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Lamy: “Putting geopolitics back at the trade table”

At a speech at the IISS-Oberoi Discussion Forum in Delhi on 29 January 2013, Director-General Pascal Lamy commented that “while the world is mutipolarising at an unprecedented scale and speed, and production and trade value chains are multilateralising, trade governance seems to be bilateralising.” He warned that “we risk scattering the level playing field”. This is what he said:

“Putting geopolitics back at the trade table”

I am delighted to be here in Delhi for this IISS-Oberoi Discussion Forum. Thanks to Sanjay Baru for making it happen.

Many of you in this room have witnessed the dramatic changes in international commerce that have taken place during the past two or three decades.

India’s trade volumes have registered healthy growth. Indian companies have thrived at home, and steadily expanded their presence abroad. Without downplaying the enormity of the challenges India faces, it is evident that the country is making a comeback in the world economy. A world economy that was being radically reshaped by the rise of emerging markets even before the transatlantic financial crisis accelerated the process.

In this changing international system, decisions made by Indian policymakers and Indian businesses matter. More to the point: the decisions you, and people like you, make will matter for the future of world trade, for the future of the world trade system and for the future of the WTO.

I intend to use my remarks today first to reflect on the importance of economic growth as a tool for managing geopolitical tension, and then to appeal for a return to thinking in geostrategic terms about the international policy environment that supports growth.

Growth

Economic growth, when widely shared, does more than increase living standards. It helps ease tensions within societies. Benjamin Friedman, a Harvard political economist, has noted that when standards of living are

rising for a clear majority of citizens, it tends to foster greater tolerance of diversity, social mobility, fairness, and dedication to democracy. The absence of growth, in contrast, tends to foster conflict over how wealth is distributed. Even in wealthy societies, stagnation and decline have often been marked by divisive politics and xenophobia.

As within societies, so too between them. Societies riven internally by economic anxiety and distributional conflict are not likely to deal with their neighbours in a spirit of friendliness.

We have seen this all too well since the beginning of the 2008 crisis. In high-income countries, a weak recovery and stubbornly high unemployment have made voters fearful that any gains made by faster-growing emerging economies are coming at their expense. This has made their political representatives even more reluctant to make what they see as “concessions” to China, Brazil or India in international negotiations. Emerging economies have responded in kind, wary of losing hard-earned developmental gains.

The result has been that **multilateral rule-making on issues ranging from trade governance to climate change,** already struggling prior to the crisis, has come to a near halt.

The once-widespread conviction that well-managed globalisation could offer ‘win-wins’ for developed and developing countries now seems distant. Hopes of cooperative action to tackle environmental degradation appear to have dwindled.

In the words of Financial Times columnist Gideon Rachman, the ‘age of optimism’ that reigned between the collapse of the Soviet Union and the fall of Lehman Brothers has given way to a ‘zero-sum world’.

But the world has never been more interdependent in terms of economic stability, food security, climate security, and even health and political security. The gains to be had from greater co-operation are immense, but governments in thrall to zero-sum thinking cannot hope to realize them.

I believe that increased growth could help to soothe geopolitical tensions, by making positive-sum outcomes more visible.

Trade

Trade has an important role to play in boosting both growth and security, even more so when complemented by policies to ensure that its benefits are widely shared.

For low-income countries, open global markets are essential sources of demand and know-how for achieving rapid catch-up growth.

For countries at the technological frontier, recent studies predicting **diminishing productivity returns from innovation** make it all the more important to maximise the growth obtainable through trade policy. New WTO-OECD research on measuring trade in value added has confirmed that export performance and business competitiveness have become increasingly dependent on countries' openness to imports and participation in value chains. Services add considerable value to manufacturing exports. We need to internalise a paradigm shift: today, one of the best ways of encouraging exports is to facilitate goods and services imports!

Turning now to trade and security. The recognition that trade promotes peace, by binding nations together in ties of mutual interest and dependence, dates back at least to the Enlightenment. It is an insight no less relevant today than it was during the 18th century.

Conflicts are about much more than economics, of course. Nevertheless, it is clear that India-Pakistan relations will be quite different when a vibrant trading relationship creates constituencies for peace on either side of the border. Indian and Pakistani policymakers have recognised this, and have set targets for opening and expanding trade. Their leadership deserves praise.

A similar case could be made for the Israelis and the Palestinians, for whom two decades of increasing economic separation have helped to make peace an even more distant prospect than it was twenty years ago.

To put it bluntly: it is important for people to have a stake in something other than wanting to kill each other.

Perhaps nowhere is the imperative for growth more visible than in the Middle East and the Maghreb, where, in the absence of job creation and realistic hopes for a better future, the Arab Spring is all too likely to wither into a long and arduous winter.

While trade and growth can contribute to easing

geopolitical tensions, we should also remember that geopolitical tensions can impact trade and growth. We saw this last year with the tensions between China and Japan in the China Sea. It is also true for the relationship between Morocco and Algeria, or even between the US and Cuba.

Even civil conflicts in seemingly isolated places can have global consequences, as we are seeing with the on-going events in the Sahel and, in particular, Mali. But such conflicts are also rooted in a lack of economic development and the neglect of regional and social disparities. Academic research on civil conflict serves to underscore the importance of growth: The lower a country's starting income levels, the higher the risk of civil war. Growth reduces the risk of civil war, but a decline in GDP increases it. Diversification matters, especially for commodity rich countries – countries heavily dependent on exports of primary commodities are at vastly higher risk of civil conflict.

UN Post-2015 Agenda

No country has achieved the sustained high growth necessary for mass poverty reduction without successfully exporting a diversifying range of products into open global markets. This is why promoting growth, increased productive capacity, and trade must be central parts of the United Nations' post-2015 development agenda.

But open markets alone are not enough. Rising labour costs in East Asia will not inevitably drive light manufacturing towards poorer countries. In Africa, for instance, invisible costs arising from expensive finance, unreliable electricity and poor transportation infrastructure mean that business operating costs are relatively high even when wages are not. Inclusion in the UN's future development agenda would encourage national governments and donors alike to focus on removing supply- and demand-side obstacles that prevent new countries from breaking into world markets. Aid for Trade must therefore be an essential ingredient of a post 2015 development agenda.

Institutions

And finally, strategy. History teaches us that growth, trade and investment do not automatically secure peace and prosperity. A century ago, decades of cross-border trade and investment could not prevent the classical liberal order from collapsing into thirty years of economic chaos and two wars of unprecedented brutality.

As the architects of the post-1945 international order worked to revive world trade in order to stimulate growth and employment, they sought to entrench trade opening in a non-discriminatory, predictable, rules-based institution, the GATT then turned into the World Trade Organization.

The Cold War presented the GATT with strategic imperatives from the start. The pursuit of these imperatives actually helped to strengthen the system, according to historians of early GATT negotiations: the need to present a common front to the Soviet bloc pushed leading members – initially the US and the UK – to moderate colliding demands, and then to face down domestic political opposition to their compromises. In a similar vein, Europe’s trade and investment integration was driven as much by political logic as by economic rationale.

The fall of the Berlin Wall liberated many countries to join the world economy. The supposed ‘end of history’ also afforded us the luxury, after nearly half a century, of disconnecting economic diplomacy from geopolitical concerns.

Or so it seemed. The US National Intelligence Council last year predicted that by 2030, “no country – whether the US, China, or any other large country – will be a hegemonic power.” It anticipates the rise in economic importance of a variety of regional players such as Indonesia, Nigeria, and Turkey. The report openly wonders whether multipolarity will lead to increased resilience in the global economic order, or whether “global volatility and imbalances among players with different economic interests” will result in collapse.

Geopolitics is back. Or at least it should be. Bringing foreign policy interests back to the table might conceivably help systemically significant countries build domestic support for multilateral co-operation on trade: not as a bulwark against a common foe, as during the Cold War, but because of their shared interest in preserving a functional international order.

What we have been seeing instead, however, is a paradox: the world is multipolarising at an unprecedented scale and speed. Production and trade value chains are multilateralising. Trade governance, however, seems to be bilateralising.

But one has to ask whether these bilateral rules will adequately respond to the needs of the regional and global value chains that now make up a majority of world

trade. While bilateral tariff reductions can ultimately be multilateralised, a plethora of bilateral trade agreements will produce a multitude of regulatory standards with which businesses will struggle to comply. We risk scattering the level playing field. It does not help economically. But what about geopolitics?

While it has become fashionable to say the WTO has too many members to agree on new rules, the reality is that the deadlock in the WTO Doha Round negotiations is due to disagreement among a small handful of advanced and emerging economies. Like the climate change negotiations, it is geopolitical in nature.

Agreement is still lacking on the balance of contributions and benefits between the US, the EU, Japan and the like on the one side, and India, China, Brazil and the like on the other side. Advanced economies argue that emerging economies have now “emerged” and should therefore accept a trade regime that is similar to theirs. Emerging countries argue that they still face daunting development challenges which require flexibilities in the form of “special and differential treatment”, as we say in the WTO, or what the UN climate process calls “common but differentiated responsibilities”. Behind this conundrum lies a simple geopolitical question: are emerging countries “rich countries with many poor people” or “poor countries with many rich people”? Until and unless both sides agree on the answer, consensus in major multilateral negotiations will remain elusive.

In my view, the answer is also geopolitical. It requires agreement on three principles.

Principle one, emerging countries must accept that, as they develop, they will align their level of international commitments to those of advanced economies.

Principle two, advanced economies must recognise that, given their own historical responsibilities in existing global warming and the remaining unfairness in trade rules, emerging countries deserve long transition periods to converge towards common commitments.

Principle three, for the poorest countries, whether on trade or on climate change, the issue is less what level of commitments and more how to help them build the capacity to be active members of the international family.

If convergence could be found on these principles, I am convinced that the technicalities of trade or environment

reforms could rapidly emerge.

On the trade side, one logical first step for both sides to take together would be an agreement on trade facilitation, i.e. a deal to cut customs red tape: low political costs, modest financial costs, but very substantial economic returns, widely distributed. The thickness of borders today costs two to five times more than import tariffs, depending on whether you look at macro or micro economic impact studies.

Another step would be to examine how to start rolling back the accumulation of post-crisis trade-restricting measures, which now affect around 3 per cent of world trade.

Businesses have an important role to play in these short term deliverables, both in asking governments to engage internationally, and persuading them to implement domestic trade policies that reflect commerce as it is practised today, not as it was twenty years ago.

The last time I spoke at an IISS event, I said that a Doha Round agreement would provide one of the world's first confirmations of a changed economic power balance. We are still waiting for proof that multilateral rule-making will be possible in a multipolar world. Only a new age of strategic pragmatism can get us there.

I thank you for your attention.