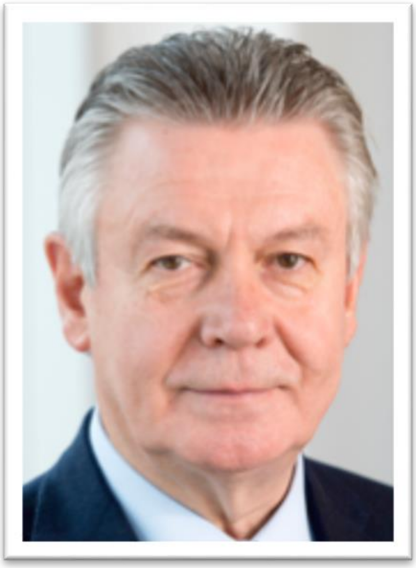
New legal and material developments in international trade



Karel De Gucht, Belgian Minister of State and former European Commissioner for Trade

Report of the speech given by Mr. Karel De Gucht, Belgian Minister of State and former European Commissioner for Trade, at the Belgian Financial Forum in Brussels, December 21, 2017, written by Frank Lierman, chairman of the Editorial Board of Bank- en Financiewezen-Revue bancaire et financière.

Introductory remarks by Professor Freddy Van den Spiegel, chairman of the Coordination Committee of the Belgian Financial Forum.

International trade has been all over the news lately, mainly because support for freer trade has weakened, most notably in advanced economies.

Nonetheless, the benefits of international trade are manifold. Not only does trade give us access to a wide variety of goods and services from all over the world, it has also been a critical source of growth and productivity, through different channels.

As basic economic theory puts it, trade enables a country to use its resources more efficiently, specializing in the production of goods and services for which it has a comparative advantage. But trade also fosters innovation and productivity, by facilitating the distribution of knowledge and technologies.

Moreover, competition from abroad forces domestic companies to raise their efficiency and upgrade product quality.

The two decades before the crisis marked a period of very high trade growth, boosted by a rapid pace of trade liberalization, through multilateral trade agreements, the deepening of the EU single market and the accession of many emerging market economies, such as China, to the WTO.

More recently however, this trend seems to have reversed. While they recovered strongly since the end of last year, international trade flows have slowed dramatically since the global financial crisis – last year marked the weakest growth in global trade since 2009. Though this mostly reflects anemic global demand, it is also a consequence of the slower pace of new trade reforms and an uptick in protectionist measures.

Indeed, while trade has many benefits, the gains from trade – or trade liberalization – have not always been divided equally. The excessive search for “cheap labour” by most multinational companies has been leading to massive delocalization of production and has contributed to worldwide unsustainable imbalances. The effects on employment and wages differ between sectors and workers. In advanced economies, the traditional, manufacturing industries and lower-skilled workers have generally borne the losses as production moved abroad. This uneven distribution of the benefits and drawbacks of trade liberalization has been an important source of the growing opposition against globalization. While the financial crisis itself was not a direct consequence of globalization, the subsequent period of consistently low growth and high unemployment in many countries and regions probably fed the anti-globalization trend.

Moreover, after 25 years of globalization, the structure of the world economy has totally changed. China, among other emerging economies, changed from a poor underdeveloped country to the biggest economy of the world. And these economies are no longer specialized in cheap labour activities but are increasingly competing for high value parts of the global value chain.

Against that background, support for trade liberalization has waned. The post-crisis period saw an upswing in trade-restrictive measures, while progress with the conclusion of free trade agreements has stalled over the last years.

More particularly, uncertainty about the future of several trade agreements has increased under the Trump administration, as the US has withdrawn from the Trans Pacific Partnership (TPP) for example, or insisted that the NAFTA agreement with Canada and Mexico be renegotiated. Negotiations about the Transatlantic Trade and Investment Partnership (TTIP) between the EU and US have also been put on hold.

Also, the WTO 2001 Doha Round of multilateral trade negotiations was abandoned in December 2015, in favour of negotiating on specific, more narrowly focused agreements. Last but not least, the nature of trade relations between the UK and the EU post-Brexit remains highly uncertain.

A further shift towards more inward-looking policies would reduce trade and cross-border investment, harming global growth. The EU has always been a frontrunner when it comes to free trade and we should continue to resist protectionist tendencies, while keeping agreements fair. Just two weeks ago, the EU and Japan concluded a free trade deal that that will create the world's largest open economic zone when it comes into effect in 2019.

That doesn't mean however that concerns about the consequences of globalization needn't be recognised. Governments should increase their efforts to ensure that gains from free trade are more broadly shared.

At the same time, further trade reforms are needed in several areas, as trade regulations have not always kept pace with the evolving global economy. Integrated global production structures for example require more coherent rules across different policy areas. In addition, a further deregulation of services trade or progress in new areas such as digital trade could provide a renewed boost to global trade.

No one is better placed than Mr. Karel De Gucht, former commissioner for trade of the EU, to give us an update about what is going on today and what are the perspectives and challenges for the future development of international trade.

Summary of the speech of Mr. De Gucht.

According to Mr. De Gucht there is an interaction between political, economic and legal developments in the actual debate about the impact and future of International trade, which has become extremely emotional compared to former periods in which common sense used to dominate. There are three major introductory observations to be made:

- International trade is identified with globalisation, which is now largely considered an evil force. This is false. The positive development of the European economy during the last decades was impossible without international trade.

The initial members of the EU registered the most profit, but also the others which joined the EU have had positive experiences. Without international trade, we become an autarchic society, which would require a complete change of our economic organisation, and for which there is probably not much support.

- It is not true that international trade is the ultimate responsible phenomenon for the increasing challenges of the world economy. But indeed, the structure of international trade has changed fundamentally over the last 25 years. In 1990, 20% of the international trade was done by the emerging countries while the western developed countries intervened for 80%. Now, the emerging countries represent 55% and the developed countries only 45%.
- The real revolution is about digitalization, and that is an extremely challenging development. For example: some ten years ago each village had its own “wall street” of bank-offices/branches, while now most of them have only ATMs as points of contact with the banks. Digitalisation is a direct danger for jobs of the affluent middle class. A lot of jobs are in danger; new ones are indeed created but in very specialized parts of the economy, such as in the IT sector. There is a multiplication of low salary jobs such as the persons who deliver parcels (thanks to e-commerce), but will that be a socially acceptable solution (alternative)? For now, we face a society with a discontent middle class which is a source for political instability.
- The existence of international escape roads for taxation, which are often used by multinationals, is also becoming increasingly unacceptable. More and more people, who are paying high taxes themselves, do not understand why this practice is still politically accepted.

We should catch the impact of those three developments to stop the sometimes-false discussions and myths launched via social media. These often focus on one specific element of a much more complex issue, leading to simplistic characterisations, which are then spread with an extremely high speed. A striking example is the debate on ISDS (Investor State Dispute Settlement) within the discussion of TIPP between the USA and the European Union. The ISDS is an international agreement which gives a company - who feels itself discriminated in its international activities - the opportunity to bring the matter before an international arbitral tribunal. The argument used by critics is that this is only profitable for multinationals. There are indeed some concrete cases: Vattenfall in Germany after the decision of the German government to close down the nuclear power stations, or Philip Morris in Australia after the revision of the smoker’s law. But the fact is that within the EU there are already some 1400 similar ISDS clauses in agreements with and between EU countries. In Germany alone, we take note of 120 ISDS clauses.

Germany refused to ban them due to a lack of confidence in some Member States' legal system. In fact, ISDS clauses already exist since more than 50 years in the EU. TTIP has no chance to be successful without ISDS.

Meanwhile, in order to answer to the critics, the ISDS procedure has been modified into an Investment Court System (ICS), where a panel of qualified judges will make the decisions (comparable to the WTO Appellate Body).

Another crucial debate is the search for and creation of a level playing field in international trade agreements. Since the Lisbon Treaty, the procedures to negotiate such an agreement have changed dramatically. The European Parliament is now given power to approve the trade agreements which have been negotiated by the European Commission. As such, the previously administrative approach is now converted into a political process, which is a good thing. This being said, a pure 100% level playing field is unrealistic because in that case there is no economic advantage, thus competition, between partners.

The third crucial factor to be underlined is the incorporation of special compacts in the trade agreements. Some examples are: the protection of the environment in the agreement with Japan, the respect for trade unions in the agreement with Columbia, the demand for high standards for the labour market and rights in the agreement with Vietnam, corporate responsible investment standards in the agreement with Bangladesh, the anti-dumping and anti- subsidization rules in the agreement with China. They are important to keep the agreement "fair" and to encourage the partners to implement acceptable policies.

The fourth debate is focussing on who is negotiating and who is ratifying the trade agreements. The European Commission is the negotiator, while the European Parliament must ratify each agreement. Of course, there are also the so called 'mixed agreements' in which X percentage of the topics are of a national matter and need Member State approval. Nevertheless, we do need unanimity within the Council of Ministers for all agreements. Member States have in fact no power (competence) anymore in (negotiating/concluding) trade agreements since the so-called Singapore opinion of the European Court of Justice. This has put an end to the tradition that each government - local, regional, national – of each Member State in the EU must ratify the trade agreements (cf. the position of Mr. Magnette of the Walloon government in the approval process of the CETA agreement with Canada). The recent agreement with Japan was the first in which the new rules were applied for some 95% of the agreement which focuses on pure trade. The chapters concerning investments, good for some 5%, are still in negotiation. Investments are up to now still considered as shared competences.

All in all, the final question is: is there still room for international trade agreements? My answer is “Yes”. But this being said, the Doha round – as we know it - will not emerge from its deadlock. Multilateral agreements remain complex, but via bilateral even plurilateral (e.g. TPP) agreements progress is still possible.

The position of China concerning trade agreements has changed dramatically. On the one hand, it is can be considered a developed country positioning itself as a fierce competitor in the region and globally too, while on the other hand, it is still an underdeveloped country for the largest part of its territory. An example can maybe clarify this. The green good initiative in the campaign “aid for trade” was launched during a Davos summit some years ago. It was initially blocked by China, but after a few days they decided to participate, taking up their global responsibility. But the practical result has been that every progress has been blocked by China, claiming then to be a developing country in need of special rights and differential treatment. Also, the USA is playing a negative role due to its action against the WTO. Decisions from the Appellate Body are only considered and accepted if they are good for the USA. But as there is no sitting US judge in the body, every proposal is rejected as being unfair to the US. Also, the decision of the US then to give more attention to the Trans-Pacific Partnership (TPP) was a real handicap to go forward with the Transatlantic Partnership (aka TTIP). But the EU’s agreement with Japan “food for cars” is fine, due to its complementarity (reciprocity). The fact is that for example Toyota already produces more cars in Europe than cars being exported from Japan to Europe. We may not forget that the EU is the biggest world (economic) market, followed by the USA, China, Japan and South-Korea. So international trade remains crucial.

Another example is the Economic Partnership Agreements (EPAs) between the EU and Western Africa, Southern Africa and Eastern Africa. Read from the EU-side: to stop the unfair Chinese practices and influence in Africa. Giving those African countries the advantageous status of Most Favourite Nation (MFN) implies trust. It simply means that the EU, in exchange for it granting full free access to its market all products but arms from EPA partners, expects to be treated equally with other major economies – like China – if EPA partners open up their markets to them.

We may not forget that China is the biggest spoiler in international trade. More worrisome is its expanding sphere of influence into Eastern Europe and Mid-Asia through its “One Belt, One Road” initiative, a one-way network of trade and technological routes. China organises special summit meetings with those countries to seize its dominance over public procurement and public investment opportunities.

Could the US system in that respect be an example for the EU? The US can refuse investments to protect themselves against China. We know that China is looking for technology, intellectual properties and trade secrets to dominate the world.

The EU can and must do something to protect its status as a global economic giant. The EU must be a leader on global norms, standards and regulations. This is essential. Tariffs are less disruptive and less crucial. The Chinese norms are unacceptable for the EU. China could have difficulties in the coming years looking for a higher position in the (global) value chain. A new generator of growth must be found, go beyond State-Owned initiatives and the hijacking markets of others just so to get rid of its overcapacities. A level playing field and market access is a step forward. China also needs to be careful as its huge volume of non-performing loans and credits could be a major stress for its banking sector, which is not good news for the rest of the world.

To conclude, trade agreements could be part of the political toolbox. In Ukraine, for instance, the ongoing crisis and conflict is because Russia won’t accept that Ukraine chose for international trade and a closer link with the EU. Also, the ultimate objective of the Brexit discussions is to end up with a free trade agreement. A significantly ambitious deal is seeked. But the UK does not want a copy of CETA, because the UK’s dominant financial services sector would not be covered. But a single trade agreement that is open to financial services does not exist. Nowhere. Quid the trade-off between the access to the internal market and the financial support. In fact, the difference between a hard Brexit and a soft Brexit is the debt burden. It is not certain that a quick solution is possible.