ECN330 Module 1 SRP. Economic Integration versus Trade Liberalization

1. Globalization

Globalization before a multilateral system

The evolution of international commercial relations over the last 150 years charts major shifts in the balance of power among nations, the willingness of countries to create political institutions that govern international transactions, technological changes that facilitate transport and communications linkages, and other market forces. Prior to the 20th century, in the absence of international organizations enforcing a system of multilateral rules or disciplines on commercial policy, the principal instrument of diplomacy for commercial relations was the bilateral friendship, commerce, and navigation (FCN) treaty. These formed a legal framework for reciprocal treatment on a wide range of matters of international economic interest (Walker, 1958).[1] Non-discriminatory treatment in general relations aimed at strengthening normal, friendly (peaceful) relations between the signatory countries, but the emphasis was on the rights of nationals of each country in the event either should be at war with a third country, providing evidence that war was ever present (Foster, 1946).[2]

FCN treaties were tailored to suit the commercial interests and foreign relations of the parties involved rather than to create standard international law. However, they did establish legal norms for non-discriminatory treatment by formalizing the most-favored-nation (MFN) principle, ensuring that the legal treatment, under an FCN treaty, of one partner country should be at least as good as for another country (Coyle, 2013).[3] However, while MFN treatment existed since the 17th century, the principle neither implied free trade, nor guaranteed a freer trade regime, nor did it prevent different (i.e., discriminatory) treatment between nationals and foreigners. Bilateral reciprocity usually extended special access or preferential treatment that, by definition, violated MFN (Viner, 1924).[4]

The focus of FCN treaties shifted in response to expanding international shipping in the 19th century and to the volume and scope of foreign investments in the 20th century (Walker, 1958; Coyle, 2013). Provisions related to property protection, the right to control and manage enterprises established or acquired in the host country, and the right to employ managerial, professional, and other specialized personnel in the host country also needed to be included in treaty (Lewis and Ottley, 1983)[5]. Moreover, the rise of the US as a preeminent international power, major global creditor, and major trading nation undoubtedly tilted bilateral FCN treaty negotiations to reflect the country's new economic status and its ability to project power by pursuing its commercial interests through foreign policy.

Prior to World War I, the global economy was at the height of colonialism and imperialism. Much of Africa and Asia was claimed or under foreign control. Commercial and trade relations reflected arrangements among colonial master and subject territories. Imperialism strengthened with the rise of industrialization and the need for raw materials. Empires competed for influence and resources that led to power and wealth, which, in turn, fostered unrestrained nationalism. Historical grievances, rival empires, and complex balance of power shifts created secretive shifting and entangling alliances.

In anticipation of the end of hostilities in 1918, US President Wilson addressed the US Congress with a speech proposing a new world order, outlining his "14 point" peace process. These mostly addressed issues of sovereignty, e.g., the delineation of new national borders and international matters, but two points (2 and 3) touched upon issues that related to commercial treaty and point 14 pushed for an institutional multilateral framework (i.e., the League of Nations [LoN]). Point 2 called for freedom of navigation upon the seas, outside territorial waters, in times of peace and war, reiterating much of what existed previously in bilateral FCN treaties. Point 3 called for the removal of all economic barriers and the establishment of "equality of trade conditions" among all the nations consenting to peace and associating themselves for its maintenance. The meaning of this clause was for "fair and equitable" distribution of raw materials prohibiting the use of restrictive trade practices (National Archives, 2016).[6]

From its inception the LoN was concerned with the promotion of freer trade, but the post-war financial situation of Europe was unstable. The gold standard that supported the system of exchange prior to the war was based on international cooperation without a supranational organization. In the aftermath of the war, ill will, war debts and reparations destabilized the global economy (Eichengreen and Irwin, 2010).[7] There were dislocations of persons, difficulty of transport across newly established borders, fluctuating exchange rates, interruption in the flow of international credits resulting in severe credit shortages, impediments of gold exports, and increased use of restrictive trade practices. The breakdown of the financial system exposed the inter-play between domestic policies to maintain the balance of payments and trade policy.

The limitations of the lack of a proper multilateral framework with supranational organizational authority during the inter-war period was evident. The lack of cooperation persuaded world leaders that economic nationalism was the root of the instability in the international system and for the poor relations among nations. Non-discrimination in trade was the basis for the economic cooperation that was considered essential to an enduring post-war peace (AFR, 2016).[8]

Globalization through political, economic, social, and cultural integration is a salient feature of the modern world. However, the existing post-war multilateral institutions and international organizations are weakened and under increasing strain to remodel themselves for relevance and legitimacy to address contemporary problems. The world

[1] Walker, H., Jr., 1958. "The post-war commercial treaty program of the United States", *Political Science Quarterly*, 73(1 Mar):57-81.
[2] Foster, A., 1946. "Some aspects of the commercial treaty program of the United States – Past and present", *Law and Contemporary Problems*, 11(4):647-52.
[3] Coyle, J.F., 2013, "The treaty of friendship, commerce and navigation in the modern era," *Columbia Journal of Transnational Law*, 51(2 Sep):302-59.
[4] Viner, J., 1924. "The most-favored-nation clause in American commercial treaties," *Journal of Political Economy*, 32(1 Feb):101-29.
[5] Lewis, J.B. and B. Ottley, 1983. "Title VII and friendship, commerce and navigation treaties", Ohio State Law Journal, 44(1):45-91.
[6] National Archives, 2016, "President Woodrow Wilson's 14 points (1918)", https://search.archives.gov/search?query=woodrow+wilson%27s+14+points+speech&submit=&utf8=&affiliate=national-archives.
[7] Eichengreen, B. and D.A. Irwin, 2010. "The slide to protectionism in the Great Depression: Who succumbed and why?", *Journal of Economic History*, 70(4 Dec):871-97.
[8] American Foreign Relations (AFR), 2016. http://www.americanforeignrelations.com/E-N/Most-Favored-Nation-Principle-Mfn-treatment-in-practice-1934-1974-unconditional-mfn-as-one-instrument-of-trade-liberalization.html#ixzz4NdN4DzFX.

faces unprecedented global challenges and a series of overlapping crises that pose serious risk for the future welfare of humankind: (i) geopolitical rivalry, in particular between the US and China, which sets the agenda for other spheres; (ii) economic and financial instability, with the risk of increased protectionism and isolation; (iii) war, conflict and insecurity threats which is both leading to human death and suffering, and indirectly affecting the global economy with higher energy and food prices, and supply chain disruptions; (iv) climate change that is already affecting millions in the form of an increase occurrence of extreme weather; (v) pandemics and other health crises which continue to affect the global economy and the ability to find collective solutions; and (vi) international migration, pushed by the above crises, is testing national economies and international solidarity.

Globalization, trade liberalization and integration

There are many definitions of globalisation, but an all-encompassing definition must include the processes by which the main types of cross-border flows occur: trade (in both goods and services), information, people (including tourists, students and migrants) and capital [1]. Economic integration measures the amount of this activity, its direction, and how widespread it is among countries. Liberalization historically referred to the cross-border movement of goods (i.e., trade liberalization), but now includes cross-border services and addresses access to information.

The last "golden age" of globalization came in the 1980s according to the World Bank.[9] Economies became more integrated (i.e., globalised) as cross-border flows of trade, investment and financial capital increased. Consumers bought more foreign goods, more firms operated across national borders, and savers invested more than ever before in far-flung places. This coincided with a large group of developing countries breaking into global markets or reducing obstacles by which they could participate in the global economy.

In 1980 only 25% of the exports of developing countries were manufactures; by 1998 it rose to 80%. This was an astonishing transformation over a very short time involving a diverse set of countries. With the dissolution of the Soviet Union, the end of central planning in central and eastern Europe, and greater freedoms that accompanied the opening of those countries, international migration and capital movements became substantial.

International financial flows became bigger. For example, daily foreign-exchange turnover increased from 15bn in 1973 to $1.2trn in 1995. Cross-border sales and purchases of bonds and equities by US investors rose from the equivalent of 9% of GDP in 1980 to 164% in 1996 [2].

But despite the talk of a new global economy, globalisation is a process. The 50 years before the 1st world war also saw large cross-border flows of goods, capital and people. In the interwar period, globalisation ended abruptly when the world moved into a period of fierce trade protectionism and tight restrictions on capital movement. In the early 1930s, the US sharply increased its tariffs, and other countries retaliated, making the Great Depression worse. The volume of world trade fell sharply. International capital flows virtually dried up as governments imposed capital controls to insulate their economies from the global slump. Capital controls were maintained after the 2nd world war. The victors kept their exchange rates fixed—an arrangement known as the Bretton Woods system.

In the early 1970s, the Bretton Woods system collapsed, and currencies "floated" against one another at rates set by markets. This signalled the rebirth of global capital markets. The US and Germany quickly stopped trying to control the inflow and outflow of capital; the UK abolished capital controls in 1979 and Japan (mostly) in 1980. However, France and Italy did not abandon the last of their restrictions on cross-border investment until 1990, illustrating how some Europeans raise concerns with the power of global capital markets [2].

Whether globalisation is for good or ill has long been a topic of heated debate. A positive view is that globalisation has the potential to boost productivity and living standards everywhere. A globally integrated economy can lead to a better division of labour between countries, allowing low-wage countries to specialise in labour-intensive tasks while high-wage countries use workers in more productive ways. It allows firms to exploit bigger economies of scale. And with globalisation, capital can be shifted to whatever country offers the most productive investment opportunities, not trapped at home financing projects with poor returns [2].

Critics of globalisation argue that increased competition from low-wage developing countries destroys jobs and pushes down wages in rich economies. A "race to the bottom" occurs as countries reduce wages, taxes, welfare benefits and environmental controls to make themselves more "competitive". Pressure to compete erodes the ability of governments to set their own economic policies. Another concern is the increased power of financial markets to cause economic havoc, e.g. the European currency crises of 1992 and 1993, Latin American debt crisis of the 1980s, SE Asia financial crisis in 1997 [2], and later the global financial crisis (GFC) of 2008.

In an economist's dream world, things, ideas and people would flow freely across borders. Constraints on trade once bundled consumption and production together, limiting their growth. Richard Baldwin, a Geneva-based economist, describes globalisation as a series of unbundlings resulting from two forces that drive the increased flows of goods and services, and money and people [3].

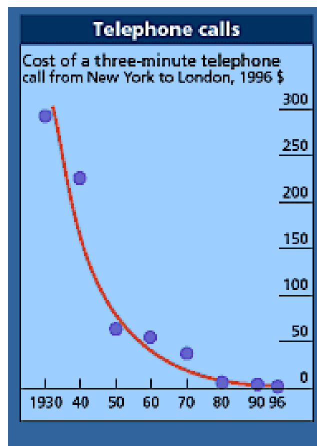
The first is technology. From the domestication of the camel around 1,000BC to the first commercial steam engine in 1712, the collapse in the cost of transport resulted in the first great wave of globalisation, unbundling (or the separation of) production and consumption [3][2]. This happened between 1870 until the outbreak of the first world war when shipping, i.e., steam ships and railways facilitated the movement of goods [2].

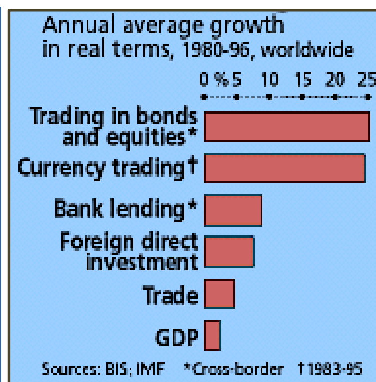
However, moving ideas remained expensive until the end of the 20th century [3]. When the costs of communication and computing fell rapidly, the natural barriers of time and space that separate national markets fell further [2]. The cost of a three-minute telephone call between New York and London fell from $300 (in 1996 dollars) in 1930 to $1 in 1997 (see chart, cost of phone calls). The cost of computer processing power fell by an average of 30% a year in real terms in the 20 years to 1996 [2]. Sending a single document by an overnight courier could cost as much as $50 [3]. The internet and the digital era was a boon for international trade in services.

The second driving force was countries' willingness to pursue trade liberalisation or economic integration. The Uruguay round of trade negotiations under the General Agreement on Tariffs and Trade (UR-GATT) resulted in

[9] "The New Wave of Globalization and Its Economic Effects", in *Globalization, Growth and Poverty: Building an Inclusive World Economy*, World Bank, Jan 2002, https://documents1.worldbank.org/curated/en/954071468778196576/310436360_20050007015044/additional/multi0page.pdf.

most countries lowering barriers to foreign trade. Most countries were more welcoming of international capital as well. Although liberalisation proceeded at different speeds in different places, the trend was worldwide. In the decade before 1997, trade increased twice as fast as output, foreign direct investment (FDI) three times as fast and cross-border trade in shares ten times as fast (see chart, annual growth rates) [2]. Regional integration such as the creation of the European Union (EU) moved this process even further than in other countries.





Washington Consensus and policy reform

The transformation from central planning and/or from closed economies to more open economies with a market orientation raised the profile of multilateral institutions such as the IMF and World Bank. The creation of the WTO complemented their mission. The "Washington Consensus" in 1989 listed ten specific policy reforms that were considered as having wide agreement for what good policy prescription would be.[10] The details of these prescriptions, the political and legal institutions that were necessary, and the sequencing in which they should be implemented were never part of any consensus. Moreover, they were intended for Latin America, which had been recover from the 1980s debt crisis, referred to as the lost decade. Nevertheless, the list included:

- Fiscal disciplines
- Public investment in education, health and infrastructure
- Broadening the tax base (and cutting the marginal rate)
- Financial liberalization (e.g., a market-determined interest rate, and reforms toward a more open capital account – this was not a suggestion for capital market deregulation or lifting of capital controls)
- Elimination of barriers to foreign direct investment
- An exchange rate regime at a sufficiently competitive rate to induce nontraditional exports – it did not prescribe either a fixed or flexible rate
- The use of tariffs rather than quotas to achieve any policy objective that required restricting imports
- Privatization of state-owned enterprises
- Deregulation in the meaning of increased competition (e.g., improving the "ease of doing business") and
- Creation of a legal system that secures property rights.

From these prescriptions, it is understandable how anti-globalization activists might confuse a set of good public policy practices for the promotion of a neo-liberal order calling for small government. Regardless of one's viewpoint of the Washington consensus, the measures were consistent with the trends toward economic integration.

2. Integration and Convergence

Convergence criteria

It is not possible to discuss economic integration without acknowledging the need for political and legal integration. Even the most basic form of economic integration, i.e., trade liberalization of goods, requires some alignment of political institutions or policy. Duty-free trade vis-à-vis the partner country is an alignment of trade policy, a harmonization of tariffs. If the terms of a trade agreement are to be respected, then the signatory countries must, to some degree, implement, enforce, and interpret those terms, i.e., a legal alignment or a common dispute settlement process. The greater the economic integration, the more involved the political and legal integration.

Consider the EU. The EU enshrines four freedoms: the free movement of goods, services, capital and persons. Trade policy is harmonized (duty-free trade vis-à-vis members and common tariffs rates on goods from non-member states). Regulations that affect all freedoms require them to approximated (i.e., made similar) at a minimum or made identical (harmonized) at a maximum. Finally, to ensure implementation, enforcement, and interpretation of those freedoms, national courts are superseded by EU courts.

Integration gives rise to convergence. An important gauge of the degree of product-market integration is the extent to which prices converge across countries. In theory, free trade should push prices together as competition forces high-cost producers to lower their prices. Studies show, however, that large divergences in price can persist for long periods. Laptop computers and Levi's jeans, for example, are consistently cheaper in the US than in Europe or Japan. This reflects a variety of factors, including tastes, transport costs, differences in taxes and inefficient distribution networks. Some of the difference is due to the persistence of import barriers [2].

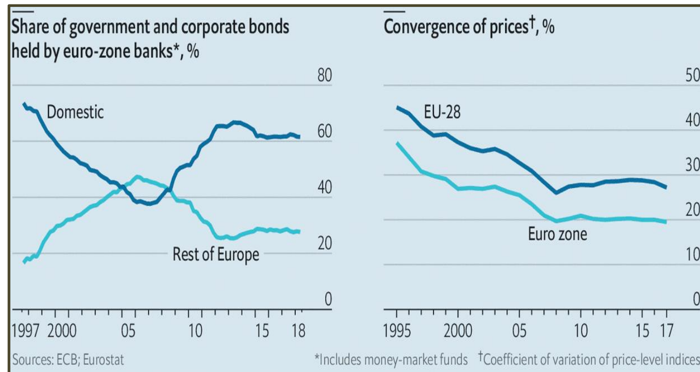
Product markets are still nowhere near as integrated across borders as they are within nations. Consider US-Canadian trade in the 1990s, one of the world's least restricted borders. Trade between a Canadian province and a US state was 20 times smaller, on average, than domestic trade between two Canadian provinces, after adjusting for distance and income levels. For all the talk of a single market, the US-Canadian markets were substantially segmented from one another [2].

In the EU's more integrated single market prices and wages should equalise as firms and workers arbitrage differences. This measure pointed to rapid convergence in the EU (see chart, convergence in prices), turning the continent into something akin to the US – itself an imperfect single market. Prices steadily converge within the EU but even faster within the eurozone countries. Investors were more willing to hold bonds of another country, suggesting more integrated capital markets. But in 2008, the GFC stalled the progress. Firms in increasingly cosseted national markets raised prices without losing share to other European firms. Part of that was down to the shift towards services, some of which are harder to trade [4]. The willingness of investors to hold the bonds of foreign firms or governments decreased, suggesting a reversal of globalisation.

Abolishing barriers to trade in services is harder. What stops services moving across borders is often how they are

[10] Williamson, J., "The Washington Consensus as Policy Prescription for Development", Institute for International Economics, Jan 2004, https://www.piie.com/sites/default/files/publications/papers/williamson0204.pdf.

regulated. In advanced economies services activities account for a larger share of GDP. So, the problem is if nothing is done to deepen services markets then market integration covers a shrinking part of the economy. With the advent of the euro, lenders increasingly ventured beyond their national borders to the rest of Europe. In the decade to 2007, the share of bonds held by EU banks issued in countries other than the banks' own tripled to 46% - overtaking the amount of bonds they had issued by companies and government entities in their own countries. The prospect of a true pan-European financial market seemed close, but the trend quickly reversed with the GFC (chart, share of government and corporate bonds) [4].



While product and capital markets may have become increasingly integrated, labour markets have not. Tens of millions of people work outside their home countries. Yet labour is less mobile than it was in the second half of the 19th century, when some 60m people left Europe for the New World. Even within the EU, which gives citizens of any member state the right to work in another, only a small proportion of workers ventures across national borders. Language, cultural barriers, and incompatible educational and professional qualifications all combine to keep labour markets national [2].

It seemed almost inevitable that the world would become ever more integrated and borders less bothersome. The GFC of 2008, which spread havoc around the world faster than any previous financial crisis, called that assumption into question. Some predicted another era of "de-globalisation" [1].

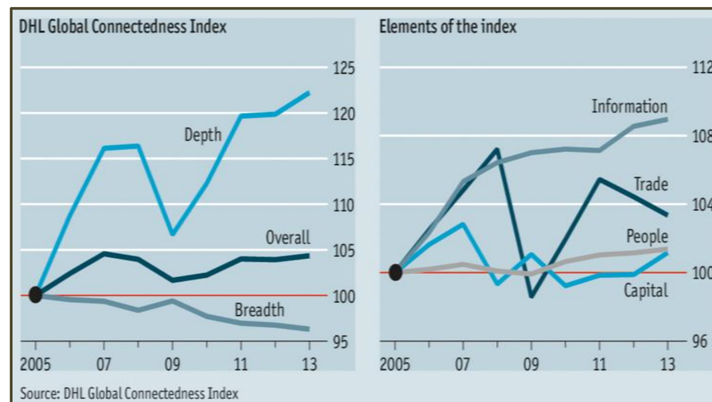
The reality was always going to be more nuanced. Globalisation's advance has never been inevitable or smooth. That is the conclusion of a DHL Global Connectedness Index study (Nov 2014).[11] Two economists, Pankaj Ghemawat of New York University's Stern School and Steven Altman of IESE Business School compiled it using data from 140 countries, which accounted for 99% of the world's GDP and 95% of its population. It showed that, after a big post-crisis drop, the trend of growing global interconnection resumed in 2013 [1].

The index uses the flow of the four main types of cross-border and tracks not just the depth of international connections (how much activity crosses borders), but also their breadth (how many different borders are being crossed) and their direction (how do outward and inward flows compare). The authors found that the depth of global integration, probably the most straightforward definition of globalisation, fell sharply after 2008, by nearly one-tenth, but it recovered strongly and by 2013 it was well above its pre-crash peak (see chart, global connectedness) [1].

By contrast, the breadth measure continued to slide in 2013 and was nearly 5% below its peak. That is, there were more cross-border connections being made, but with fewer places. This may have reflected the growing popularity of bilateral trade deals in the absence of big multilateral liberalisations. Another factor may be Western firms' slow response to the growing weight of emerging economies. In 2013 emerging economies generated only 17% of the profits of 100 of the biggest firms based in rich countries, even though they accounted for 36% of the world's GDP. The ten countries that globalised most in 2013 were emerging markets, most in Latin America and the Caribbean [1].

As the right-hand-side of the chart (elements of the index) shows, the globalisation of information, measured by such things as the number of cross-border phone calls and Skype usage, slowed after the crash but did not fall, and accelerated again in 2013. Capital flows remained below pre-crisis levels, however. Trade in goods and services plunged in the aftermath of the crash, rebounded a bit, and then started sliding again, when measured by value (volumes rose, albeit sluggishly) [1].

How worrying was the decline in trade? The authors found that the lower share of traded goods and services in total output was largely a function of sluggish global demand. There was evidence that protectionism was growing. Global Trade Alert, a watchdog, reported that during 2008-14 over 70% of the changes to trade rules around the world curbed trade, rather than spurring it. The WTO charged with resisting such measures, struggled to do so [1].



Trilemma over integration, democracy and sovereignty

Past episodes of deglobalisation suggest that political pressure to retreat from the world builds slowly but is also slow to dissipate. The fact that globalisation was advancing again after the GFC was encouraging, but further reversals are perfectly possible [1] as Brexit, geopolitical tensions, and the pandemic testify.

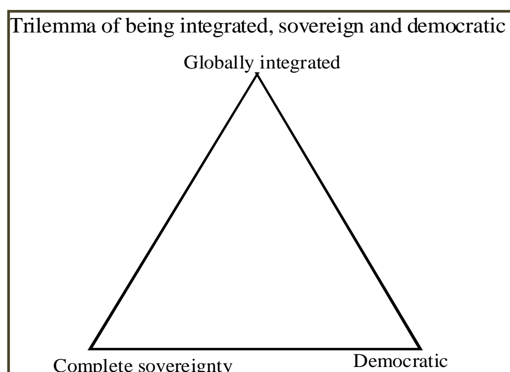
The backlash against globalisation through the Brexit vote blindsided most economists. Free trade has always been a hard sell politically, but those pressing for globalisation have tended to win more battles than they have lost. A position once considered near-heretical is that globalisation itself seems to create forces that erode political support for integration has gained currency [5].

Dani Rodrik of Harvard University is the best-known author of such critique. In the late 1990s he pointed out that deeper economic integration required harmonisation of laws and regulations across countries. Differences in rules on employment contracts or product-safety requirements, for instance, act as barriers to trade. Post-2000 mega-trade

[11] DHL, "Global Connectedness Index", 2014; and McKinsey Global Institute, "Global Flows in a Digital Age", 2014.

negotiations (e.g. the Trans-Pacific Partnership and Transatlantic Trade and Investment Partnership) focused more on "non-tariff barriers" than they did on tariff reduction. But the consequences often ran counter to popular preferences: the French might find themselves barred from supporting a French-language film industry, for example [5].

Deeper integration, Mr Rodrik reckoned, would therefore lead either to an erosion of democracy, as national leaders disregarded the will of the public, or would cause the dissolution of the nation state, as authority moved to supranational bodies elected to create harmonised rules for everyone to follow. These trade-offs create a "trilemma", in Mr Rodrik's view: societies cannot be globally integrated, completely sovereign and democratic (see chart, trilemma)—they can opt for only two of the three. In the late 1990s Mr Rodrik speculated that the sovereignty of nation states would be the item societies chose to discard. By 2020 it seemed that economic integration was most vulnerable [5].



Alberto Alesina of Harvard University and Enrico Spolaore of Tufts University presented a different but related view of the trade-offs entailed by global economic integration in "The Size of Nations" (2003). They note that there are advantages to being a large country. Bigger countries can muster more resources for national defence, for instance. They also have large internal markets. But bigness also carries costs. The larger and more heterogeneous a country, the more difficult it is for the government to satisfy its citizens' political preferences. There is less variation in political views in Scotland, to take one example, than across Britain as a whole. When policy is made by the UK parliament (rather than in Edinburgh, Belfast and so on) the average Briton is slightly less satisfied with the result [5].

Global integration, Messrs Alesina and Spolaore argue, reduces the economic cost of breaking up big countries, since the smaller entities that result will not be cut off from bigger markets. Meanwhile the benefits of separatism, in terms of being able to cater better to the preferences of voters, are less diminished. So, the global reduction in barriers to trade since the second world war, the pair contend, at least partly explains the simultaneous growth in the number of countries, even if national fractures often involve, or lead to, political instability and violence [5].

In 1713, the Abbot of Saint-Pierre wrote "the Project for Bringing about Perpetual Peace in Europe". Saint-Pierre's blueprint is strikingly similar to the EU as it stands out now, even calling his scheme a "European Union". At the heart of both schemes is a radical idea. Under his plan, sovereigns would submit to a superior law, enforced by independent supranational institutions. Three centuries of on-and-off wars and failed attempts to unify the continent suggested Saint-Pierre was on to something (despite the many critics of his time calling the scheme naïve).

Saint-Pierre had a subtle understanding of sovereignty, which still applies today. One perspective put forth by Brexiters, is that pooling sovereignty weakens it. For Saint-Pierre, true sovereignty involved no longer fearing one's neighbours, since insecurity makes independence an illusion. The same logic works in the EU. Small countries appreciate the EU because it protects them from the excesses of big countries. He understood that sacrificing sovereignty is a means of saving it.

Likewise, criticism of the abbot's plan holds true for the EU today. French philosopher Rousseau was almost right when he argued that Saint-Pierre's idea could come about only through violent means. It took two world wars for European leaders to abandon their objections to such a scheme. In the EU, things still go forward when things go wrong. A pandemic and the biggest recession in the club's history were needed for Germany and other holdouts to agree to the club issuing common debt.

Economist, "Charlemagne: The EU: 1713 edition", 21 Aug 2021, p. 20.

And then there is the question of how the benefits of globalisation are shared out. Joseph Stiglitz, a Nobel prizewinner, warned that rent-seeking companies' influence over trade rules harms workers and erodes support for trade liberalisation. Raghuram Rajan, head of India's central bank, argued that clumsy government efforts to compensate workers hurt by globalisation contributed to the global financial crisis, by facilitating excessive household borrowing, among other things. David Autor, David Dorn and Gordon Hanson documented how the costs of the US' growing trade with China fell disproportionately on certain cities. And so on [5].

Branko Milanovic of the City University of New York believes such costs perpetuate a cycle of globalisation. He argued that periods of global integration and technological progress generate rising inequality, which inevitably triggers two countervailing forces, one beneficial and one harmful. On the one hand, governments tend to respond to rising inequality by increasing redistribution and investing in education; on the other, inequality leads to political upheaval and war. The first great era of globalisation, which ended in 1914, gave way to a long period of declining inequality, in which harmful countervailing forces played a bigger role than beneficial ones. History might repeat itself, he warned [5].

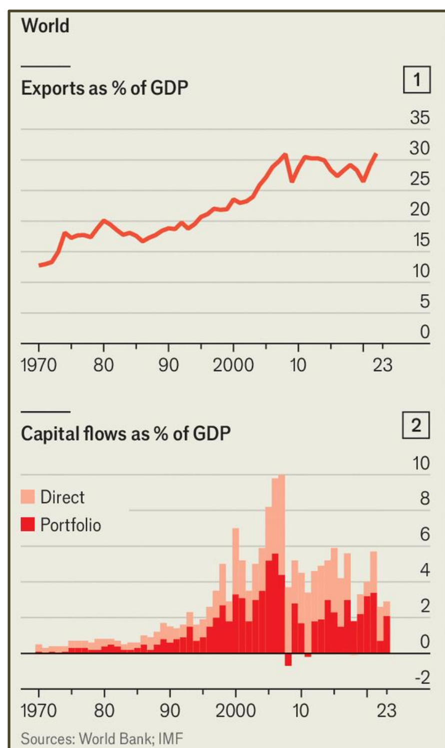
Such warnings do not amount to arguments against globalisation. As many of the economists in question are quick to note, the benefits of openness are massive. It is increasingly clear, however, that supporters of economic integration underestimated the risks both that big slices of society would feel left behind, and that nationalism would continue to provide an alluring alternative. Either error alone might have undercut support for globalisation—and the six decades of relative peace and prosperity it has brought. In combination, they threaten to reverse it [5].

The collapse of the international economic order

The dysfunction at the WTO is emblematic of a world where the institutions and rules intended to foster international trade and investment are falling into abeyance. One of the important features of the WTO was the creation of a binding mechanism to resolve trade disputes. The US has repeatedly sabotaged the process by blocking motions to fill vacancies on dispute panels. The EU intends to impose duties on Chinese electric vehicles. The US expands its sanctions on more then 300 entities, including some in China and Turkey for supporting Russia's armed forces. The proliferation of subsidies and

sanctions is one of the most obvious signs of the unravelling of the "international rules-based order" [6].

Cross border trade and investment have stopped growing (see charts, exports as % of GDP and capital flows as % of GDP). Three big scourges are undermining globalization: the proliferation of punitive economic measures of various sorts, the sudden vogue of industrial policy and the decay of global institutions. Though geopolitical tensions have involved raising tariffs (notably by the US on China and vice versa), three is little sign yet of the sort of tit-for-tat escalation that hobbled the world economy in the 1930s [6].



But the world's governments are imposing trade sanctions more than four times more often as they did in the 1990s, according to the Global Sanctions Database. This includes governments screening foreign investments more carefully and often barring investments in "strategic" companies [6].

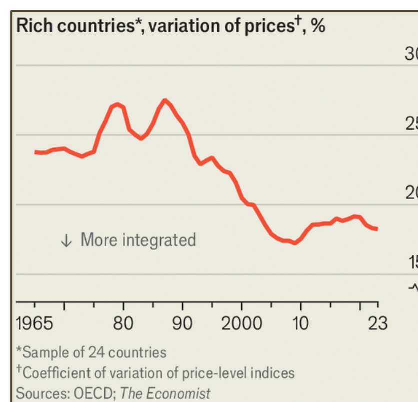
On the fiscal side, the US launched programs that provided subsidies to favoured firms to boost production of clean energy and computer chips. This was followed by well-funded schemes to boost domestic manufacturing elsewhere, e.g., "Made in Europe", "Make in India", and A Future Made in Australia, and Canada's "Made in Canada Plan". Rather than tit-for-tat tariffs the policy response is tit-for-tat subsidies [6].

The third change relates to global institutions, which are a shadow of their former selves. The IMF used to have almost exclusive power to resolve poor countries' debt problems. With the rise of alternative creditors such as China and India, it is finding that job more difficult. Each part of the debt restructuring, including steps that were once formalities, are now subject to protracted negotiations. Sub-Saharan, unable to service their debts are finding it almost impossible to resolving their crises [6].

The IMF has changed from within. The organization, chastened by widespread complaints that its policy prescriptions were too harsh in the 1980s and 1990s, now devotes growing attention to questions of climate change and inequality at the expense of its overarching mission of instilling sound macroeconomic management [6].

But the most moribund multilateral institution is the WTO. Since the collapse of a 14-year-long negotiation in 2015, all talk of expanding free trade or deepening protections for it has fallen by the wayside. Global trade in goods has stagnated; the same problem now afflicts services too. Cross-border investment in in retreat, as well as a share of global GDP. Both long-term (direct) and short-term (portfolio) flows are well below their peaks. Companies are retrenching to avoid geopolitical rift. Investors still willing ot ventrure abroad expect a higher rate of return. In recent years the aap has widened again, pointing to growing global instability (see chart, risk premium on global investment) [6].

Finally, the clearest sign of delobalisation comes from relative prices – for similar goods and services in different places. Before the pandemic average prices in the UK's costliest region were only about 10% higher than in its cheapest, for instance. For years the variation in relative prices around the world was declining, signalling convergence (see chart, variation in prices) [6].



China's rise and challenge to the multilateral system

Since the late 1990s, China's growing international engagement through trade and institutions facilitated its 'peaceful rise' to power. Since 2008, with the global financial crisis (GFC), however, China began to place greater importance on defending its core national interests (e.g., Hong Kong and Taiwan) and asserting its maritime sovereignty claims (i.e., the South and East China Seas). With its economic and military power, Beijing has become more ambitious in articulating its foreign policy goals with the aim of being treated as Washington's equal (Liao, 2016).[12]

The assertiveness can be attributed to several factors. China's global economic and trade stature increased in the early 2000s, but trade frictions arose as evidenced by China

[12] Liao, Nien-Chung Chang, "The sources of China's assertiveness: the system, domestic politics or leadership preferences?, *International Affairs*, vol 92(4), Jul 2016, pp. 817-33. https://www.jstor.org/stable/2475677

being the defendant in 17 WTO trade-dispute cases during 2008-12. The assertiveness could have been a response to the trade complaints from the West preventing the rise of China as a global power. Military might provided China the confidence to express its foreign policy intentions in terms of sovereignty over territorial claims, resulting in confrontations at sea, or using its trade position to apply sanctions, restricting imports of agricultural products from the Philippines or salmon from Norway, or restricting exports of rare earth elements (Liao, 2016).

Some might argue that a more muscular foreign policy was driven by an upsurge of nationalism at home. While a rise in episodes of popular nationalism maybe evident (e.g., in situations of Sino-Japanese tensions), it is more likely that the leadership made use of nationalism in support of its foreign policy (e.g., stirring up the public to achieve a boycott that targets a particular country's exports to China). This gives the government plausible deniability that any change in trade pattern was the result of consumer choices rather than trade measures that violated WTO rules or commitments. China, for example, does not typically formally announce a trade sanction though there might be statistical evidence that supports it (e.g., diplomatic tensions with Norway that led to the government restricting Norwegian salmon imports through SPS-related measures).

The assertiveness could be that the decisionmakers embraced a foreign policy that is commensurate with China's emerging role in the international arena. Xi Jinping's "Major Country Diplomacy" doctrine replaced the earlier Deng Xiaoping era slogan of "keep a low profile and build up power" and has legitimized a more active role for China on the world stage. Increasingly, China is seeking to participate or create a new global order that challenges the existing order created by the US and its allies. The individual-level explanations indicate that China's assertiveness is a function of both enduring elements in the political leadership and new policy-relevant perceptions (Liao, 2016).

During Xi's leadership, criticism of China's state intervention in industrialization and the distortions on international markets brought it in greater conflict with the West. But China's decoupling from the West began even earlier, in 2005 with the launch of its Medium- and Long-Term Plan for Science and Technology Development (2006-2020) in which the government called for increasing domestic content in 11 sectors to 30% by 2020 though import substitution. This was to be implemented through the pursuit of three key objectives: (1) eliminating dependency on foreign countries and corporations for critical technology and products; (2) facilitating the domestic dominance of indigenous firms; and (3) leveraging that dominance into global competitiveness.[13]

The Belt and Road Initiative introduced in 2013 is an infrastructure development program aimed at linking China's economy to the world through investment in rail, roads, ports, energy pipelines, etc. that helped place China at the hub of regional/global supply chains; the creation of the Asian Infrastructure Investment Bank in 2015 was to foster economic development through infrastructure connectivity in Asia; the BRICS New Development Bank established in 2015 is a multilateral financial institutions to rival the IMF and World Bank dominated by the West; Made in China 2025, announced in 2015, is an industrialization strategy with domestic and trade targets; Standards China 2035, announced in 2018, was to set international standards on emerging fields such as biotechnology, renewable energy, information and communications technology (5G), AI, robotics etc. by taking a first mover position.

In addition, in 2015 China created the Cross-Border International Payment Systems (CIPS) in 2015 to offer clearing and settlement services for transactions denominated in renminbi to rival the SWIFT system and substitute the dollar's role in international transactions. In 2016 China completed its goal to increase its role in internationalizing the renminbi by having it included in the IMF's basket of reserve currencies (SDRs).

3. Regional integration vs multilateral liberalization

In classical economic theory, trade through multilateral liberalization boosts prosperity by encouraging nations to focus on their relative strengths. The reality of regional integration deals is messier. Jacob Viner, a Canadian economist, showed more than 60 years ago that customs unions can sometimes divert rather than create trade by inducing consumers to buy from inefficient producers. A tariff on a low-cost Chinese good might encourage intra-EU duty-free trade for a similar good because the tariff makes the Chinese good less competitive [7].

The pros and cons of regional versus multilateral liberalization have been debated for decades. How much trade is diverted and how big the distortions that result from regional liberalization are at the center of the debate [9]. An outline of the positions is presented. For free traders, the objections to regional trade agreements (RTAs) stem from the following criticisms:

[a] RTAs, by definition, discriminate, offering market access on preferential terms to members;
[b] RTAs create a tangle of different, but partially overlapping regulations, such as rules of origin designating which goods qualify for preferential treatment [8] and excludes sensitive sectors which makes life difficult for multinational firms whose supply chains cross multiple borders [9];
[c] Negotiations on RTAs last several years and retard rather than promote liberalisation, because countries delay unilateral liberalisation to store up "bargaining chips" that can be traded off against concessions by prospective partners [8];
[d] RTAs distract political attention from the rules-based multilateral system, particularly when a country's commitment to multilateralism appears to falter [8];
[e] RTAs can expand trade between members, but unless barriers to third-country imports are also removed, the gains come at the expense of non-members (i.e., trade diversion) [8];
[f] Big countries inside an RTA can dictate terms or conditions to smaller economies, which if politically motivated undermine the basis for specialisation [10]; and
[g] RTAs often exclude very poor countries leaving them even more divorced from globalisation or brought in as spokes within a "hub and spoke" system where the rich country is the hub [10].

For supporters, RTAs are positive because:

[a] RTAs free trade between participating countries and lay a foundation for multilateral liberalisation [8];
[b] Negotiations between neighbouring countries achieve results faster (full liberalisation) and deeper (beyond tariffs and toward harmonisation of regulations) than cumbersome world trade rounds [8];

[13] Black, J.S. and A.J. Morrison, "The strategic challenges of decoupling", *Harvard Business Review*, May-June 2021. Hbr.org/2021/05/the-strategic-challenges -of-decoupling.

[c] RTAs help cement domestic economic reforms and market-based economic policies [8];

[d] Successful RTAs work because they involve economies that are geographically close at similar stages of development [8];

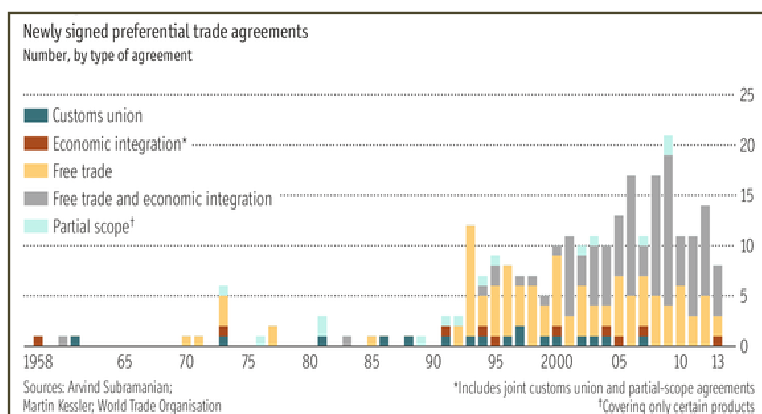
[e] RTAs reduce the number of players on the multilateral stage because the group negotiates as one; and

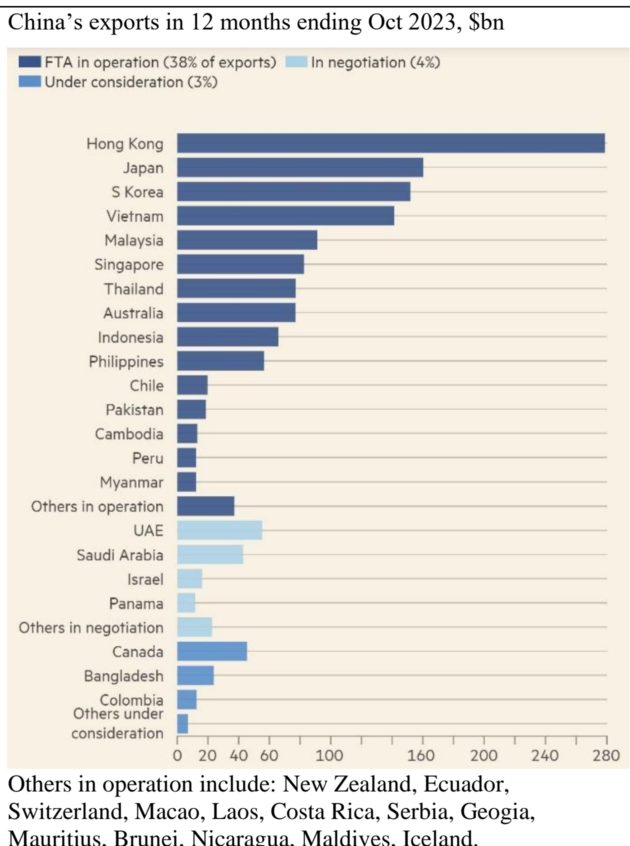
[f] Small-country members of an RTA increase their relative strength in global negotiations by being part of a bigger coalition.

As the WTO Doha round of multilateral trade talks were collapsing in the late 2000s, the worry was that the proliferation of RTAs was to blame. Researchers at the Peterson Institute for International Economics called the rise of ever-larger RTAs an “existential threat” to the multilateral system. As the Doha talks foundered, RTAs appeal grew [9].

Optimists saw both processes proceeding in tandem, albeit unevenly. As European countries began their regional integration in 1957, they continued to cut tariffs as members of the GATT. In the 1990s US president Clinton signed the North American Free-Trade Agreement as the UR-GATT was being completed. China joined the WTO in 2001 as the EU expanded into eastern Europe [9].

Jagdish Bhagwati of Columbia University was a leading voice in arguing that regional deals might be stumbling blocks limiting multilateral deals because less efficient producers would lobby for deals that kept them protected inside. In the 20 years since the WTO, Bhagwati’s warnings bared out. From 1994, there had been more than 10 regional deals a year negotiated, on average, but only one global deal concluded- the underwhelming WTO “Bali package” of 2013 [7]. The number of trade agreements rose from 104 during 1958-2001 to 154 since then to 2014 (see chart, newly signed trade agreements) [9].





Others in operation include: New Zealand, Ecuador, Switzerland, Macao, Laos, Costa Rica, Serbia, Geogia, Mauritius, Brunei, Nicaragua, Maldives, Iceland.

It is hard to know which view is correct because no clear criteria for judging the economic effects of RTAs exist. WTO rules are vague and not applied, not least because most members belong to at least one RTA [8]. The minimal condition on RTAs is that trade restrictions must be eliminated on “substantially all trade” among members and achieved “within a reasonable length of time”. The EU's customs union meets these standards, but the same cannot be said of the Association of Southeast Asian Nations (ASEAN) and China, or of Mercosur, the 4-nation South American bloc that includes two unstable macroeconomies [8].

One point on which the evidence is fairly conclusive is that RTAs are rarely initiated purely for commercial and economic reasons; politics is an important consideration. And, as the World Bank observed, “… the economic consequences, good or bad, are side effects of the political pay-off [8]." The rise of Brazil, Russia, India, and China (the BRICs) present an obstacle to multilateral deals. The rich world increasingly views the BRICs as full-fledged economic competitors whose state capitalism is incompatible with a free and open global economy [9].

With the failure of the Doha round, trade liberalisation proceeded along two different tracks. One track was China’s establishment of a network of bilateral FTAs with its neighbours, which gained impetus with the death of the multilateral talks and China’s rise after the GFC. While the FTAs were numerous, they were shallow (mostly cutting tariffs) and often left out sensitive sectors and subjects (e.g., state trading). Its FTA with the Association of South-East Asian Nations, for example, allowed signatories to classify 400-500 tariff categories as sensitive and thus eligible for slower tariff reduction [9].

A unifying aspect of the domestic industrial policy and the trade and investment policy architecture under construction was a China-centric network of bilateral and regional FTAs. By the end of 2023 this network included 28 countries that accounted for almost 40% of its exports (see chart, Chinese exports) [41]. A further sense of exclusion came when the US excluded China from trade negotiations to join the Trans-Pacific Partnership (TPP), a comprehensive regional trade deal that was being negotiated (from which US president Trump later pulled the US out).

China later negotiated entry to the 15-country Regional Comprehensive Economic Partnership (RCEP), concluded in 2020 and entered into force in 2022, which accounts for one-third of the world’s GDP. And as the West seeks to decouple or de-risk their economies from China, China has reoriented its economy toward Asean countries resulting in an upsurge in investment there. As Asean countries climbed the technology ladder, China’s investment and technological knowhow has become more complementary

to their economic ambitions. This also serves as a means of circumventing US and the EU's trade restrictions through transshipment or near-shoring, i.e., locating production capabilities near consumers.

China has since proposed an FTA with the Gulf Cooperation Council, a union of Arab states, which represents a strategic destination as an export destination for China and a vital source of fossil fuels. Another big prize that China is eyeing is the African continent. The 2018 establishment of the 54-country African Continent FTA (AfCFTA) creates an opportunity for China. It funds the AfCFTA's secretariate and in 2021 China's ministry of commerce signed an agreement to establish an export group at AfCFTA to collaborate on questions on digital trade, customs procedures and intellectual property rights [41]. Through these various efforts, China by 2022, had become the major trading partner of more than 120 countries, including the US and EU.

The other track, preferred by the US and EU, was the pursuit of comprehensive mega-regional deals that would account for a large share of global trade. The US and EU negotiated the Transatlantic Trade and Investment Partnership (TTIP) that was to go "behind the border", focusing on things such as harmonising safety, health and technical standards, currencies, national treatment of foreign investors, protection of intellectual property, services such as telecommunications, and enforcement of labour and environmental protection [9]. However, the comprehensive nature of the agenda and the detailed level of the talks undermined the process. US-EU WTO trade disputes spilled over to the TTIP talks (e.g., food and farm regulations; objections to the US's "buy American" requirements for government procurement). But the controversial 'investor-state dispute settlement mechanism to give foreign investors protection from regulations) derailed those talks too.

In theory, successful conclusion of TPP or TTIP could have encouraged other countries to join, achieving multilateral trade liberalisation by default. In practice it was unlikely. China's and Russia's interventionism and state capitalism are difficult to reconcile with the "behind-the-border" liberalisation the US and EU pursued. Without having any say in the rules, China and Russia would be reluctant to join later [9].

A decline in multilateralism may not make much difference to big countries able to negotiate RTAs on their own terms, but small countries without such leverage could be harder hit. The marginalization of the WTO as a deterrent to protectionism would hurt everyone just as new forms of protectionism arose and which are harder to deal with [9].

As for RTAs serving as a neat system of hubs and spokes, Baldwin argues that the trading system is much messier. Trading blocks in the US, Europe and Asia overlap. Mexico, for example, is a member of NAFTA and party to an FTA with the EU and others. This tangle of interlocking and overlapping deals raises an interesting conceptual question. What if the forces of regionalism and bilateralism were left to play out to their logical conclusion? If every WTO member struck a free-trade deal with every other, the world would have been criss-crossed by 11,026 bilateral deals in 2006. How would this have differed from multilateral liberalisation [10]?

A bilateral or regional deal, by definition, favours one nation's goods over another's. It matters a great deal where an import arrives from. But a product's origins can be difficult to pin down. As a NAFTA member, Mexico can export its overcoats to the US duty-free. But what counts as a Mexican overcoat? What if the zip comes from Taiwan, the lining from India, or the fabric from the UK? [10]

These elaborate rules of origin also differ from agreement to agreement. Mexican garment-makers must contend with one set of regulations for the US, another for the EU. Worse, the rules set off ripple effects throughout the rest of the world trading system: because the US charges duty on Mexican coats made from Indian fabric, Mexico will not import fabric from India. It is as if Mexico had imposed a tariff on India, and a bilateral deal between the pair would do nothing to change that [10].

In the economics literature, the simplest way to assess trade deals is to ask how good they are at lowering barriers like tariffs and subsidies. A 2011 OECD study looked at 55 RTAs, to see whether agricultural duties were lowered.[14] It showed that deals between rich and emerging economies lifted the number of duty-free trade goods from 68% to 87% within ten years. In deals between emerging economies, the share rose from 28% to 92%. (Sectors like sugar and dairy proved resistant even in the best RTAs.) Three out of five deals banned export subsidies. These results suggest that RTAs lower these sorts of barrier [11].

Tariffs are not the only measure of success. Technical and regulatory obstacles and other non-tariff barriers are often more important. When rules do not match, trade cannot take place at any price. The evidence suggests that RTAs do target these non-tariff barriers as well. In a 2009 study of the WTO found that 58 of the 70 RTAs examined tried to align rules or speed accreditation processes [11].[15]

The truest test of an RTA, however, is its trade impact. Calculating this can be hard because lots of things, including growth and exchange rates, affect trade. The US Department of Agriculture (USDA) examined 11 big RTAs in operation between 1975 and 2005, focusing on the impact on foods, a particularly contentious area of trade.[16] The RTAs included the EU and the NAFTA agreement between the US, Canada and Mexico. USDA estimated what trade patterns would have looked like in the absence of the relevant RTA, using factors like distance, common borders, language and macroeconomic variables. By stripping away the trading activity that can be explained by all these factors, the authors isolated the impact of the RTAs [11].

USDA's findings explain why RTAs were popular. The trade of foods inside the region rose in ten of the 11 cases; in the EU and NAFTA the impact was a rise of at least 3% annually on average. In six of the 11 RTAs outside countries gained, too. Trade between NAFTA members and other countries in "commodity" foods like grains, fruit and vegetables rose by 2% a year. It may be that by gearing up for trade (investing in distribution networks, for example), firms within an RTA are able to exploit efficiencies that boost trade more widely [11].

Another way to isolate the impact of a trade deal is to study stockmarket reactions. If RTAs really boosted trade, the prospects for firms in an economy would improve when trade talks were announced or completed. Because

[14] Fulponi, L., M Shearer and J. Almeida, "Regional Trade Agreements – Treatment of Agriculture", OECD Food, Agriculture and Fisheries Working Papers, No. 44, 2011.
[15] Piermartini, R. and M. Budetta, "Mapping of regional rules on technical barriers to trade", in *Regional Rules in the Global Trading System*, e-book, CUP, 2009.

[16] Vollrath, T., J. Gran and C. Hallahan, "Reciprocal Trade Agreements: Impacts on US and Foreign Suppliers in Commodity and Manufactured Food Markets", USDA, ERS, Aug 2012.

investors look ahead when picking stocks, prices should rise as soon as news breaks. To test the idea, Christoph Moser of the KOF Swiss Economic Institute, a think-tank, and Andrew Rose of the University of California, Berkeley, collected data on 1,001 announcements relating to 122 RTAs between 1988 and 2009.[17] First, they establish the relationship between national and foreign stockmarkets, using this to strip out any changes in a country's stocks that were due to global shifts rather than local news. They then study stocks over a window starting the day before each trade announcement and lasting for ten days after it. The findings again support RTAs: they tend to boost markets, especially when member countries are poorer and already trade a lot (so there is more to gain) [11].

Comprehensive RTAs: TTIP, TPP and RCEP

Comprehensive RTA deals do not focus on tariffs, they focus on deeper regulatory issues such as rules governing capital flows and competition policy [7]. TTIP focused big sticking points such as bringing "coherence" to transatlantic regulation of cars, chemicals [13]. In the auto industry, US companies hoped they would no longer have to engineer separate seat belts, defrosters and myriad other components for each market, according to Ford's vice-president for intergovernmental affairs. "When you eliminate regulatory differences and tariffs, you combine the size of the market [and] you create scale. That makes it attractive to continue to invest in the automobile industry in the US and Europe," he said [13].

Non-tariff barriers (NTBs) were far more burdensome than tariffs. Chemical exporters to the US faced a tariff rate of 1.2%, but an NTB equivalent of a 19.1% duty. European NTBs added what amounted to an additional 25.5% duty on top of the 8% tariff levied on US car imports. Separate drug-approval processes in the EU and US added to the burden of operating across the Atlantic. Different consumer-product safety standards or inspection procedures have similar effects. Common standards, or mutual recognition of each other's regulatory processes, could deliver an economic boost to what was a US-EU combined annual output of around $30 trillion, almost half the world total [12].

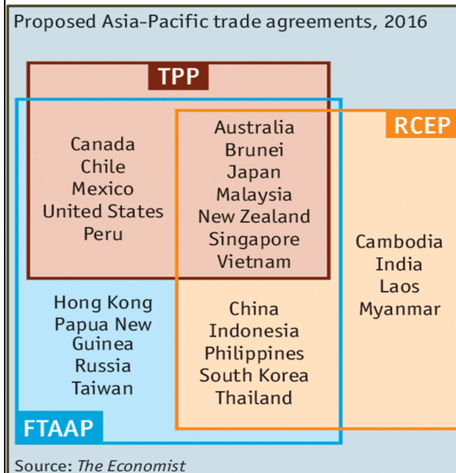
The "investor-state dispute settlement" (ISDS), a term used in trade and investment treaties to protect foreign investors from rogue actions by governments, usually in the developing world, faced increasingly vocal opposition articulated on social media and by member states. The European Commission was forced to suspend negotiations with the US over the investment chapter [14].

For Washington, the TPP had several overlapping aims. One was to update the WTO's rules, unchanged since 1994. Another, part of the broader "pivot" to Asia, was to avoid being marginalised from a region in which China held increasing sway and in which rival trade pacts were gathering pace [15]. Based on size alone, the TPP would have been the largest ever RTA. It encompassed 12 Pacific countries, including the US, Japan and Canada (see chart, overlapping trade agreements) [16]. Together, they accounted for two-fifths of the world economy. But what made it all the more significant was its strategic intent.

The stated aim of the TPP was to deepen trade by addressing issues such as government procurement, enforcement of stricter intellectual property protection and the conduct of state-owned enterprises. TPP sought to regulated SOEs so that they did not enjoy unfair access to licenses, contracts or state finance. This was an assault of the sort of state capitalism in countries such as China. It called for an ISDS mechanism. It was also meant to update trade agreements by dealing with post-WTO developments, including e-commerce and cloud computing, as well as addressing labour and environmental standards [15].

The absence of Chinese membership in TPP made little economic sense. Studies indicated that including China, the world's biggest exporter, would have substantially expanded the benefits of TPP. But the US wanted to show that it could set Asia's economic agenda. China might eventually have been invited to join TPP, but only after the US had written "the rules of the road", as its negotiators liked to say [16].

With the US's withdrawal from TPP, the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) was stitched together by the remaining participants incorporating most of what the original TPP included, dropping mainly strictures insisted on by the US (e.g., reducing copyright protection from 70 to 50 years, and special protections for biologics, a drug subcategory). China is not a member mostly due to CPTPP's 'competitive neutrality approach' to state-owned enterprises (SOEs). This means that SOEs and private businesses must compete on a level playing field, something that is contrary to the dominant role SOEs play in China's economy.



Instead, China joined the Regional Comprehensive Economic Partnership (RCEP) which included 15 Aisa and Pacific countries. In Nov 2020 it became the world's newest and biggest trade deal, but it was not the deepest as it eliminated fewer tariffs than normal, and some only after two decades. Its coverage of services was thin as was that of agricultural goods [17].

RCEP began as a tidying-up exercise, joining one overarching compact of various trade agreements in place between the Association of South-East Asian Nations (ASEAN) and Australia, China, Japan, New Zealand and South Korea. That limited how much new trade would be affected. Of the $2.3trn in goods flowing between signatories in 2019, 83% passed between those that already had a trade deal [17].

Some trade would be affected. China had no existing deal with Japan or South Korea. But India did not sign up. Perhaps the biggest benefit to come from RCEP would be from the rules of origin, which set out the regional content a product must have to enjoy the lower

[17] Moser C. and A. Rose, "Who Benefits from Regional Trade Agreements? The View from the Stock Market", 2011.

tariffs. Under the previous overlap of agreements, a cup of coffee exported by a member could have faced three different sets of rules depending on the destination. RCEP offers firms one set of rules. Rules on content are relatively liberal: many products need just 40% of their value to be added within the region to take advantage of lower tariffs [17].

The deal served China's interests. It had previously warily watched its neighbours sign up to the TTP, which would have reined in state-owned firms and included rules on labour and environmental standards. RECP strengthened China-centric supply chains – with none of those constraints [17].

Global supply chains
Apart from China's economic rise and assertive foreign policy, there have been other shocks to the global economy since 2000 that have affected global supply chains (e.g., the tsunami that created the Fukushima nuclear reactor accident in Japan in 2011; Covid-19 lockdowns; the blocking of the Suez Canal by a container ship, the Ever Given, in 2021; attacks on ships in the Red Sea since the invasion of the Gaza Strip in 2023; Russia's invasion of Ukraine in 2022, etc.).

The business lesson to these shocks is to build bigger buffers, both of raw materials needed to produce whatever firms make and of its final product. In practice, this simple solution comes at a big cost. And that cost is rising. Higher interest rates make short-term loans used for day-to-day operations, including holding inventory and paying suppliers, dearer. A shortage of warehouse space means higher rents to stash the extra stocks. Each dollar tied up in inventory is a dollar not invested in pursuit of future profits [42].

These shocks have shifted the balance of power across the world's supply chains. For all the talk of efficiency in logistics through "just in time" delivery the shift is now toward "just in case". As supply chains became more efficient in the 1990s, thanks to globalisation, retailers drove a harder bargain with suppliers. Being closer to the consumer, they had a better idea of what shoppers wanted and when they wanted it. Limited shelf space allowed shop owners to demand that producers hold more inventory themselves in exchange for having their products displayed on those scarce shelves. Manufacturers' hopes that e-commerce would strengthen their hand by giving them direct access to buyers were dashed [42].

The new challenge is for firms to deliver "on time in full. This means suppliers must either use forecasts to make products in advance, and hope that they made the right amount, or the alternative is to build spare production capacity, which allows them to react to changes quickly without having to hold more inventories [42].

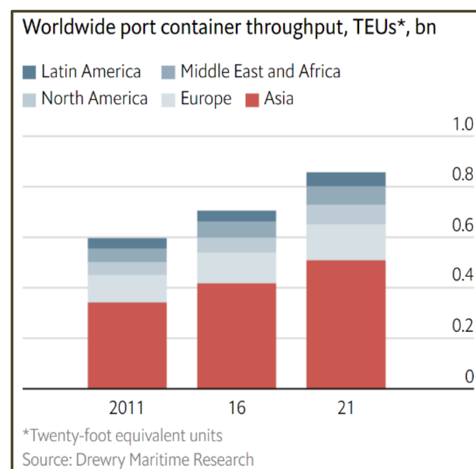
The world's logistics are moving more into high tech and into Asia. The shift in the future of trade is happening on two fronts. First is that port operators the world over are deploying clever technologies to meet the demand for their services in the face of obstacles to the development of new port facilities, from a lack of space to environmental concerns. The expansion of seaports is becoming tougher. Space in the right locations is scarce. Big port expansions in Greece and Mexico, for example, were blocked by courts for failing to provide the right assessment of its environmental impact or on environmental grounds [43].

One solution is to make existing logistics networks more efficient rather than merely larger. But streamlining supply chains can only go so far. At some point, new capacity is needed. One way to achieve it is by reclaiming land from the sea as is happening in Singapore and the Netherlands [43].

But many ports are too deep for land reclamation to be viable. Some are therefore deciding to build upwards. In conventional set-ups, it is impractical to stack more the six containers on top of each other, and even then tall stacks require boxes to be shuffled around constantly to get hold of the right one. Shuffling can take more time than moving containers around the port and onto vessels. New storage systems are becoming available where containers sit on an individual rack, stacked 11 high, where automated cranes can pluck them out individually [43].

Where space is more limited and it is not possible to build up or out, the other option is to build elsewhere. This explains the rising popularity of inland "dry ports", where goods are put into containers ahead of time, ready to be loaded onto ships as they arrive at the pier without needing to be stored for days at the port itself. This lightens road congestion at the terminals. Dry port development in Asia points to the second force reshaping the ports business. The centre of its gravity is eastwards. For decades Asian trade has tended to be one way. Containers loaded with goods manufactured by the continent's cheap labour sailed to advanced economies and came back largely empty [43].

In the late 1990s more than 70% of Asian exports by value went to other parts of the world. In the 2020s, nearly 60% of Asia's exports flow within the region, reflecting changes in trade flow and more complex supply chains (see chart, worldwide port container throughput). Asia economies have become big markets. The regions five largest economies – Indonesia, Malaysia, Singapore, the Philippines, and Thailand – are expected to be the fastest growing bloc in the world by trade volume between 2022-27 [43].



A boom in investment in warehouses for storage and hubs for distribution and fulfillment in the region is already under way. When seaborne trade boomed in the last century, investments in logistics reflected shifts in the global patterns of production and consumption. They are doing so again. This time the future looks leaner, smarter, and more eastern [43].

<u>Preferential treatment between the global north and south</u>
As China's influence in Africa has increased, the US and EU have taken a rethink on their trade relations with the continent. Trade with Africa has long been viewed as both a boost to development and a spur to good governance. It is increasingly seen as a contest between great powers [18].

In the past the granted concessions, such as lower tariffs on African exports, without requiring African countries to reciprocate. This approach is paternalistic and gave Africans little say. Since 2000 US policy was built around

the African Growth and Opportunity Act (AGOA), which grants duty-free access to almost 7000 products exported from around 40 eligible countries. It was a law passed by Congress, not a treaty negotiated between governments, so African countries have no control over the eligibility criteria. That crates friction. Rwanda, for example, was partially suspended in 2018 because its ban on imported second-hand clothes, intended to boost local production, irked the US firms that exported them. In 2024, AGOA was extended to 2041 [19].

In the eyes of US officials, it was about more than just trade. To qualify countries must respect human rights, uphold labour statndards, promote a market-based economy and eliminate barriers ot US investment, among other criteria. But can a system of trade preferences also be a tool of foreign policy, without stifling trade's potential for development [18]?

The US only buys about 6% of sub-Saharan Africa's goods exports; China and the EU each purchase three times as much. Only in a handful of countries does AGOA really make a difference, especially in clothing. Ethiopia, ineligible over abuses by soldiers and rebels during a civil war, lost its duty-free access which made Ethiopian exports uncompetitive. South Africa, the biggest exporter under AGOA, cannot take its trade access for granted. The US, alarmed by its close military ties to Russia questioned whether the country should remain eligible for AGOA. Because countries have little recourse when they are removed from the list of eligible countries, the US s accused of bullying. But US officials add that human rights and democratic principles do create the right environment to deepen trade and investment [18].

European countries once gave preferential access to exports from their former colonies in Arica, the Caribbean and the Pacific. That clashed with the WTO rules on discriminatory behavior. So, in 2000 the EU started touting reciprocal deals called "economic partnership agreements", negotiated with regional blocs. A southern African pact with the EU came in to force in 2016. But countries such as Nigeria (in the west African bloc) and Tanzania (in the east) have refused to sign deals in their respective regions. They worry, with some justification, that dropping tariffs would expose nascent industries to a flood of European competition [19].

The incentive to cut a deal with the EU undermines intra-African regional trade. If Kenya agrees to a deal with the EU and Tanzania does not, then it undermines the east African bloc union. Then in 2021 37 countries started the gradual process of trading under the African Continental Free Trade Area (AfCFTA). The idea is to kickstart Africa's stalled industrialization by selling manufactured goods to each other, rather than raw materials to distant continents [19].

4. Economic Integration: Creating the EU

Writing in 1948, George Kennan, a US diplomat, summed up the view in Washington: if Germany was restored without European integration, there would be a German attempt to dominate it. If Germany was not restored, there would be domination by Russia. A strong prosperous Europe that settled the German question was what was required and the US worked to that end [20].

The Coal and Steel Community (ECSC) of 1952 was a modest first step toward economic integration. It was a trade treaty with a novel twist. It created a High Authority, which stood above the six governments to administer its provisions. All the participants were equal, and the pact was open to new members. France's prosperity required West German raw materials. France had depended on German coal since the 1890s, and by the 1930s had become the world's largest coal importer. At the same time Germany had to be kept from renewed aggression [20].

After the war, Germany was divided into four zones: US, UK, French and Soviet zones. In the Soviet zone factories were dismantled or their products shipped east, as war reparations. In the Frech zone products were sent ot France at cut-rate prices. Industrial production was capped for fear of reviving Germany's military might, and commerce between the zones was restricted. Stalin blocked all attempts by the US and UK to liberalise trade unless they would agree to crate a unified German government – which he planned to subvert and control, as he had throughout eastern Europe [21].

US president Truman turned to George Marshall, a former US general, to devise a plan for post-war Germany. Marshall wanted to unify and liberalise German commerce, but hesitated at the implications, knowing that Stalin would reject the move and could provoke him to war [21].

Marshall's plan for a European Recovery Programme envisioned a huge injection of US aid. US dollars would solve Europe's shortage of foreign exchange, allowing its industries to trade their way to prosperity. It would be a prize to induce European governments to relax the trade restrictions paralysing their economies. Marshall invited the Soviets to join, knowing that Stalin would likely sabotage the programme, but the gamble that the conditions placed on the grants (open trade integrating all of Europe, rather than quota-based trade oriented towards Moscow) would make Stalin reject the plan. He did just that and told his new satellites in eastern Europe to stay out too [21].

As the aid began to flow in 1948, European growth took off. Industrial output in Marshall Plan countries increased by more than 60% between 1947 and 1952; in West Germany it more than tripled, and annual GDP growth in some years hit double digit growth. The plan had tremendous power and ensured that funds were spent on genuine investments. In some countries much of the aid was used to back national champion firms. In other cases, it was used to import commodities rather than industrial machinery or used to pay off war debt. There is a consensus among historians that there was a lot of rent capture [21].

On 25 March 1957 ministers of six European nations gathered in the Rome to sign the European Economic Community's (EEC) founding Treaty of Rome. In 2017, 60 years later, 27 leaders of the EU returned to Rome to renew their vows. Britain absence at the creation, left an empty chair at the anniversary celebrations, preparing for its Brexit [17].

The defining characteristic of the EU is the 1957 Treaty of Rome which established the EEC. Article three says: "The activities of the Community shall include . . . the elimination, as between Member States, of customs duties and quantitative restrictions on the import and export of goods . . .; the abolition, as between Member States, of obstacles to freedom of movement for persons, services and capital [32]."

Jaques Delors, the EC president from 1985 to 1995, helped create the single market, then laid the grounds for the euro and passport-free travel among other federalisig milestones. To bring down barriers between countries, Mr. Delors cajoled national governments into giving up veto powers, particularly on economic matters. He convincingly explained how a little loss of sovereignty could result in a lot of economic gain [23].

The essence of the EU are the four freedoms: movement of goods, services, capital and people. The first freedom, relating to goods, was clearly the priority when the treaty was signed. Subsequent EU treaties strengthened the other freedoms though not all are equally developed. The free movement of goods is the most advanced while the free movement of services is the least developed of the four. Freedom of movement for citizens is fundamental [32].

Theresa May, the UK's PM initiating the Brexit process, remarked of Europeans being "citizens of nowhere". This explained the Brexit mentality because in the EU one is always a citizen of one's home state and of the union itself, no matter where one happened to live. This is the essence of Europeanness. There is a political and economic logic behind the unity of the four freedoms. They constitute the ultimate trade-off in EU politics. The EU's strength is to mediate between conflicting interests – large countries versus small, producers versus consumers, employers versus employees. While the roots of the old EEC were economic, as the name implied, it required a political and social component to keep it going. As a club of producers, the EU would not have survived for long [32].

The inability to understand, or the refusal to accept, the four freedoms constitutes the deep reason behind Brexit. UK PM Cameron famously misjudged it. He tried and failed to get the EU to agree to a relaxation of the principle of free movement. Some still argued that the UK could remain a member of the single market while imposing restrictions on free movement. But the logic of the four freedoms is not based on economic but political reasoning [32].

Fracture and fragmentation have drained faith in solidarity. Running on a north-south axis there are divisions between stronger and weaker eurozone members; west-east the rupture is between the EU's founding democracies and the nationalist bent of new members in the post-communist east. The EU of 2017 faces an entirely different environment. It was not so easy to make the case for supranational co-operation and shared sovereignty when the political currents run in favour of a renationalising world. The financial crash and subsequent economic recession sapped public confidence in globalisation. Rising migration heaped cultural location on to economic hardship. A revanchist Russia challenged the fundamental principles of postwar European order. The US, long the cheerleader for European integration, turned against it in the person of US President Trump when applauding Brexit [32]. The challenge facing all multilateral institutions is a greater symptom of the tide moving against globalisation.

The European Court of Justice (ECJ) has acted as a quiet but powerful motor of European integration for most of its existence. The four freedoms associated with the EU owe as much to its judges as to its politicians. Once it ruled solely on dry economic issues, but its responsibilities have expanded as deeper integration was pursued. Where European treaties are vaue, it is the ECJ's job to bring clarity. Such a mandate gives the EU's judges scope to roam. When negotiations involve 27 countries, hundreds of MEPs and legions of officials, the result is often unclear. Better to have a blurred text than no text at all. It is the ECJ that is left with finetuning the constitutional details of the meaning of that text. For example, it was a case in 1964 over an electricity bill worth 1,925 lire – about €22 in 2020 money – in which the ECJ determined that EU law trumped national law [24].

Managing the small-large country power dynamics

Of course, the big beasts of the EU, notably France and Germany, hold plenty of sway in dealmaking. But a club which is happy to negotiate through the night to reach consensus is one that ends up giving a disproportionate amount of power to the likes of Ireland, Luxembourg or the Baltics. For the tiddlers, though, the era of small-state privilege may be drawing to an end. There are three elements that give Europe's small states their unexpected heft. One is their sheer number: 15 members have populations of under 10m, jointly making up 14% of the bloc's 448m. At Brussels summits, the German leader representing 84m Germans must jostle with three Baltic leaders whose combined population is 6m. Second is that the EU is more an intergovernmental confederation than a fully formed union. Many decisions must be agreed unanimously, notably on tax or foreign affairs which gives all national governments veto power, magnifying the power of the "smalls". However small countries know this privilege is unearned and vetoes from small countries are rare (with the exception of Hungary more recently). The departure of the UK through Brexit harmed the interest of the smalls because a more intergovernmental union of the sort favoured by Britain was precisely the sort that preserved their interests. Finally, small states manage to nab plenty of the top jobs, often as compromise candidates [25].

Recent events are causing changes. A shift in economic policies has swung the pendulum in favour of the bigs. For decades the EU machine in Brussels was a champion of free trade, and enforced rules that forbade national governments from subsidizing their favoured companies This suited small countries as well: their instincts are or for more open economies, given how small their domestic markets are. Big countries have large firms that can benefit from protection from Chinese or US rivals. Following the Covid-19 pandemic and the war in Ukraine, the trend has been for state-aid rules to be relaxed, allowing billions to be spent in the name of "strategic autonomy". The small states still have a card to play. They still have a veto in approving any new EU arrangements (especially with a new round of enlargement that will require how an EU-36 would be run). This will be an important chance to make sure that any rule changes do not hit them too hard [25].

The "Brussels effect" refers to the EU's ability to unilaterally globalize its regulations by shaping rules and technological standards outside the borders of the EU through market mechanisms. With its size and economic heft, the EU has become the world's chief regulator.

On issues such as product safety, financial regulation, antitrust, transport, telecommunications and myriad other policy areas, the EU has left an indelible mark on nations outside the bloc.

Sometimes voluntarily, sometimes through gritted teeth and sometimes without even knowing, countries around the world are importing the EU's rules. It is a trend that has sparked concerns among foreign business leaders and that irritates US policymakers. Whether they like it or not, rice farmers in India, mobile phone users in Bahrain, makers of cigarette lighters in China, US chemicals producers, accountants in Japan and software companies in California have all found that their commercial lives are shaped by decisions taken in the EU capital [26].

"Brussels has become the global pacesetter for regulation," says David Vogel, a professor of business and public policy at the University of California, Berkeley. Prof Vogel points out that even the US – the world's most powerful nation and the biggest economy – is finding it increasingly hard to escape the clutches of the Brussels regulatory machine: "The relative impact of EU regulation on US public policy and US business has been dramatically enhanced. Even if a country does not adopt [EU] standards, the firms that export to the EU do. Since most firms export to the EU, they adopt the EU's more stringent standards" [26].

The EU's emergence as a global rulemaker has been driven by a number of factors, but none more important than the sheer size and regulatory sophistication of the EU's home market. The rapid expansion of the economic bloc to 27 nations with a total of more than 480m largely affluent consumers turned the EU into the world's biggest and most lucrative import market. At the same time, the drive to create a borderless pan-European market for goods, services, capital and labour triggered a hugely ambitious programme of regulatory and legislative convergence among national regimes [26].

Transatlantic philosophical differences might explain why the EU is usurping the US's role as the source of global standards. The US model turns on cost-benefit analysis, with regulators weighing the effects of new rules on jobs and growth, as well as testing the significance of any risks. Companies enjoy a presumption of innocence for their products: if this proves mistaken, punishment is provided by the market (and a barrage of lawsuits). The European model rests more on the "precautionary principle", which underpins most environmental and health directives. This calls for pre-emptive action if scientists spot a credible hazard, even before the level of risk can be measured. Such a principle sparks transatlantic disputes: over genetically modified organisms or climate change [27].

In Europe corporate innocence is not assumed. Indeed, a vast slab of EU laws evaluating the safety of tens of thousands of chemicals, known as REACH, reverses the burden of proof, asking industry to demonstrate that substances are harmless. Some Eurocrats suggest that the philosophical gap reflects the US constitutional tradition that everything is allowed unless it is forbidden, against the Napoleonic tradition codifying what the state allows and banning everything else [27].

Yet the more proscriptive European vision may better suit consumer and industry demands for certainty. If you manufacture globally, it is simpler to be bound by the toughest regulatory system in your supply chain. Self-regulation is also a harder sell when it comes to global trade, which involves trusting a long line of unknown participants from far-flung [27].

This exercise of [harmonizing regulations] gives the EU a body of law running to almost 95,000 pages – a set of rules and regulations that covers virtually all aspects of economic life and that is constantly expanded and updated. Compared with other jurisdictions, the EU's rules tend to be stricter, especially where product safety, consumer protection and environmental and health requirements are concerned. Companies that produce their goods to the EU's standards can therefore assume that their products can be marketed everywhere else as well [26].

As Henrik Selin and Stacy Van Deveer, two US-based academics, point out: "The EU is increasingly replacing the US as the de facto setter of global product standards and the centre of much global regulatory standard setting is shifting from Washington DC to Brussels" [26].

For Japan the importing of foreign laws is nothing unusual, says Franz Waldenberger, an economics professor at the Japan Centre of Munich's Ludwig-Maximilians University. "Ever since Japan opened itself to the west, there has been a long tradition of turning to western laws for inspiration. There is barely a Japanese law that has not taken a western law as a model. The key factor is having the highest standard. Global companies develop products for the global market and that means they have to follow the highest standard – which today tends to be European" [26].

Mark Schapiro's resereach[18] began with him finding that firms resisted the notion that the US market would follow EU standards for items like cosmetics, insisting that their US products were already safe. As the book neared completion, firm after firm gave in and began applying EU standards worldwide, as third countries copied EU rules on things like suspected carcinogens in lipstick. Even China leaned to the EU approach [27].

The book records similar US reactions to the spread of EU directives insisting that cars must be recycled, or banning toxins such as lead and mercury from electrical gadgets. Obey EU rules or watch your markets "evaporate", says a computer industry lobbyist. "We've been hit by a tsunami," says a big wheel from General Motors. US multinationals that spend money adjusting to EU rules may lose their taste for lighter domestic regulations that may serve only to offer a competitive advantage to rivals that do not export. Mr Schapiro is a campaigner for tougher regulation of US business. He predicted that US industry would want stricter standards to create a level playing-field at home [27].

A second way in which the EU has stamped its authority on other jurisdictions is through influencing the decisions of international standard-setting organisations and global regulatory bodies such as the International Maritime Organisation or UNECE, the Geneva-based branch of the United Nations that deals with economic co-operation [26].

Carmakers around the world – with the exception of the US – follow UNECE's technical standards. These are based on norms drafted and agreed in Brussels, so European automotive groups such as Volkswagen or Renault can export their vehicles to Japan, India or China without having to remodel their cars or seek the approval of foreign safety authorities. Their US rivals, meanwhile, are often forced to invest in additional tests and costly tweaks to their models before they can be shipped abroad [26].

Perhaps the most famous example of an EU standard conquering the world is in the market for mobile phones. The GSM standard was enshrined in a 1987 EU law, then rapidly spread across the economic bloc and formed the platform used by more than 2bn mobile phone customers around the world (the US was largely an exception). Thanks to EU's first-mover advantage, companies such as Finland's Nokia, Ericsson of Sweden and Britain's Vodafone emerged as some of the biggest players in a vast and expanding market [26].

The EU's emergence as a global rulemaker has not been without controversy. Washington and Brussels have clashed at the WTO over the EU's strict limits on genetically modified crops, not least because the US biotechnology industry fears that EU's aversion to GM foods will spread. Even if Brazilian or Indian farmers do not share the EU's hostility to the new varieties, they think twice before planting GM rice or maize: falling foul of the EU's strict GM laws, can mean being shut out from the world's most lucrative market [26].

Companies outside the bloc, meanwhile, are waking up to challenges posed by the EU's growing clout. Groups such as Microsoft – which was fined close to €780m ($1.1bn, £528m) by the EC for breaking EU antitrust laws – now employ large teams of lawyers and lobbyists to attempt to ensure that their views are heard in the Brussels corridors of power. Others use their national governments or trade

[18] Shapiro, M. *Exposed: Toxic Chemistry of Everyday Products and What's at Stake for American Power*. Chelsea: Green Publishing, 2007.

associations to seek to influence the outcome of the EU regulatory process. They all know that Brussels is slowly but steadily emerging as the regulatory capital of the world. As much as some loathe it, it is a trend that business leaders and policymakers from Tokyo to Washington feel they cannot afford to ignore [26].

In the tech world, Europe is both small player and big player. The continent has lots of cutting-edge technology but hardly any significant digital platforms. It accounts for less than 4% of the market capitalisation of the world's 70 largest platforms (the US boasts 73% ad China 18%). At the same time, the EU is a huge market, with a population of more than 500m, which no tech titan can ignore. It contributes to about a quarter of the revenues of Facebook and Google. A book written by Anu Bradford of Columbia Law School (*The Brussels Effect*, 2020) argued that this combination gives rise to the Brussels effect. Digital services, for example, are indivisible which makes it too expensive for big tech firms to offer substantially different services outside the EU. As a result, most firms have adopted the General Data Protection Regulation, Europe's strict privacy law, as a global standard [28].

The EC appears to what to repeat the trick in other areas. A white paper on artificial intelligence is a grab bag of measures to foster the use of AI in Europe and to limit its perceived dangers. The EU commissioned a "digital strategy" to promote the use of data, the most important input for AI applications. The idea was to create a "single European data space" in which digital information flows freely and securely. This was proposed in a draft of "Digital Services Act" [28].

Labour mobility a fundamental component of integration

The European project was meant above all to be a process of economic integration (intended, in the words of the Schuman declaration in 1950, "to make war [within Europe] not merely unthinkable but materially impossible"). Dissatisfaction with the EU often boils down to the suspicion that its original mission of economic integration has morphed into a misguided push for political union. Which one of these agendas does the free movement of people advance [29]?

Some economists argue that though the free movement of people is essential to Europe's political project, it is not necessary to accomplish the sort of deep economic integration that reduces wage inequality across countries. In the simplest trade models, such as the one developed by Bertil Ohlin and Eli Heckscher in the early 20th century, this is certainly true. Such models suppose that countries' comparative advantages are determined by their relative abundance of resources. Countries with lots of low-wage labour, for instance, tend to export goods that use a lot of low-wage labour in production. Building on this theory, Paul Samuelson pointed out that opening trade between two countries ought to cause the price of traded goods to equalise across markets. That, in turn, should cause the return to the factors used in production, including the wages paid to labour, to converge, even if those factors could not move across borders. Free trade alone is enough to generate convergence [29].

Yet this is an impoverished view of integration. New models of trade do not imply that close economic integration should cause incomes to converge. Firms and places are often subject to economies of scale: they become more productive as they grow larger. As freer trade expands the size of the market, producers with initial size advantages outcompete rivals. In an integrated market one country might specialise in a high-wage industry with increasing returns to scale (like skilled manufacturing or finance) and others in areas in which wages are lower. In fact, the conditions needed to bring about convergence go well beyond what free trade alone is likely to achieve. For incomes to equalise, different countries must use similar sorts of technology, for instance. Yet achieving comparable levels of technological capability across countries may require more than just free trade: supranational standards, for example, and the flow of knowledge in other ways—such as through the movement of individuals [29].

In 1961, in his book, "The Theory of Economic Integration", Bela Balassa, a Hungarian economist, offered a more satisfying definition of his subject. He suggested it was an "absence of various forms of discrimination" between economic units in different countries. A free-trade agreement, he noted, is a step towards economic integration, but just a step. Harmonising external tariffs is a further leap, and setting common internal standards and regulations is yet another move along the continuum [29].

Using discrimination as a metric strongly implies that limits on movement of labour inhibit economic integration. Such limits directly prevent competition among providers of in-person services from different countries; Polish doctors cannot easily treat British patients from surgeries in Poland. And constraints on labour mobility undermine the formation of social ties across borders: relationships that play an important economic role. A paper published in 2013 examined the fortunes of different regions in West Germany after the fall of the Berlin Wall, and found that where households maintained close social ties to East Germany, the fall of the wall led to more cross-border investment and a higher return to entrepreneurial activity. It is costly to gain valuable economic information about unfamiliar places. Social ties reduce that cost. Borders, which frustrate the creation of those ties, necessarily mean that firms on one side of the line will be at a disadvantage when investing or operating on the other [29].

Indeed, it may be the very logic of economic integration, with its attendant erosion of discriminatory barriers, that truly irks Eurosceptics. Cultural differences of all sorts, from language barriers to tastes and habits, make it harder for people and firms from one country to do business in others: for French-language newspapers to sell in Frankfurt or for Spaniards to network with Czechs. Complete economic integration implies the smoothing away of these differences, and the formation of something closer to a European identity. Pro-Brexit voters were not wrong to fear that European economic integration threatened the primacy of their unique culture, or to worry that in the big, cosmopolitan cities—where people from many countries mix to build ties and share knowledge—a broader, post-national identity is being forged [29].

The goal of ending war within Europe through deep economic integration is not so different from that of ending war by eliminating the pesky nationalism of individual states. As enthusiasts and critics of the European project should know, closer economic, political and cultural ties are indivisible. Putting up barriers to labour mobility is not just a political choice. It implies a halt to—and perhaps even the reversal of—economic integration [29].

Enlargement

Russia's invasion of Ukraine has prompted a slew of geopolitical realignments. Europe is now actively considering bringing new countries into the bloc for the first time in more tan a decade, what is likely to be the last big enlargement. The road to EU membership for up to nine new countries – including Serbia, Albania and four others in the Western Balkans, as well as Ukraine, Moldova and possible Georgia – will be tortuous. Joining the world's largest economic bloc will require deep reforms 8the sort so far shunned by them) [30].

From the EU's perspective, morphing from a club of 27 today to perhaps 36 tomorrow will be possible only if its inner workings are revisited. The target date of 2030 is being considered, but it ambitious [30]. However, there are wo obstacles, the applicants and their readiness. Bosnia-Herzegovina, Montenegro and the others are not particularly well run. They suffer from a mix of autocracy, corruption and weak rule of law. Moldova, Georgia and Ukraine all have Russian troops on their territory. Serbia and Kosovo and Bosnia are still riven by ethnic tensions [30].

The next concern is readiness. The buzzword in Brussels is "absorption capacity", so that a union of 27 does not collapse under its own weight when it swells to 36. Not only would d enlargement alter the shape of the EU but it would have to modify its inner workings too. The EU budget only has about 1.2% of its combined members' GDP over a seven-year budget cycle. That is both not very much and yet enough to create winners and losers. The CAP hoovers up a third of the bloc's budget and "cohesion " and regional-aid funds flowing to poorer countries and regions. Under current rules, such funds would be soaked up by the newcomers. There are already 18 members that now receive more money than they put in, including all of central Europe. This should have to be overhauled [30].

The other challenge is to adjust the EU's basic rules over how decision are made. In a union of 36, some (smaller) countries might have to give up the right to a commissioner. A more contentious but necessary change would be for more decisions to be made by qualified majority voting, whereby big countries carry more weight than small ones. Important swathes of policymaking – including foreign policy, economic sanctions, policing matters and taxation – must be agreed unanimously by all 27 members. France and Germany are keen for more areas to be impervious to veto by one or two countries. But many small countries feel that such vetoes preserve their countries. The topic of when and how enlargement will happen will dominate the EU political discourse for years. The final destination remains unclear, but the fact that the prospect of a bigger EU is at least a mark of how much the war in Ukraine has reverberated far beyond the front lines [30].

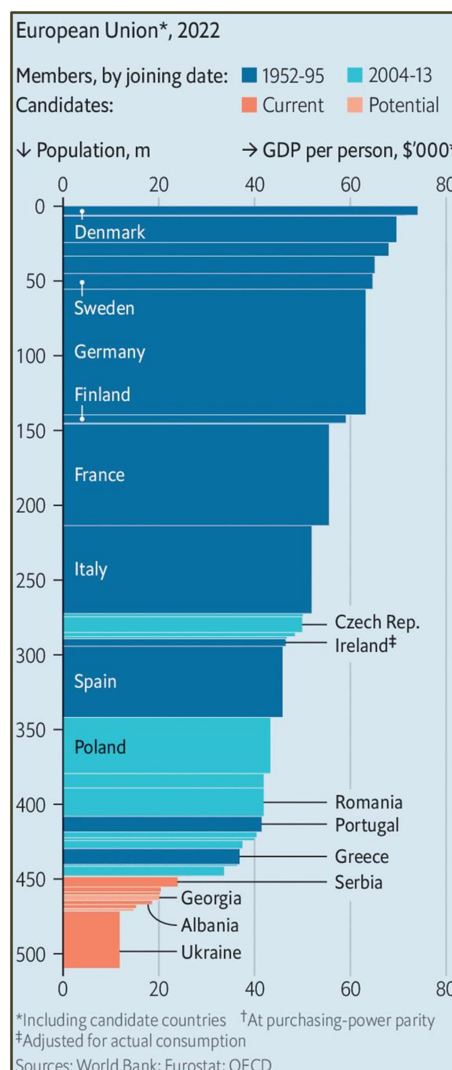
De-integration: The Case of Brexit

On 31 January 2020, the UK left the EU and went into limbo until the end of the year as the final details of the withdrawal were to be discussed. The UK government made clear there would be on alignment with EU regulations once the UK was out of the single market and the customs union. The EC response was that greater regulatory divergence would necessarily mean a more distant trading partnership with the EU [31].

UK manufacturers protested. The car and aerospace industries, chemicals and pharmaceutical firms, the Confederation of British Industry and Unite, the biggest trade union, all talked of the adverse consequences of divergence. The only way to avoid customs, rules of origin and regulatory border checks is to make legally binding commitments to observe all current and future EU rules, which the government rejected. Some 80% of the auto industry's output is exported, and over half of those exports go to the EU. Regulatory divergence would men cars (and car parts) would be subjected to compliance checks in both directions, increasing costs and delays. Some 60% of the chemicals industry's output goes to the EU [31].

The Brexiters' plan to leave the EU envisaged the UK regaining sovereignty over its rulemaking. It would be difficult combining that freedom with still being able to trade freely and easily with the EU. Also, the "Brussels effect" would be a challenge for international supply chains. Optimists thought mutual recognition of standards would be relatively easy to pull off. Peter Chase of the German Marshall Fund think-tank in Brussels and a former US diplomat, said: "the UK starts off from a position of unparalleled harmonisation, with both sets of regulators knowing and trusting each other. It should be possible to design a flexible system that builds on this confidence." Yet ensuring the UK gained any real measure of regulatory independence would be harder. There were few reliable mechanisms to guarantee broad, deep and rapid recognition of disparate international sets of rules [28].

If regulatory divergence was the plan, then mutual recognition through either softer negotiation mechanisms or somewhat more formal dispute settlement bodies that still fell short of the direct authority of the ECJ. The EU already has mutual recognition arrangements with seven other advanced economies, including the US, Australia and Japan, where both sides accept each other's rules as equivalent. However, there have critical limitations. In most case, they do not grant legal "equivalence", which would automatically allow imports of goods into the EU produced under the partner country's rules. They merely acknowledge the competence of laboratories and testing centres in the partner country to confirm that goods conform to EU regulations. They arrangements also tend to cover a small subset of industries, e.g., certification of standards for electronics and telecoms equipment. Whatever attempts were made to recognise the adequacy of other's regulations, it would be the ECJ that has jurisdiction over companies selling in the EU [28].



When the UK decided to leave the EU, there were five models from which it could choose. The first was to join the European Economic Area, a solution adopted by all but one of the EFTA states that did not join the EU. But the

EEA now consists of just one country, Norway, and two smaller ones, Iceland and Liechtenstein. The second option was to try to emulate Switzerland, the remaining EFTA country. It is not in the EEA but instead has a string of more than 20 major and 100 minor bilateral agreements with the EU. Thee third is to seek membership to the ta customs union with the EU as Turkey has done, or at least to strike a deep and comprehensive FTA. The fourth is simply to rely on normal WTO rules for access to the EU market. Fifth, the preferred by most Eurosceptics, was to negotiate a special deal for the UK alone that retains free trade with the EU but avoids the disadvantages of the other models [33].

Apart from immigration and taking control over its borders, Brexit was about getting control over its own regulations. Since Brexit, the UK government has been seeking to benefit from opportunities that come from being outside the EU's cautious and cumbersome regulatory system, where approvals that cover 27 member states are slower than in a single country. But industry representatives express frustration and warn of the gap between the UK's stated ambitions and the capacity of regulators like the Food Standards Agency (FSA) to approve regulations in new areas, e.g., novel foods that include alternative proteins, (cultured meat, edible insects, algae, and chia seeds), but also gene editing, AI and autonomous vehicles [34].

Though laws have been passed promising to deliver "a distinct regulatory framework that provides an economic advantage" and to "remove unnecessary barriers to position the UK as a leading country in which to invest in agri-food research and innovation", they have not been translated into action. Industry representatives argue for a system that approves quickly and gives people the confidence that they will not encounter domestic bureaucracy or create frictions with the EU [34].

The failure to act on the opportunity to strip back time-consuming EU rules inherited from the UK's membership of the bloc is argued to be a big part of the problem. Under the EU rules, approvals for novel foods, for example, take at least 17 months once a formal application has been submitted, including up to a seven month wait for authorisation from ministers. As a non-member now, the UK could not change this but has not. By contrast, the US regulatory body, the Food and Drug Administration (FDA), takes a year. This is in part because the FDA allows companies to ask assessors detailed scientific questions and make necessary changes before submitting their final application – another rule change the UK could make as a non-member of the EU [34].

5. The Multilateral Trading System of the WTO

The WTO provides a forum for negotiating agreements aimed at reducing obstacles to international trade and ensuring a level playing field for all, thus contributing to economic growth and development. The WTO also provides a legal and institutional framework for the implementation and monitoring of these agreements, as well as for settling disputes arising from their interpretation and application. The current body of trade agreements comprising the WTO consists of 16 different multilateral agreements (to which all WTO members are parties) and two different plurilateral agreements (to which only some WTO members are parties) [35].

More specifically, the WTO's main activities are:

- Negotiating the reduction or elimination of obstacles to trade (import tariffs, other barriers to trade) and agreeing on rules governing the conduct of international trade (e.g. antidumping, subsidies, product standards, etc.);
- administering and monitoring the application of the WTO's agreed rules for trade in goods, trade in services, and trade-related intellectual property rights;
- monitoring and reviewing the trade policies of our members, as well as ensuring transparency of regional and bilateral trade agreements;
- settling disputes among our members regarding the interpretation and application of the agreements;
- building capacity of developing country government officials in international trade matters;
- assisting the process of accession of some 30 countries who are not yet members of the organization;
- conducting economic research and collecting and disseminating trade data in support of the WTO's other main activities; and
- explaining to and educating the public about the WTO, its mission and its activities [35].

The WTO's founding and guiding principles remain the pursuit of open borders, the guarantee of most-favoured-nation principle and non-discriminatory treatment by and among members, and a commitment to [predictability and] transparency in the conduct of its activities. The opening of national markets to international trade, with justifiable exceptions or with adequate flexibilities, will encourage and contribute to sustainable development, raise people's welfare, reduce poverty, and foster peace and stability. At the same time, such market opening must be accompanied by sound domestic and international policies that contribute to economic growth and development according to each member's needs and aspirations [35].

The WTO has legal texts to address globalisation and oversees the process of liberalization. These cover four broad areas: (1) General Agreement on Tariffs and Trade (GATT) for the rules on goods; General Agreement on Trade in Services (GATS); Trade-Related Intellectual Properties (TRIPs); and the Dispute Settlement Mechanism (DSM). The basis structure is as presented in the chart (Structure of the WTO).

<table>
<tr><td colspan="4">Basic structure of the WTO</td></tr>
<tr><td>Goods</td><td>Services</td><td>Intellectual Property</td><td>Trade disputes</td></tr>
<tr><td colspan="4">Legal texts covering each of the four areas</td></tr>
<tr><td>GATT</td><td>GATS</td><td>TRIPs</td><td>DSM</td></tr>
<tr><td colspan="2">Sub-agreements and annexes cover specific rules that apply to goods and services sectors</td><td colspan="2"></td></tr>
<tr><td>Schedule of commitments on goods</td><td>Schedule of commitments on services</td><td colspan="2"></td></tr>
<tr><td colspan="2">Country-specific obligations that each country negotiated and to which they agreed</td><td colspan="2">Source: WTO</td></tr>
</table>

Pascal Lamy, former director general of the WTO, defended the one aspect of the organization that is the most frequently cited source of frustration for trade negotiators – its "bottom-up" democracy. One of the bedrock principles embodied in the Marrakesh Agreement that established the WTO in January 1995 is that decision-making is taken by consensus. It means countries, whether small or large, poor or rich have equal rights, and crucially, the power of veto over any agreements [36].

"The WTO decision-making process is democratic," Lamy said. "If it were different, taking decisions on the negotiations would probably be easier." "But it would not be as legitimate. Reaching agreement in the WTO is difficult because it is done bottom-up – and it is good this is so." But critics question whether the democratic principles of the WTO might reduce it to a forum of open-ended debate, which makes little concrete progress towards

the goal of promoting trade to improve the welfare of the world's people [36].

The concerns grew with the rapid increase in the number of WTO member countries and economies. In 1986, at the start of the last global trade negotiation marathon, the 8-year-long Uruguay round, there were 86 members [36]. In 2020 there were 164 member states.

Mike Moore, Mr. Lamy's predecessor and former prime minister of New Zealand, said the rapid expansion in the size of the membership had made the process of reaching trade agreements "more difficult." "It is a victim of its own success," in expanding the membership, he said [36].

Moore, who actively sought the accession of new members when he was director general between 1999 and 2002, supported calls for reform of the organization. The Doha Development Round of trade negotiations, which started in 2001, gave the impression that the WTO was unable to negotiate effectively, " the report said. "As public and political interest has increasingly focused on the institution, it has not always appeared to be able to deliver on the stated ambitions of the member governments" [36].

Despite the slow pace of progress in the Doha round, the report said "it would be wrong to jump to conclusions about the need for structural and procedural change." The only restraint recommended on the use of veto powers was that any member considering blocking a measure should be required to declare "in writing, with reasons included, that the matter is one vital interest to it" [36].

Still, some veterans of the system say that reform in how the WTO works and how members approach the multilateral trading system is vital. The core principle of non-discriminatory trade has been eroded by a plethora of bilateral preferential trade agreements and deals for special and differential treatment of developing countries [36]. The collapse of the Doha Development Round highlights the difficulty of bridging the interests of many players among countries at different stages of development and the comprehensive nature of the agenda makes the trade-offs all the more complex.

During US President Trump's administration, the WTO faced an identity crisis with his instinctual suspicion of multilateral institutions. Trump turned the WTO from what his predecessors saw as a strategic tool into a strategic target. "Simply put, we [the US] have not been treated fairly by the WTO", said Mr. Trump. He charged that the creation of the WTO in the 1990s helped cause the economic heartache that hit many US communities as they lost jobs to new competitors in China and elsewhere. US officials in his administration blamed the WTO for failing in its mandate to negotiate new rules for the global economy. The existing procedures were never designed to cope with the brand of state capitalism that China rode to success for 30 years. The WTO's dispute settlement process was a barrier to trade wars, but disputes take too long and end up in the hands of an appellate body that they accused of encroaching on national sovereignty [37].

Trump's top US trade official, Robert Lighthizer, noted that "there was one challenge on the current scene that is substantially more difficult than those faced in the past, and that is China". The WTO being unable to deal with this problem meant that the US needed to find new ways to ensure a market-based economic system prevailed. Diplomats in Geneva noted that after Trump's election the US played a back-seat role to most WTO negotiations, saying that the US was "not in the game" at all. However, the US took direct aim at the WTO's dispute function by blocking the filling of vacancies on the WTO's 7-member appellate boy on technical grounds. Officials in Geneva believed it masked a sinister agenda to bring down the WTO's dispute settlement system to remove it as a restraint on the sort of unilateral trade action – whether tariffs or other measures – that Mr. Trump preferred to take [37].

The issues raised by the US actions during the Trump administration still matter. The question is whether the concerns the US has with China are more effectively handled multilaterally at the WTO in concerted effort with the EU, Japan, Canada and others. Does it make more sense to strengthen the multilateral system's dispute settlement mechanism rather than resort to unilateral measures? Is negotiating "voluntary import expansions" by China or Japan for US goods an appropriate means to settle issues of trade deficits? Do the more expeditious short-term benefits of a unilateral action wind up costing more in the long run because it results in tit-for-tat trade wars? Does using questionable "national security" justification for initiating trade measures open the door for its general use, undermining the principles of the WTO and the rules-based system that has brought stability since the 1950s? Will the global trading system become less predictable and more contentious without the appellate body to act as honest broker?

Perhaps the most pressing problems are the national security concerns many countries have with China dominating 5th-generation (5-G) IT, raising the issue of "decoupling" the West from China. Blacklisting Chinese firms from US or western technology can create parallel platforms (separate infrastructures and supply chains) for 5-G. Under Trump the US bullied allies to stop buying gear for 5-G networks from Huawei and threatened sanctions on chipmakers who supply it. Tightened export controls on US technology could as easily force Chinese companies such as Huawei to look for non-US components from competitors as it could isolate US firms from Chinese technology. China is already pulling countries into its orbit with initiatives such as the "digital Silk Road", helping them to build out their digital infrastructure [38].

A grand bargain is being considered to turn conflict with Europe into collaboration. The EU's effort to carve out its own space in the regulation of the digital realm makes it a relevant ally in confronting China. The ECJ's ruling on the Privacy Shield to protect it citizens is an example. Through shared approaches to critical technologies, it might be possible to specialise rather than duplicate research efforts. By diversifying supply chains and vetting each link countries can protect themselves from accidental or malevolent disruptions. By working on technical standards, a favourable environment can be created for companies. By collaborating on ethical norms over, say, facial recognition, like-minded democracies can protect their societies. A grand bargain would help allied countries to keep up with China in the race for tech dominance [38].

Death of the Doha Round

The Doha Round of the WTO was launched in 2001 with much rhetoric about gestures of global unity but too little support from businesses to keep it going. It was oversold as a "development round", with the aim of helping poorer countries trade their way out of poverty with a particular focus on agriculture [39].

Three problems rapidly became evident. One, behind the mask of solidarity between developing countries lay deep divisions, for example between agricultural net importers and exporters, preventing constructive proposals for liberalisation. Two, countries such as China transformed beyond recognition during the round, becoming global export powerhouses yet continuing to plead developing country status. Three, the US in particular proved to be largely spineless in taking on its own farm lobby, which

demanded improbable amounts of market access a broad in return for subsidy cuts at home [39].

Doha in effect died when a ministerial meeting failed in 2008. While it continued for another seven years on life support, governments, particularly the US, pushed ahead with the mega-bilateral or -regional deals. These agreements, especially the TPP, were weak substitutes for multilateral deals, not least because they were one-sided agreements written by the strongest signatory. They died as Doha died, but does their passing open up the space for multilateralism to be reborn [39]?

On 1 Mar 2021, Ngozi Okonjo-Iweala became the first woman and the first African to lead the WTO. She noted that if the WTO's credibility is to be restored, differences must be set aside, and reforms agreed to when trade ministers were to meet later in 2021. The WTO rule book must be updated to take account of 21st century realities such as the digital economy. The pandemic accelerated the use of ecommerce, enabling women and small and medium-sized enterprises to participate in international trade. The digital divide must be bridged or some developing countries will be reluctant to join the ecommerce negotiations [40].

Negotiations among some WTO members on facilitating investment and removing regulatory red tape in services trade have continued intensively despite the pandemic. Participants need to broaden the support for these initiatives and attract interest from developing countries with the aim of concluding talks by the end of the year [40].

More can be done to ensure the TO addresses the nexus between trade and climate change. Members should reactivate and broaden the negotiations on environmental goods and services but climate-related restrictions cannot become disguised restrictions on trade, and we must assist developing countries as they transition to the use of more environmentally friendly technologies [40].

The WTO's work in new or innovative areas does not mean that traditional topics such as agriculture are forgotten. Improving market access for export products and dealing with trade-distorting farm subsidies remain of paramount importance to developing and least-developed countries. One area ripe for early agreement involves the removal of export restrictions on farm products purchased for humanitarian purposes by the World Food Programme. Ensuring government support for state-owned industrial enterprises does not distort competition is also a top priority for many WTO members [40].

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