a nutshell, the US administration has referred to four ideas that seem to provide the premises for its trade policy activism: one, to make trade fair and reciprocal; two, to induce the return of manufacturing jobs to the United States; three, to reduce bilateral trade imbalances; four, to fix the US overall trade and current account deficits.

American officials seem to imply that somehow the country's trading partners have managed to extract deals or simply get away with bad behavior conducive to trade surpluses that have drained manufacturing jobs from the US economy. The corollary of this view is that correcting, one by one, the existing bilateral trade imbalances—themselves the expression, in their opinion, of the unfairness and lack of reciprocity endured by the United States in its trade relations—not only would lead to gaining back lost manufacturing jobs but also to correcting the trade (and current account) deficit that for many years has been a feature of the American economy. Negotiating, one by one, new rules of engagement with trade partners has proven the preferred US approach to attempting such a correction.

The problem with this peculiar narrative is that it defies both reality and sound international economics. Take, for example, the concept of comparative advantage, which simply means that, with free trade, countries will tend to export goods that they produce relatively efficiently (with a low opportunity cost) and import goods that they produce relatively inefficiently (with a high opportunity cost). This implies that as firms and households in a country engage in international trade, an efficient outcome would entail a changing pattern of production—relatively more of some things and relatively less of others. This shift in production, which provides the opportunity to exchange goods and services in international markets, is what provides the gains in national income that countries derive from trade. It is not possible to have the latter without the former.

That an open economy like the United States—as it grew richer with increasing average productivity of its labor force—changed its productive structure, certainly to the detriment of traditional manufacturing sectors, should not come as a surprise. In fact, that structural shift is a robust measure of the country's great success. Had the United States still been producing the same products and with the same labor intensity that it did in the 1950s and 1960s, it would be a considerably less rich country than it is now, and its post-baby-boom labor force, by virtue of holding jobs like the ones their parents and grandparents had, would be a group of very unhappy (and poor) people.

The shift in countries like the United States toward employing relatively fewer people in traditional manufacturing has been heightened by fast technological progress, itself a very positive development but also a chief cause of phenomena such as labor force displacement, increasing skill premiums, and deepening wage inequality. These effects frequently are wrongly attributed purely to trade. Technological change, particularly in transportation and information technology has led to the fragmentation of production processes into complex global supply chains, a process in which US workers, as far as quality and compensation of jobs are concerned, have been clear beneficiaries. In modern manufacturing, most value is accrued in the preassembly and postassembly stages of production thus rendering what is known as the smile curve (when value added is mapped against stages of production). It is in the higher-value-adding jobs of global manufacturing supply chains where US designers, technologists, entrepreneurs, engineers, financiers, and marketeers get employed (Baldwin 2013).

It is curious that some political leaders express so much longing for old-fashioned manufacturing jobs while not acknowledging the better jobs that open markets and technological progress bring. In short, those politicians are disregarding the benefits of production and trade specialization driven by comparative advantage, which is an old and sound economic principle. Almost as old, and equally sound, is the conceptual and empirical insight that free trade, simply by changing relative prices of both the products and the factors of production, is bound to change a country's income distribution and, depending on a host of factors, possibly in a regressive manner. This is why a conventional posture of the economics profession is that trade liberalization must be accompanied by other policy actions with a view to mitigating or even fully compensating those distributional effects that are deemed undesirable.

The mistaken picture of trade as a bellicose zero-sum game is completed by neglecting another basic economic principle: that the external balance of an economy is determined by the difference between gross domestic product and gross national expenditure. This is not high-powered economic theory but rather an expression of the elementary national income identity taught at the outset in elementary macroeconomics. Notwithstanding its simplicity, the identity is insightful, for it suggests that variables more directly influencing national income and expenditure can be more effective than trade instruments to balance a country's external accounts. It also suggests that focusing on bilateral imbalances is a totally

idle exercise. If a country expends more than its national income it will have a deficit.

In short, ignoring the essential insights stemming both from the notion of comparative advantage and the basic national income identity of an open economy leads to using the wrong instrument—protectionism—to pursue two policy objectives: a change in the production and trade mix of the economy and a correction of its external imbalance. This undertaking is wrongheaded in its entirety for it causes harm to the US economy that is self-inflicted.

### THE MYSTERY OF RENEGOTIATING NAFTA

Candidate Trump characterized the North American Free Trade Agreement (NAFTA) as “the worst trade deal maybe ever signed anywhere but certainly ever signed in this country” and committed to renegotiate it to make it “a great deal” or otherwise to “tear it up.” It thus came as no surprise when, shortly after becoming president, his administration announced officially that it would initiate negotiations to update the agreement with Canada and Mexico.

The talks started off on the wrong foot, considering that in July 2017 the US Trade Representative (USTR), when formally explaining the objectives of the renegotiation, asserted that, because of NAFTA, the United States’ “trade deficits have exploded, thousands of factories have closed, and millions of Americans have found themselves stranded” (Office of the United States Trade Representative 2017, 2).<sup>5</sup> There is not a single serious study anywhere that would support or give credence to this bizarre statement. It is therefore an enigma why the US officials included it along with other arguments that actually did make some sense, like the fact that NAFTA had been in place for almost a quarter of a century and therefore warranted certain updates in light of developments such as growth in electronic trade, and evolving views on matters such as intellectual property rights, protection of the environment, and labor and regulatory standards.

The rather awkward demands made by the American negotiators over practically the entire first year of talks made it hard to believe that the US government really wanted to modernize the old NAFTA. It looked rather as if their chief objective was to destroy trade and investment among the three North American partners to the point of making the agreement ineffective and even counterproductive. For too long the US representatives



insisted on demands such as that trade in goods should be balanced—presumably by fiat, not by markets; a sunset clause that would terminate the agreement every five years unless the three governments agreed otherwise; a set of highly convoluted and discriminatory rules of origin (chiefly against Mexican exports) for the automotive industry; the freedom to impose seasonal antidumping tariffs on fruits and vegetables; nonreciprocal rules (favoring the United States) in government procurement; and making the NAFTA investor-state dispute settlement system optional, which would have allowed the United States to withdraw at any moment, thereby discouraging US firms from investing in Mexico and Canada.

Fortunately, the Mexican and Canadian governments did not cave to these peculiar demands and repeatedly submitted that they would rather take the unilateral termination of NAFTA as threatened by the American president than accept an agreement that would have the same practical consequence of killing the existing trade and investment opportunities among the three partners. To get a deal, the United States had to water down most of its positions. The most significant US demand accommodated by Mexico and Canada was in the automotive sector, where more restrictive and cumbersome rules of origin were accepted. It was agreed that 75 percent of any vehicle (as compared to the 85 percent that had been demanded by the United States) should contain components from North America to qualify for tariff-free imports, up from the NAFTA level of 62.5 percent; that 70 percent of the steel and aluminum used in the sector would also have to be from North America; and that 40 percent of a car or truck must be made by workers earning at least \$16 per hour, a requirement clearly intended to dent Mexico's comparative advantage and establishing a delicate precedent of discriminatory rules of origin within a free trade agreement.

If effective, the new rules of origin would reduce both the regional and global competitiveness of the North American automotive industry and have bad consequences for its workers in the three countries. Fortunately, this adverse effect is limited in the case of cars because, if the rules fail to be met, cars could be exported by paying the most favored nation (MFN) tariff of 2.5 percent as long as total exports did not exceed an agreed number of vehicles; that number exceeded the existing level of exports, though only slightly in the case of Mexico. For trucks, however, the new rules of origin will almost certainly be binding since the MFN tariff is 25 percent.<sup>6</sup> On balance, there should be no doubt that the North American automotive industry as a whole will lose international competitiveness, a circumstance

that makes it more likely that the United States will impose tariffs on cars from Europe, Japan, and Korea, a step that could give rise to retaliatory measures by those trade partners.

Although the original five-year sunset clause demand was dropped, the agreed provision instituting a revision of the instrument after six years and its extension after sixteen years only if affirmed by the partners, does introduce significant uncertainty about the stability of the pact, which obviously does not encourage investment. The same consequence is to be expected from the mutilations applied to the Investor-State Dispute Settlement, which practically disappeared for issues between Canada and the United States and was severely curtailed for cases between the United States and Mexico. In the new agreement, inequitably Mexico loses the protection from the arbitrary imposition of antidumping and countervailing duties that the NAFTA binational arbitration procedure provided, while Canada retains such protection.<sup>7</sup>

Curiously, the good parts of the renegotiated agreement are also somewhat redundant, at least for the United States. The CPTPP already contains most of the modernizing features of the United States-Mexico-Canada Agreement (USMCA) on intellectual property rights, e-commerce, and data. By signing the CPTPP, Mexico and Canada had already granted the United States the stronger disciplines on those aspects because of that instrument's commitment to nondiscrimination. In short, it is a total mystery what true advantages the United States will derive from launching a new agreement.

Disturbingly, the conclusion of the USMCA negotiations, while tempering US trade rhetoric against its North American partners, did not put an end to its hostile economic actions. For one thing, it took much longer than expected—until mid-May 2019—to exempt those neighbors from the tariffs that the United States imposed rather arbitrarily in early 2018 on steel and aluminum imports. By contrast, the Mexican and Canadian governments immediately fulfilled their commitment to suspend the retaliatory tariffs that they themselves had imposed on certain US exports.

Unfortunately, trade peace between the United States and Mexico did not last long. By the end of the same month, additional steel and aluminum tariffs were removed, President Trump was threatening to impose a 5 percent tariff on all imports from Mexico in June and to increase it by 5 percentage points every month until reaching 25 percent permanently by October if Mexico did not intensify its efforts to curb Central American

migration at its southern border. Although the two governments were able to strike a deal that prevented the imposition of the announced tariffs, an extremely dangerous precedent of linking trade and migration issues in a very negative way was established. Consenting on more liberal migration policies as a sequel to significant trade openings has not been unusual; that is how single markets are born. But it is anomalous to impose on a country a specific migration policy under the threat of unilateral trade sanctions in circumvention of existing bilateral and multilateral agreements.<sup>8</sup>

### THE MYSTERY OF THE TRADE WAR WITH CHINA

The unwarranted rough treatment of its North American trade partners pales in comparison with the trade aggressiveness displayed by the US government against China. Step by step, from initial moves that had not yet singled out China—first with tariffs on solar panels and washing machines and then on steel and aluminum products in early 2018—to the imposition of tariffs on imports specifically from China announced initially in March 2018 and extended repeatedly ever since, the Trump administration has set off an authentic trade war practically without precedent since the one that took place in the 1930s. To every US announcement of new tariffs, starting with the ones on steel and aluminum imports, China, not surprisingly, responded in kind, albeit in a measured and strategic way.

In chapter 4 of this volume, Alan Winters discusses the underlying economic dynamics that help us to understand the trade tensions that emerged following China's decision to reintegrate into the world economy in the 1980s. The speed and magnitude of China's growth and ability to leverage trade opportunities to support its economic development are historically unprecedented. China's rapid export growth led many countries to take measures to reduce import competition, as permitted by the WTO (Messerlin 2004),<sup>9</sup> as did concerns that some of the policies implemented in China are inadequately regulated by the WTO.<sup>10</sup> However, rather than using the WTO as a mechanism to agree on rules to manage the externalities that such policies may create, the United States has chosen to pursue an aggressive unilateral path.

The resulting tit-for-tat tariff exchange between the United States and China has transformed a formerly quite open trade relationship into one that threatens to set back the clock of their trade integration by forty years. Chad Bown, a meticulous observer of the American administration's trade

actions, has calculated that if all the tariffs announced in 2018 and 2019 had materialized the average US tariff on imports from China would have risen from 3.1 percent in 2017 to 24.3 percent by December 15, 2019, and would cover 96.8 percent of all products exported by China to the United States. Bown estimates that average US tariffs on Chinese products would be similar to the ones that the United States imposed with the infamous Smoot-Hawley Tariff Act of 1930 (Bown 2019).

In turn, China's announced retaliatory actions would have driven the average tariff on imports from the United States to 25.9 percent from 8 percent before the trade hostilities started. Yet, absent additional measures, 31 percent of US exports to China—including aircraft, semiconductors, and pharmaceuticals—would remain unaffected by the retaliatory tariffs, suggesting that China's reaction to the American trade hostilities was more restrained, particularly considering that China has taken no actions on US services exports and inward foreign direct investment (FDI) or played the card of disinvesting massively from US dollar-denominated financial assets. China, moreover, lowered its tariffs on imports from other countries, thus further reducing the competitiveness of US exports relative to third countries in the Chinese market.<sup>11</sup> The “phase 1” deal concluded by China and the United States in January 2020 retained the 25 percent tariffs imposed on \$250 billion of Chinese exports but cut US tariffs on an additional \$120 billion of Chinese exports imposed in September 2019 by 50 percent, to 7.5 percent, and suspended the US threat to impose punitive tariffs on those exports not already targeted by the United States. The main feature of the agreement was a promise by China to increase imports from the United States within two years by \$200 billion more than the country had imported in 2017.<sup>12</sup> This explicitly mercantilist deal blatantly violates the fundamental rules of the WTO. It also makes no economic sense in that it is an exercise in trade diversion. The effect may be to put China into a position where it becomes a distributor of US goods for which there is global demand, importing and then re-exporting products to the rest of the world. This is a costly exercise that will increase trade transaction costs, but it will do nothing for US businesses.

Given how consequential the trade war against China could prove to be, inquiring about its rationale—or lack thereof—is even more important than in the case of other trade policy actions undertaken by the Trump administration. A logical place to start is with the formal arguments pro-

vided by the American government itself. The tariffs on imports of steel and aluminum announced on March 1, 2018—imposed not just against China but on imports from other trade partners and allies as well<sup>13</sup>—were purported to be necessary for reasons of US national security, allegedly in conformity internally with section 232 of the Trade Expansion of 1962 and externally with Article XXI of the General Agreement on Tariffs and Trade (GATT).<sup>14</sup>

Craig VanGrasstek, in chapter 3 of this volume, explains that presidents before Trump had used the national security provision only three times, and only against countries within the orbit of the Soviet Union. The European Union used the security invocation only twice during the GATT period, and like the United States, under conditions where the security reason was evident—restrictions against Argentina during the Falklands/Malvinas War and the withdrawal of preferential treatment to Yugoslavia right before its breakup. That the invocation of national security provisions was so infrequent over more than seven decades helps to explain why no country was asked to argue its security excuse before a dispute-settlement body.

Despite this antecedent, it is pertinent to determine whether the recent invocation by the United States is consistent with its WTO obligations. Of course, the US government would submit that it is. Interestingly, in its capacity as a third party in the WTO complaint by Ukraine against Russia regarding the latter's restrictions on traffic in transit from Ukraine through the Russian Federation,<sup>15</sup> the US government argued that the invocation of GATT Article XXI is self-judging and shall not be subject to review by a Dispute Settlement Understanding (DSU) Panel or Appellate Body, in practice supporting Russia. Nevertheless, a WTO panel on the Ukrainian complaint was established and delivered its report in early April of 2019. It determined that WTO panels do have jurisdiction to review a government's invocation of the national security exception, thus rejecting the Russian and American assertion that the invocation of GATT Article XXI is wholly self-judging. However, the panel also determined that Russia's invocation of GATT Article XXI was justified given that the restrictive actions against Ukraine were taken during an emergency in international relations that has existed between the two countries since 2014.

The fact that the WTO panel found that it had jurisdiction to review whether a country had met the conditions for invoking national security as a justification for trade restrictions does not bode well for the US unilateral

imposition of the steel and aluminum tariffs in effect since 2018—and others it has threatened on other products—on the basis of section 232 of the Trade Expansion Act of 1962. A WTO panel reviewing the WTO legality of the US steel and aluminum tariffs will find it difficult, if not impossible, to rely on the Russian case as a valid antecedent. Most US imports of steel and aluminum came from trade partners like Canada, Japan, Germany, Mexico, and other close allies. Very few of the imports came from countries the US government likes to see as adversarial, namely China and Russia.<sup>16</sup> Furthermore, over 70 percent of US steel demand is satisfied by domestic production.

It is bizarre that, on the eve of the third decade of the twenty-first century, trade in such basic metal commodities as steel and aluminum, or products like cars and trucks, can be posited as “strategic” from a national security perspective by any country. Such a claim could have been plausible a century ago, but not today. Not surprisingly, as reported by Bown and Irwin (2019), even the US Defense Department has been skeptical of the national security argument for imposing tariffs on steel and aluminum. VanGrasstek also argues that President Trump’s reliance on the national security invocation is highly problematic, and characterizes it as an absurd, cynical, spurious, and abusive attempt to game the multilateral trading system, with the consequence of subjecting it to an existential threat.

The alleged reasons to impose tariffs on practically all Chinese exports to the United States are also questionable, to put it mildly. The “formal” justification started on August 14, 2017, with an instruction by President Trump to the USTR to investigate whether China “has implemented laws, policies, and practices and has taken actions related to intellectual property, innovation, and technology that may encourage or require the transfer of American technology and intellectual property to enterprises in China or that may otherwise negatively affect American economic interests.”<sup>17</sup> The investigation, under section 301 of the Trade Act of 1974, was initiated a few days later and concluded with the report delivered by the USTR on March 22, 2018. On the same day, President Trump announced that tariffs on up to \$60 billion on imports from China were forthcoming based on the section 301 investigation.

A brief discussion of the report that purportedly convinced the US government to launch the first great trade war of the twenty-first century is salient here. A first observation concerns the category of actions (acts, pol-

icies, and practices) that the USTR decided to inquire into and report about. Section 301 may be used to address trade agreement violations; actions that are inconsistent with US international legal rights; and actions that are unreasonable or discriminatory and that burden or restrict US commerce. Tellingly, the USTR did not build its case on either of the first two categories but, rather, on the third—action unreasonable or discriminatory, that “while not necessarily in violation of, or inconsistent with, the international legal rights of the United States, is otherwise unfair and inequitable” (US Congress, 1974, 3).<sup>18</sup>

One can only speculate why the USTR opted to go after the weaker, more ambiguous, and subjective violation contemplated in section 301. One plausible explanation is that USTR lawyers were aware that the actions they were mandated to investigate were hardly in violation of US rights stemming either from trade agreements or international law and therefore had to look for legally “softer” violations to report. Their inclination to do so perhaps was encouraged by the fact—as recognized at the outset in the USTR report—that the two other kinds of issues are justiciable in the WTO, an eventuality that most likely would have been profoundly distasteful to the Trump White House. By focusing on actions that are “unreasonable or discriminatory and that burden or restrict US commerce,” the focus was put on something wherein the determination of violation (by China) would be purely unilateral while still being justified as legal under US statutes.

Key targets of the USTR are China’s joint venture (JV) requirements and foreign equity limitations that, along with administrative approval processes, are allegedly used to extract commitments of transfer technology from foreign investors. There is little hard evidence offered for this in the report. The report states that after WTO accession in 2001, to comply with its new obligations, China formally gave up its former practice of mandating technology transfers. However, it goes on to note that “since then, according to numerous sources, China’s technology transfer policies and practices have become more implicit, often carried out through oral instructions and ‘behind closed doors.’”<sup>19</sup> In fact, the report affirms that Chinese officials do not put their requirements in writing. We are asked to believe somehow that US companies, with a well-earned reputation for being law abiding, take improper verbal instructions from Chinese bureaucrats in secret and compromise the value of their businesses—by giving

away proprietary technology—making sure that they do not leave any written trace of their bad behavior.

More plausible is the case, also put forward in the 301 report, that the pressure on foreign investors to be generous with their technology comes through their chosen local JV partners. If this were the case, it seems pertinent to believe that such JVs happen in sectors where Chinese law does not allow full foreign ownership—a circumstance that exists in varying degrees in practically all countries, including the United States—without violating any international legal obligation. When a foreign company nevertheless decides to do business in China, it is then expected that the economic value of the knowhow to be transferred is adequately accounted for in the corresponding cost-benefit analysis. Whether to enter into a JV becomes essentially a business decision. Of course, that company's home country may be entitled, by domestic and international law, to prohibit or place conditions on the transfer of certain technologies that company possesses and may proceed to exercise that right, as does happen from time to time, not least in the United States.

In sectors where there is no restriction on wholly foreign-owned enterprises (WFOEs) the Chinese government lacks legal capacity, but also has very limited practical capacity to force the feared technology transfer. It is not surprising, as the 301 report itself indicates, that in those unrestricted sectors, foreign companies prefer and do indeed have full ownership of their operations in China. Given the qualitative distinction between the case of JVs and WFOEs, it is extraordinary that the USTR report does not compare the quantitative importance of both vehicles to do business in China, at the very least to get an idea of the relative strength of the reputed arm twisting undertaken by China to forcefully acquire technology—granting, for the sake of argument, that such improper behavior has taken place.

The conspicuous omission of such a comparison is not due to lack of reliable information or research. For an excellent example of the latter, there is the work of Nicholas Lardy, who reports that, while in the early years of China's opening, practically none of the FDI into China was through fully owned foreign enterprises, in recent years as much as 70–80 percent of the total has been in that form (Lardy 2018). The claim that forced transfers of technology are pervasive in China, by means of use and abuse of JVs, simply cannot be objectively sustained. Nevertheless, that accusation is at the core of the formal justification of the US trade war with China.



That the core argument is at the very least questionable is something that must be considered in assessing the validity and severity of the actions undertaken by the Trump administration.

Admittedly, the USTR report deals with other alleged Chinese infractions. China is being accused of entertaining discriminatory licensing restrictions, encouraging certain outbound investments, committing cybercrimes to the detriment of American companies, supporting improperly and using inappropriately its state-owned enterprises, and even of having an industrial policy. The report concludes, as in the case of forced technology transfers through JVs, that China's acts, policies, and practices are unreasonable and burden or restrict US commerce. Granted—even in the face of weak supporting evidence offered in the 301 report—that there is some truth in those charges, there is the question of whether this warrants the massive trade hostilities initiated by the American government.

To answer that question, it is important first to distinguish among three kinds of actions imputed to the Chinese government: (1) actions that are legal and legitimate but are vilified as a result of unfairly applying a double standard or, even worse, that stem simply from enviousness and paranoia about China's economic successes over the last four decades; (2) actions that conform to the existing multilateral rules but create negative spillovers and should be the subject of a collective effort to update international standards consistent with the challenges of contemporary interdependence; and (3) actions that by any standard, present or conceivable for the future, are unacceptable—like outright theft of intellectual property (IP) or cyber-criminality. Once such distinctions are accepted and the 301 report is analyzed in its entirety, it is impossible to find in it a sufficiently valid justification for the massive trade punitive measures taken against China by the Trump administration.

It is not a great stretch of imagination to infer that the authors of the report were also unconvinced that their findings could possibly be used to justify a massive trade war. Consider that, in addition to looking at the JVs, discriminatory licensing, cybercrimes, and misuse of SOEs, most of what it concluded were unreasonable practices burdening or restricting US commerce (reputedly a possible cause of sanctions) constituted “other acts, policies and practices of China.” This heading comprised, among other things, inadequate protection of IP of American companies doing business in China and an alleged twisted use of China's cybersecurity, antimonopoly,

and standardization Laws. For these other alleged Chinese infractions, the report revealingly concludes:

USTR acknowledges the importance of these issues and agrees with stakeholders that the matters warrant further investigation. . . . A range of tools may be appropriate to address these serious matters including more intensive bilateral engagement, WTO dispute settlement, and/or additional section 301 investigations.<sup>20</sup>

It is a mystery why this judicious consideration—that patently advises engagement in negotiations with China and reliance on the WTO—was not adopted for all the matters under investigation in the 301 report. The enigma grows when we consider that, as disclosed by former USTR Michael Froman, a US-China Bilateral Investment Treaty, launched toward the end of President George W. Bush’s administration and effectively negotiated between 2014 and 2016, was 90 percent complete by the end of the Obama administration. The nearly agreed accord contained “binding and enforceable requirements on China to dramatically increase its intellectual property rights enforcement, prohibit forced technology transfer, adopt meaningful disciplines on state-owned enterprises and open vast portions of the Chinese economy to market competition, including from US firms” (Froman 2019).

If the arguments contained in the USTR section 301 report, which supposedly provide the strictly formal justification for the US trade war against China, do not really hold water, the question emerges whether there could be other economic arguments that may make sense from the perspective of the American national interest but were not made explicit by the Trump administration. Eddy Bekkers, Joseph Francois, Douglas Nelson, and Hugo Rojas-Romagosa attempt to answer that question in chapter 5 of this volume, relying on the insights provided by the theory of rational trade wars, defined as “an extended period during which a pair of countries, or groups of countries, apply instruments of trade policy with the intention of affecting a substantial share of the trade between those countries (or groups of countries) . . . to maximize national welfare by affecting the terms of trade.”

Notwithstanding their open-minded search, Bekkers and coauthors end up declaring their failure to provide us with an economically rational explanation for the trade war. After a sincere try, laconically they conclude:

So, as a practical matter, the theory of rational trade wars cannot tell us about actually existing trade wars. Perhaps more important, the

notion that it tells us anything about the trade policy of the Trump administration with say, China (or Europe, or its NAFTA partners) literally beggars belief. . . . In the case of the current trade policy of the Trump administration, the most difficult issue would seem to be figuring out what the president, and what for want of a better term we will call “advisers,” are using for an objective function. Clearly not among them are: social welfare (however we might want to define that); reelection maximization as represented in standard political economy forces (to the extent that we can tell, the distribution of costs and benefits seems all wrong for that); and pursuit of geostrategic goals (the policies seem too collectively incoherent to reflect such goals). At this point, we seem to fall back on personal psychology, but this is an area in which, as economists, we are manifestly unqualified.

Other authors would question that “the pursuit of geostrategic goals” can be dismissed that easily as the *raison d’être* of the American administration’s trade policy. VanGrasstek (chapter 3 suggests that “the evolution of American trade policy is best understood over the long run as a function of the international distribution of power and wealth, and especially the rise and fall of the country’s leadership role.” In this view, purportedly based on the idea of hegemonic stability, much of the Trump administration’s trade actions can be seen as an attempt to rectify the policies favoring open markets—policies propelled and led by the United States itself in the past—that have allowed the ascendance of China.

This suggests the objective function is the preservation of US hegemony by preventing China from rising sufficiently to take the position the United States has enjoyed for a long time. Aaditya Matoo and Robert W. Staiger argue that over the period of unchallenged dominance it is in the self-interest of the hegemon to support a rules-based system to preserve and enhance its own dominant condition, but when this condition begins to be threatened by the emergence of a meaningful competitor, the hegemon, the United States in our contemporary example, may turn against the rules-based system and fall back onto a power-based strategy to delay or even prevent the newly emerging power from taking over the dominant position—China in the present case. This strategy of seeking to delay the transition from one dominant power to the other only makes sense from a narrow and myopic perspective in which the challenging power or powers do not react. If they do, by raising their own tariffs and leveraging other

policy instruments, the payoff to the hegemon is reduced. More important, it may be left exposed to suffer damages in the future caused by the rising powers acting in a system rendered undisciplined and weakened, ironically—as is happening now—by the hegemon itself (Mattoo and Staiger 2019).

Even in the most charitable interpretation of the current situation—that there is a certain logic for the United States to move from a rules-based to a power-based regime by means of trade policy—this misses the point that longer term it is better to count on a multilateral system capable of restraining other economic powers from actions that would damage the interests of the United States. There is nothing new in this proposition. It was dutifully applied by the United States when its GDP was the highest ever as a proportion of world GDP and there was little question about its military supremacy. That moment was right at the end of World War II. That was a time when the main multilateral institutions and other initiatives of international cooperation were launched under US leadership and over time supported the recovery and ascendancy anew of Europe and Japan. But more important—from the American perspective—these initiatives and institutions proved decisive in consolidating the economic and geopolitical supremacy of the United States, not least over the Soviet Union.

### THE MYSTERY OF SEEKING TO CRIPPLE THE WTO

Among the institutions the United States endeavored to create and nourish, the one charged with establishing the rules for international trade (the GATT/WTO) has been by many measures extremely successful. Trade across borders has been key for countries that have achieved the most significant economic progress since the middle of the twentieth century, with China being exhibit number one, as discussed by L. Alan Winters in chapter 4. This performance would be unthinkable without the system that has allowed for increasingly open markets and rules to make them work more fluidly. The GATT/WTO has been the core of that system. Round after round, agreement after agreement, effort after effort by states, trade ministers, diplomats, and dedicated officials over several generations have delivered a governance mechanism that, despite its shortfalls, is considered one of the most singularly effective international institutions. By virtue of being endowed with a set of procedures to address disputes that uniquely constitutes an enforcement apparatus, the WTO is an aspirational model

for other international arrangements that count on good rules yet lack levers to enforce them.

The WTO was provided at its birth (in 1994) with the Dispute Settlement Understanding mainly as a result of reasonable US insistence on the importance of implanting within the new institution a robust capacity to predictably secure the rights and enforce the obligations of the members, particularly as new sectors and issues were being brought under the disciplines of the GATT successor. Other countries overcame their original resistance as it became clear that the DSU would mitigate the risk of suffering from arbitrary and unilateral actions, particularly from the most powerful members.

In retrospect, the multilateral instrument for regulating international trade—the GATT followed by the WTO—has performed remarkably well, both in times of buoyancy such as during the great moderation, as well as in times of crisis such as the Great Recession, having usefully and beneficially served its members, the United States certainly among them. While the dispute settlement system has not always been successful in addressing trade conflicts, most disputes have been resolved. As noted by Jaime de Melo in chapter 15, even in very politically sensitive cases such as the long-running conflict between the United States and Latin American banana exporters and the EU, the system eventually delivered.

Notwithstanding the record, President Trump and his officials have not been hesitant about expressing their annoyance with the WTO. Curiously, after characterizing the WTO in exactly the same terms he had used before for the TPP and NAFTA as “the single worst trade deal ever made” (Micklethwait, Talev, and Jacobs 2018), he threatened to withdraw the United States from the organization, an action that by all accounts will carry a high cost for the world, including the United States itself, as Bown and Irwin have submitted in a careful analysis:

A decision by President Trump to withdraw from the WTO—if deemed legal under U/S/ law—could deal a disastrous blow to America’s foreign trade. The cost to consumers and import-reliant manufacturers . . . would be enormous. And the resulting foreign retaliation against American exporters—farmers and manufacturers alike—would severely damage the economy. (Bown and Irwin 2018, 8)

Having a country that represents almost one-fourth of world GDP and 15 percent of global exports leave the WTO clearly would enormously

weaken the organization's mission and efficacy, causing serious damage to the prospects for global prosperity. Unfortunately, the United States does not even need to go outside the WTO to cause enormous damage, for it can do exactly that from inside simply by continuing to do what it has been doing for several years: blocking the appointment of any new members of the Appellate Body (AB) of the Dispute Settlement (DS) mechanism. The AB must have seven judges or members, and it needs a minimum of three to rule on an appeal. The term of two of the remaining three members expired in December 2019, as a result of which the AB became non-operational. This could lead to a collapse of the DS capability the WTO has had since it was created. Significantly, the WTO's most distinctive and enviable characteristic would then be lost.

As in practically every multilateral institution, there is much in need of reform at the WTO, including its DSU. Practitioners, scholars, and a number of countries have put forward sensible ideas to improve the DS process that was negotiated almost three decades ago to address conditions very different from those prevailing now and the more complex circumstances that conceivably will arise in the future.<sup>21</sup> Yet the American grievances with the DSU do not seem to stem from the objective of making it a better multilateral instrument. As in other aspects of its trade policies, the Trump administration's undertaking against the AB is rooted in wrong or even false premises. President Trump has repeatedly said that the WTO was set up for the benefit of everybody but the United States, that his country loses almost all lawsuits, and that the system has been great for China and terrible for the United States.

All these views are unsubstantiated. No serious analysis has ever produced evidence of bias against the United States.<sup>22</sup> The United States is the most frequent user of the WTO DS system, having brought more cases than China and the EU combined. The United States has a higher proportion of wins (91 percent) than other complainants. It is also true that, as a defendant, the US proportion of losses is high (89 percent). These statistics reflect the fact that countries tend to bring cases where they estimate a high probability of winning, resulting in a pattern in which complainants tend to win. An exception is disputes involving China where the United States has done very well on both sides of the argument. Jeffrey J. Schott and Euijin Jung report that between 2002 and 2018, of the twenty-three cases brought by the United States challenging China's practices, its win-loss record was 19-0, with four cases pending. Conversely, in its fifteen com-

plaints against the United States, China won only four, the United States won one and parts of three others, and six were pending (Schott and Jung 2019).

Closer scrutiny reveals that American officials are typically upset about losing cases brought against US trade remedy actions (antidumping and countervailing duties). On many occasions, the United States has been found in violation of the WTO Antidumping Agreement, a result that has ignited claims that US trade remedy laws were unfairly targeted by the WTO. To this accusation the first response must be that it is not the WTO that brings cases to the DS process. This prerogative belongs to the WTO member countries alone. Those crying foul at alleged targeting and bias should be made to confront the highly credible American analysts who agree that complaints against US trade remedy actions are caused by the United States' own aggressive use of such actions that plainly violate the rules agreed to by all signatories of the WTO, including the United States. (see, e.g., Ikenson 2017).

Be that as it may, the objective of the Trump administration seems to go beyond merely winning cases against its trade remedy actions. By blocking new appointments to the AB the Trump administration has paralyzed the DS process and caused the WTO damage that may be irreparable for a long time. Without a functioning Appellate Body, the WTO may revert back to a one-stage DS process in which adoption of panel reports can be blocked. Professor Rachel Brewster puts it succinctly:

The United States' block on Appellate Body nominations is a direct assault on the idea that disputes should be resolved through a neutral interpretation of trade law rather than more negotiated, economic-power-based solution. Without a dispute settlement system, international trade law would return to a GATT-era type system where panels would issue legal opinions but most significant trade disputes were resolved through negotiations, and where the meaning and operation of the law were largely determined through power politics. (Brewster 2018, 4)

A rationale for shutting down the AB, in addition to long-standing dissatisfaction with AB rulings against US antidumping measures, is that it closes the circle in the Trump administration's pursuit of aggressive unilateralism. If subject to WTO due process, many US trade policy actions would likely be found illegal, but such adjudication is undercut because the mechanism

charged to decide cases is no longer operational. Thus, unilateral trade actions, like imposing tariffs on automotive imports from otherwise friendly trade partners on “national security” grounds, would not be contestable at the WTO. Bilateral negotiations would be the only expedient left. The VanGrasstek view of US behavior, described above, would be validated again, along with its obvious consequence: a multiplication of costly trade wars, as countries predictably would react to more US unilateralism with their own—as has happened already in response to the questionable US section 232 and section 301 tariffs.

As noted by Simon Evenett in chapter 6 of this volume, the EU has signaled that it can also “do stupid” in imposing retaliatory tariffs. Evenett argues that the classic “playbook” for dealing with American trade discrimination—targeted retaliation, bilateral negotiations to improve market access, and cooperation with the United States to pursue joint interests related to China through discussion of new rules of the game for subsidies, SOEs, and related matters—has major weaknesses. Retaliation appears to have limited salience in affecting US political dynamics and is costly, while negotiation of new PTAs runs into European sectoral sensitivities and resistance by major trading partners to consider acceptance of EU demands on nontrade issues. Finally, although the EU has been an active proponent of WTO reform and the pursuit of cooperation on a plurilateral basis, such efforts inevitably require time to bear fruit. Worryingly, Ursula von der Leyen, the president of the European Commission who took office in late 2019, has indicated the EU may be taking a more aggressive unilateral trade policy stance, implying a possible greater willingness to emulate the United States in putting aside multilateral disciplines (Vela 2019).

It is not hard to infer that a world economy under siege by a proliferation of trade barriers would be a feeble and unstable one, and not propitious for any country. Reconstituting the appeals function should be the highest priority for all the WTO members for their own national interest, including the United States. In 2017 the US government began blocking new appointments to the AB by invoking Article 2.4 of the DSU, which indicates that decisions by the DSB shall be made by consensus. In the view of the US representatives, this provision provides their government with veto power. This interpretation is not only arguable but outright wrong, in the opinion of reputable legal experts (see, e.g., Kuiper 2017; Hillman 2018). All WTO members have the collective responsibility to fill vacancies in the AB as they arise, given their precisely defined duty to administer the rules



and procedures of the DSU. There is nothing preventing members from relying on a voting procedure to discharge their collective obligation to keep the DSU fully functional.

The WTO treaty provides that in the event of a conflict between a provision of the WTO Agreement and that of a subsidiary multilateral trade agreement (like the DSU), the provision in the WTO Agreement shall prevail. Article IX of the WTO permits voting and can be invoked if three-quarters of WTO members desire to do so.<sup>23</sup> Thus a vote to approve new appointments to the Appellate Body is possible. A vote is unlikely to be taken, however, for fear of setting a precedent and the further erosion of trust among members it may give rise to. A majority vote may also become the straw that breaks the camel's back, providing the United States with the excuse to leave the WTO, which would be a very unfortunate and costly decision for all purposes. Nevertheless, this regrettable scenario should be assessed not against a business-as-usual situation but against the prospect of a totally dysfunctional WTO dispossessed of its enforcement capacity. Preserving the existence and faculties of the WTO must be of the utmost priority.

Bernard Hoekman and Petros C. Mavroidis (chapter 7 in this volume), while not condoning the US decision to block appointment of new Appellate Body members, note that in principle many of the concerns expressed by the US government about the DSU are not particularly difficult to address. This is because, taken at face value—that is, assuming good faith, which is a questionable assumption at the time of this writing—the core of what the United States has been arguing is that WTO members should recommit to what was negotiated in the Uruguay Round. The elements of a possible solution along these lines began to emerge in late 2019. A group of WTO members tabled a proposal to reform the DSB's rules in order to address the concerns raised by the Trump administration.<sup>24</sup> An informal process during 2019 on the functioning of the Appellate Body led by Ambassador David Walker of New Zealand identified a series of measures that could be taken by decision of the WTO General Council that would address many of the matters raised by the United States. These included specific language addressing potential Appellate Body “overreach,” a decision that panels and the AB will consider the provisions in the Antidumping Agreement that pertain to zeroing and put in place a mechanism for regular dialogue between WTO members and the Appellate Body. A necessary condition for such a decision to be meaningful, as noted by Ambassador

Walker, is that there be an Appellate Body and thus that members agree to new appointments to the AB.<sup>25</sup>

At this writing in mid-2020, the United States has not considered any proposals sufficient to address its concerns. In the course of 2019, as it became more evident that efforts to induce the United States to cease blocking new appointments to the AB would not be successful, several WTO members, led by the European Union, began work on a “plan B” centered around putting in place a substitute mechanism that could be used on a voluntary basis by those WTO members who desire to be able to continue to appeal the findings of panels. This resulted in the establishment of a Multi-Party Interim Appeal Arbitration Arrangement (MPIA) in April 2020. The MPIA is intended to operate as an interim appeals board until the AB crisis is resolved. This permits signatories to appeal panel rulings and commits them to adopt and implement panel reports if they do not appeal. As of early summer 2020, twenty-one WTO members had signed the MPIA, including Brazil, Canada, China, the European Union, and Mexico.<sup>26</sup>

The MPIA reveals the strong commitment of many WTO members to retain an appeals mechanism. Whether this interim measure will evolve into a new DS system will depend on the ability of the WTO membership to agree on a broader effort to push for WTO reforms.

### **CAN WTO REFORM HELP RESUSCITATE MULTILATERAL COOPERATION?**

The careful monitoring of trade policy trends by the Global Trade Alert (see chapter 1 by Evenett) makes clear there is a large agenda confronting WTO members. A basic purpose of the WTO is to provide a platform that allows countries to agree on rules to address trade-related policies that create adverse effects for trading partners and to support their implementation. The fact that it is not fulfilling this purpose matters for the global economy.

Several of the contributions to this volume discuss policy areas that call for multilateral cooperation and rulemaking to reduce potential international spillovers of national policies.<sup>27</sup> In chapter 8, Anne Krueger discusses agricultural policies; Bernard Hoekman and Douglas Nelson focus on the need to revisit existing rules of the road for subsidies and state-owned enterprises in chapter 9; Erik van der Marel analyzes issues associated with the rise of the digital economy in chapter 10; and in chapter 11 Patrick Low

explores what can be done to blunt the potential conflict between actions to address climate change and WTO rules on the use of trade policies. All of these areas call for multilateral cooperation. Although some of these matters can be addressed partially in PTAs, the spillover effects of policies in these areas are often global in nature. Moreover, even where PTAs could in principle help to reduce the trade costs associated with national policies, in practice they may be of only limited utility. Thus Sébastien Miroudot and Ben Shepherd show in chapter 12 that to date PTAs have done little to reduce the costs of trading services. Similarly, it is unlikely that countries will be willing to consider disciplines on the use of industrial policies and subsidies in PTAs, as these would also benefit nonsignatories. A multilateral approach is required.

As noted in a 2018 report commissioned by the Bertelsmann Stiftung, a necessary condition for new rulemaking is a willingness to define a negotiating agenda.<sup>28</sup> Defining such an agenda requires dialogue and deliberation, something that has been in short supply (see, e.g., Odell 2015). Reasons for this include the consensus working practice and the outdated approach that is embedded in the WTO to recognize differences in levels of development and capacity across the membership (Hoekman 2019). Space constraints preclude a lengthy discussion of possible WTO reforms. Here we simply note that some initial positive steps have already been taken. One positive development is the breaking of the consensus constraint, with groups of WTO members deciding to launch plurilateral discussions and negotiations on new rules of the game or to agree on good regulatory practices in an area. Plurilateral discussions in the WTO are addressing liberalization of trade in environmental goods, approaches to assist micro-, small, and medium-sized enterprises (MSMEs), rules of the game for e-commerce and digital trade, action to facilitate investment, and disciplines on domestic regulation of services. While not a panacea, plurilateral initiatives may lend themselves better to addressing specific policy cooperation challenges than PTAs or broader multilateral trade negotiation rounds that include all WTO members (Hoekman and Mavroidis 2015; Hoekman and Sabel 2019). As Hoekman and Nelson argue in chapter 9, this applies also to policies that are key areas of disagreement, such as subsidies and SOEs, in the sense that the major trading powers must agree on any rules in these areas.

Another positive step relates to the urgent challenge of dealing more effectively with development differences. In part the urgency is because the

matter is a core demand of the United States (in this case supported by the EU and many other OECD nations). As important, a good case can be made that the approach that has historically been pursued is outdated and ineffective. The engagement of developing nations in the WTO is premised on the principle of “special and differential treatment” (SDT). This implies less than full reciprocity in trade negotiations and acceptance that developing nations should be less constrained in the use of trade policies than high-income countries. The constituent elements of SDT date back to the mid-1960s and were designed for a world economy that no longer exists. The challenge today is to identify and implement policies that promote economic development in a world of global value chain-based production, e-commerce, and digitization where small firms can become micro-multinationals by using electronic platforms and exploiting mobile information and communications technologies. Such policies will not revolve around trade policy but will rely on measures to enhance access to finance, adopt new technologies, ease cross-border payments, and develop efficient logistics.

A central feature of SDT is that it applies to all developing countries. The WTO, following precedent set under the GATT, does not define what constitutes a developing country, leaving it to members to self-determine their status. Outside the group of forty-seven (UN-defined) less-developed countries (LDCs), the only distinct group of developing countries identified in the WTO, there are no criteria that allow differentiation between developing countries. The United States has proposed that members agree to such criteria. This is very controversial and unlikely to be accepted. It has been proposed many times in the past to no avail. More important, it is not necessary. Rather than continuing to fight old battles, it would be more productive for WTO members to do more to identify good practices and policies to address market failures, complemented by provision of assistance where needed.

It is not sufficiently recognized that the WTO has made strides in revisiting the approach used to recognize economic development differences. Examples include the 2013 Agreement on Trade Facilitation and the launch of the Aid for Trade program at the WTO Ministerial conference in Hong Kong in 2005—an initiative that Patrick Messerlin helped to prepare the ground for in his role as co-chair of the UN Millennium Project Task Force on Trade and Finance in 2005 (see Millennium Project 2005)—and the associated Enhanced Integrated Framework for LDCs. Two chapters in this

volume discuss these matters. In chapter 13, Olivier Cattaneo and Sébastien Miroudot spell out the implications of changes in the structure of the world economy and the need to update trade and development paradigms. In chapter 14, Jean-Jacques Hallaert provides a critical assessment of the WTO's Aid for Trade Initiative.

### CONCLUDING REMARKS

It remains to be seen how deeply the Trump policies will damage the international trading system, and how long they will last. In only three years they have proven to be deleterious to the economic and geopolitical benefit of the United States. Irrespective of the duration of the “siege” endured by the rules-based mechanisms, it is clear that the system has suffered enormous harm caused by the US administration since 2017, but also from key governments’ unwillingness to keep reforming it. As the work of several contributors to this volume shows, there is no lack of ideas for how to mend it and make it more effective. Political willingness to acknowledge that a better-functioning and stronger multilateral system is in the interest of all nations has been missing in the in the twenty-first century, with unmistakably tragic consequences. An enlightened reckoning, perhaps impelled by recent events, will be necessary to set in motion the reform and regeneration of the mechanisms of international cooperation and coordination—the trading system included. Such action will go far to propel both a recovery from the economic devastation caused by the great pandemic and a future of global prosperity, peace, and security.

### NOTES

1. The appendix to this book provides a selected list of Patrick’s publications.
2. Patrick Messerlin played a leading role in economic analysis of anti-dumping by the European Community (see in particular Messerlin 2001, 1989, and 1990).
3. For an excellent and succinct analysis of the TPP, see Schott (2018).
4. For a careful calculation of the economic cost, see Petri and others (2017).
5. Office of the United States Trade Representative, Executive Office of the President, Summary of the Objectives for NAFTA Renegotiation, July 17, 2017 (p. 2).

6. As in the case of the automotive sector, the textiles and apparel sector was also subject to more stringent rules of origin, which are also bound to impact the competitiveness of this industry in the regional and global markets.

7. Another highly problematic precedent is the so-called China clause by which a member could withdraw from the agreement if another of the partners enters into a trade accord with China that the member does not approve of. The China clause is clearly an economically redundant condition, given the stringent rules-of-origin and investment disciplines agreed to in the new deal. And it is certainly an unwarranted geopolitical overreach on the part of the United States.

8. In May 2019, Mexico was also hit with a tariff on its tomato exports to the United States, precipitating negotiations that led Mexico to accept nontariff barriers—in the form of additional inspections at the border—as well as higher reference prices for this product.

9. Patrick Messerlin was one of the first to analyze the use of contingent protection instruments against China; see Messerlin (2004).

10. Industrial subsidies and the significant role played by state-owned enterprises are examples. These are discussed in chapter 9 by Hoekman and Nelson.

11. Some of the decreases in tariffs were planned before the trade war, such as the adjustments to comply with the WTO Information Technology Agreement. Still, a substantial portion of the tariff reductions on imports from other countries are in reaction to the American trade hostilities.

12. See Economic and Trade Agreement between the Government of the United States and the Government of the People's Republic of China, January 15, 2020, [https://ustr.gov/sites/default/files/files/agreements/phase%20one%20agreement/Economic\\_And\\_Trade\\_Agreement\\_Between\\_The\\_United\\_States\\_And\\_China\\_Text.pdf](https://ustr.gov/sites/default/files/files/agreements/phase%20one%20agreement/Economic_And_Trade_Agreement_Between_The_United_States_And_China_Text.pdf).

13. Although imports by the United States of Chinese steel and aluminum are relatively small, US tariffs on these products marked the start of the trade war as the Chinese government responded with tariffs of 15 to 25 percent on \$2.4 billion of imports from the United States.

14. General Agreement on Tariffs and Trade (GATT), Part II, Article XXI, "Security Exceptions," October 30, 1948, Geneva Final Act. Article XXI states that "Nothing in this Agreement shall be construed (a) to require any contracting party to furnish any information the disclosure of which it considers contrary to its essential security interests; or (b) to prevent any contracting party from taking any action which it considers necessary for the protection of its essential security interests (i) relating to fissionable materials or the materials from which they are derived; (ii) relating to the traffic in arms, ammunition and implements of war and to such traffic in other goods and materials as is carried on directly or indirectly for the purpose of supplying a military establishment; (iii) taken in time of war or other emergency in international rela-

tions; or (c) to prevent any contracting party from taking any action in pursuance of its obligations under the United Nations Charter for the maintenance of international peace and security.

15. Ukraine complained before the WTO in 2016, arguing that it would suffer a significant reduction in trade with Asia and the Caucasus region after the Russian government prohibited rail and road transport from Ukraine unless the route also went through Belarus.

16. The national security argument on the steel and aluminum tariffs is demolished in just one paragraph of Bown and Irwin (2019, p. 128).

17. Office of the United States Trade Representative (2017, 4n10).

18. Office of the United States Trade Representative (2018, 3),

19. Office of the United States Trade Representative (2018, 19).

20. Office of the United States Trade Representative (2018, 182).

21. See, for example, Payosova, Hufbauer, and Schott (2018). For government proposals, see e.g., the submission to the WTO General Council by the EU, China, Canada, India, Norway, New Zealand, Switzerland, Australia, Korea, Iceland, Singapore, Mexico, Costa Rica, and Montenegro on December 13, 2018. WTO, WT/GC/W/752/Rev.2.

22. It is worth noting that for most of the WTO's history one of the judges of the AB has been an American, a circumstance not enjoyed by any other country.

23. Art. IX WTO specifies that if voting occurs, unanimity is required for amendments relating to general principles such as nondiscrimination; a three-quarters majority for Interpretations of provisions of the WTO agreements and decisions on waivers; and a two-thirds majority for amendments relating to issues other than general principles. Where not otherwise specified and consensus cannot be reached, a simple majority vote suffices.

24. See note 30.

25. Informal Process on Matters related to the Functioning of the Appellate Body—Report by the Facilitator, H. E. Dr. David Walker (New Zealand), WTO JOB/GC/222, October 15, 2019.

26. Jointly the signatories represent 14 percent of the WTO membership, counting the EU as one. Disputes between MPIA signatories accounted for about a quarter of the total DSU caseload from 1995 to 2019. While substantial, many frequent users of the DSU, including India, Indonesia, Malaysia, and Russia, did not sign the MPIA.

27. For a comprehensive catalogue of such policy areas, see the papers compiled by the E-15 Initiative at <https://e15initiative.org/publications/executive-summary-synthesis-report-full-report/>.

28. Bertelsmann Stiftung, "Revitalizing Multilateral Governance at the World Trade Organization, 2018," <https://www.bertelsmann-stiftung.de/en/publications/publication/did/revitalizing-multilateral-governance-at-the-world-trade-organization/>.

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