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Why the World Still Needs Trade

The Case for Reimagining—Not Abandoning—Globalization

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The international economic architecture built after 1945 was based on a powerful idea: economic interdependence is crucial, if insufficient, for global peace and prosperity. The International Monetary Fund, the World Bank, and the predecessor to the World Trade Organization were founded in response to the three preceding decades of ceaseless instability, when the world had been devastated by two world wars, the Great Depression, and political extremism. It had also been a period of deglobalization, in which countries retreated into increasingly isolated trading blocs. In the rubble of World War II, governments sought to construct a new system that, by linking countries in a dense web of economic ties, would consign such chaos and division to history.

For much of the past 75 years, policymakers from across the world recognized the power of economic interdependence. Countries tore down trade barriers, opening their economies to one another. On balance, their record was impressive. Closer economic integration went hand in hand with rising global prosperity, an unprecedented reduction in poverty, and an unusually long period of great-power peace. Since 1990, the share of the world's population living in extreme poverty has fallen by three-quarters. At the center of this great leap in human well-being was a 20-fold increase in international trade volumes, which helped lift per capita incomes by a factor of 27 over the last six decades.

This economic vision is now under attack, and its achievements are in danger. A series of shocks in the space of 15 years—first the global financial crisis, then the COVID-19 pandemic, and now the war in Ukraine—have created an alternative narrative about globalization. Far from making countries economically stronger, this new line of thinking goes, globalization exposes them to excessive risks. Economic interdependence is no longer seen as a virtue; it is seen as a vice. The new mantra is that what countries need is not interdependence but independence, with integration limited at best to a small circle of friendly nations.

But dismantling economic globalization and the structures that support it would be a mistake. That is because, despite persistent rhetoric to the contrary, countries and people rely on trade more than ever in this age of "polycrisis." Moreover, international cooperation,

including on trade, is necessary to meet challenges to the global commons, such as climate change, inequality, and pandemics. Globalization is not over, nor should anyone wish for it to be. But it needs to be improved and reimagined for the age ahead.

THE END OF AN ERA?

The drift away from ever-closer economic integration was reshaping trade policy even before COVID-19. Rising geopolitical tensions between the world's two biggest economies, the United States and China, saw the imposition of tit-for-tat tariffs. But the events of the past few years have supercharged the trend. The pandemic and the war in Ukraine exposed genuine vulnerabilities in global trade, causing product shortages and supply bottlenecks that harmed businesses and households alike. Talk of "decoupling" became widespread. More recently, governments have enacted a growing number of export restrictions, particularly for goods deemed strategically important, such as semiconductors and critical minerals. They have also revived industrial policies aimed at promoting domestic production.

That said, talk of deglobalization remains at odds with the trade data. In fact, global merchandise trade hit record levels in 2022. Over three-quarters of that trade was conducted on the basic "most-favored nation" tariff terms that governments extend to all World Trade Organization (WTO) members, suggesting that the multilateral rulebook still plays a defining role in international commerce. According to data from the U.S. Department of Commerce, total trade between the United States and China reached an all-time high of $691 billion in 2022, which is 24 percent higher than it was in 2019. The share of intermediate inputs—goods used to produce other goods—in world exports remains roughly constant, suggesting that there has been no mass reshoring of international supply chains. Companies still make sourcing decisions based on cost and quality considerations. Policy measures could yet alter this calculus, but not overnight.

Outside a brokerage office in Tokyo, March 2022
Kim Kyung-Hoon / Reuters

The experience of COVID-19 also showcased the power of international trade as a shock absorber. Early in the pandemic, as demand for medical products such as masks, gloves, and nasal swabs spiked, some of the disruptions were made worse by export restrictions on such goods. But trade swiftly became a vital means for ramping up access to desperately needed supplies, from personal protective equipment to pulse oximeters to, eventually, vaccines. Even as the value of global merchandise trade shrank by nearly eight percent in 2020, trade in medical products grew by 16 percent. Trade in cloth facemasks nearly quintupled. After COVID-19 vaccines were developed, billions of doses were manufactured in supply chains cutting across as many as 19 countries. Without trade, the recovery from the pandemic—from both the immediate public health crisis and the resulting economic crisis—would have been much slower.

In other words, despite the growing movement to dismantle the system underpinning globalization, people and businesses rely on it more than ever. Advocates of deglobalization

are effectively calling for the disruption of the roughly 30 percent of all global output that depends on trade, a move that would only add to the downward pressure on peoples' purchasing power across the world. In light of the strong rebound in trade that helped economies recover and kept most pandemic-induced shortages temporary, it is clear that the fundamental problem is not interdependence per se but an overconcentration of some trading relationships for certain vital products. And if the goal is more resilient supply networks that are less susceptible to weaponization by rivals, there is a better way forward.

DON'T DEGLOBALIZE, REGLOBALIZE

Deeper, deconcentrated, and more diversified global supply chains—what we at the WTO call "reglobalization"—offer a route to interdependence without overdependence. The problems exposed over the last three years can be turned into an opportunity to give countries and communities that have so far been excluded from global value chains a way in.

In a handful of sectors, some reshoring or near-shoring looks inevitable. But beyond these limited areas, such measures could come at enormous economic cost. Researchers at the WTO have estimated that if the world splits into two separate economic blocs, the resulting reduction in international trade and loss of productivity from specialization and scale economies would reduce real incomes over the long term by at least five percent on average from the current trend. The output losses would be far greater than those caused by the 2008–9 global financial crisis. Low-income countries would see real incomes drop by as much as 12 percent, dealing a massive blow to their development prospects.

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What is more, large-scale reshoring could backfire by making supply chains less, not more, resilient. Negative supply shocks are likely to become more frequent in the years ahead as droughts, heat waves, and flooding wreak havoc with production and transport. Closing the door to trade would increase countries' exposure to such shocks. In contrast, a reglobalized world economy would offer countries more outside supply options and thus more resilience.

In 2022, the United States saw firsthand that domestic production alone cannot ensure supply resilience when it experienced a shortage of baby formula. Nearly all formula sold in the United States was made domestically, and when one of the four major manufacturers had to stop production at one of its plants because of bacterial contamination, heart-rending shortages ensued. What ultimately mitigated the crisis was trade: the Food and Drug Administration authorized imports of formula on an emergency basis.

"Friend shoring," the notion of moving production to geopolitical allies, is no panacea, either. Whenever someone proposes "friend shoring," I always ask, "Who is a friend?" History has plenty of examples of friends behaving in unfriendly ways, especially when it comes to each other's exports. Trade tensions can arise even among allies.

TRADING GREEN

But the case for reglobalization goes further than such practicalities. It springs from the fact that the world needs international trade to overcome the most pressing challenges of the day, such as climate change, poverty, inequality, and war. It is often said that global problems demand global solutions. Too frequently, however, cooperation on trade is omitted from the list of those solutions.

The WTO is doing its part to rectify that omission. Last June, at our 12th ministerial conference, the organization's 164 members agreed to cut tens of billions of dollars in harmful fisheries subsidies, helping ease pressure on overexploited marine fish stocks while boosting the livelihoods of the millions of people who depend on healthy oceans. Members committed to preventing emergency food aid purchases from getting bogged down in export restrictions. They also pledged to keep food and medical supplies moving around the world, helping ensure availability and reductions in price volatility. When the war in Ukraine disrupted the supply of food, feed, and fertilizer, the WTO stepped up monitoring of related trade policies and urged members to stick to their pledges to keep markets open. As of early May 2023, around 63 of the 100 or so export-restricting measures that countries had introduced on food, feed, and fertilizer since the start of the war were still in place. Although there is much room for improvement, things are headed in the right direction.

The existential imperative of climate change is another area where trade can—and must—be part of the solution. Trade is often portrayed as damaging the environment, with concerns about emissions related to shipping, air freight, and trucking spawning initiatives to "buy local." It is true that transportation, like other carbon-intensive sectors, needs to reduce its emissions, and indeed, researchers are hard at work on alternative fuels, such as green hydrogen and green ammonia, to power cargo ships. But what critics miss is that the world cannot decarbonize without trade. It is an indispensable channel through which green technologies can be disseminated and countries can access the goods and services they need to recover from extreme weather events and adapt to a changing climate. The competition and scale efficiencies made possible by international trade and value chains are critical for driving down the costs of renewable energy technologies, accelerating progress toward the goal of net-zero emissions.

Moreover, international trade can help reduce emissions related to goods by allowing countries to specialize. Just as countries can reap economic gains by focusing on what they are relatively good at, the world can reap environmental gains if countries focus on what they are relatively green at. From the perspective of the planet, it makes sense to import energy-intensive products from places with abundant low-carbon energy or water-intensive products from places with abundant water. For example, a recent World Bank report noted that abundant wind and sun put Latin America and the Caribbean in a good position to produce green hydrogen.

But this sort of environmental comparative advantage works only when the right policy incentives are in place, so that the environmental costs of a given activity are taken into account—"internalized," in the language of economists. Here, too, cooperation on trade has a critical role to play. As more governments take serious climate action, divergence in their policies could give rise to serious trade frictions and concerns about lost competitiveness. If

these tensions go unchecked, countries could end up introducing trade restrictions and retaliating in kind to the restrictions of others. This would increase uncertainty for businesses, thus discouraging low-carbon investment. Higher trade barriers and lower investment would in turn combine to raise the cost of decarbonization—the exact opposite of what the world needs. Governments can avoid this scenario by reaching a shared understanding of how to assess and compare the equivalence of each other's climate policies—whether taxes, regulations, or subsidies—with a view to helping preempt trade conflict associated with climate measures. The WTO is at work on potential approaches that could inform this kind of global carbon pricing framework, as are the International Monetary Fund, the Organization for Economic Cooperation and Development, and the World Bank.

Trade can help the world achieve environmental objectives in other ways, too. Many WTO members are looking at reforming and reducing the subsidies that governments give to fossil fuel producers and consumers, and some are considering lowering trade barriers to environmental goods and services such as technologies to manage air and water pollution. Parallel to these efforts, some members are taking bold steps to incentivize investment in green technology. Although the WTO rulebook supports efforts to decarbonize, it encourages members to do so in ways that do not discriminate against others or lead to subsidy races in which trading partners are harmed. There are ways to go green and to subsidize, including by supporting research and innovation, that do not undermine a level playing field.

CLOSING THE GAP

Trade has long been a powerful force for poverty reduction as well. It permits countries with small or poor home markets to take advantage of external demand to shift people and resources out of subsistence activities and into more productive work in manufacturing, services, and agriculture.

In the decades before the COVID-19 pandemic, trade played an instrumental role in lifting over one billion people out of extreme poverty. This was not just a story of China's economic ascent. The share of the global population living on less than the equivalent of $1.90 a day declined from 36 percent in 1990 to around nine percent in 2018. Taking China out of the equation, that share over the same period still fell substantially—from 28 percent to 11 percent. The result of this boom was a dramatic rise in living standards almost everywhere. In the quarter century leading up to 2019, the gap between incomes in poor countries and those in rich economies began to narrow for the first time since the Industrial Revolution, 200 years earlier.

These trends have now been thrown into reverse. The World Bank has estimated that the pandemic and the war in Ukraine have pushed as many as 90 million more people into extreme poverty. Rich economies, which enjoyed early access to vaccines and the resources to rescue their economies through big fiscal stimulus packages, are once again leaving poor countries behind. Without global trade, it will be impossible to put development and poverty reduction back on track.

But the world needs a different, reimagined type of trade, because not all people and not all countries shared adequately in the progress of recent decades. Although the overall trends were impressive, the top-line numbers hid a darker story. Many poor countries—most notably in Africa—lagged behind their counterparts elsewhere, even during the pre-pandemic era of convergence. Many poor people and regions in rich countries also lagged behind, since the opportunities created by better access to international markets were not always, or not often, in the same regions or sectors hurt by attendant import competition.

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Even as economic inequality declined between countries and across the global population as a whole, inequality within many advanced economies increased. Trade was one of several factors at play, including technological changes that favored skilled workers and replaced many manufacturing jobs with machines. Tax, labor, and antitrust policy choices also shaped these changes, which is why inequality increased much more in some countries than in others. When the financial crisis and the painfully slow labor-market recovery that followed fed populist extremism, trade and immigrants became easy scapegoats. The political disruptions of recent years underscore the importance of cushioning the impacts of trade and technological changes on people's lives and livelihoods. By introducing active labor-market and social policies, governments can ensure that the gains from trade and technology are broadly shared while their disruptive effects are softened.

There is surely scope to bring more people and places from the margins of global production and trade networks to the mainstream. This is already starting to happen. Multinational companies are diversifying their supplier bases in pursuit of cost savings and better risk management. Bangladesh, Cambodia, Morocco, and Vietnam are expanding their participation in regional and global value chains. From Barbados to Bali to Ohio, remote services work is creating opportunities and breathing new life into struggling communities.

Taking this reglobalization process further to encompass more places and draw in more small and women-owned businesses would yield considerable dividends. It would promote growth and reduce poverty in the parts of Africa, Asia, and Latin America that have good macroeconomic and business environments but weak connections to the most dynamic sectors of the global economy. It would lead to greater socioeconomic inclusion for sections of society that typically register higher rates of poverty and underemployment. And it would increase the depth, security, and flexibility of supply chains.

A strong, open, multilateral trading system is necessary for this potential next wave of trade-driven growth. But reglobalization will look different from the export-led industrialization that transformed East Asia. With advances in automation making manufacturing a somewhat weaker engine for job creation than it used to be, services will have to play a major role alongside manufacturing and agricultural production and processing. Services are increasingly important drivers of growth and trade, expanding faster than trade in goods. This is especially true for services delivered digitally—everything from streaming games to consulting by videoconference. Cross-border trade in these services grew by an average of 8.1 percent between 2005 and 2022, compared with 5.6 percent for goods. In 2022, digitally

delivered service exports reached $3.8 trillion in value, equivalent to 12 percent of all goods and services trade, up from eight percent a decade earlier.

To support this process of reglobalization, the international trade regime will need to adapt by setting forth clear rules on digital trade and promoting deeper cooperation on services trade. Gaps in existing trade rules—or the absence of shared global rules altogether—result in uncertainty and transaction costs that weigh heaviest on smaller businesses. Members of the WTO have been taking steps in the right direction. In 2021, a group of members accounting for over 90 percent of global trade in services struck an agreement on reducing regulatory barriers to services trade, and nearly 90 members, including China, the United States, and the European Union, are currently negotiating a basic set of global rules for digital trade. Regional initiatives to lower trade barriers and build connective infrastructure, such as the African Continental Free Trade Area, are also useful.

Finally, maintaining peace and security is particularly salient these days. The increasing weaponization of trade relations and policy has cast doubt on the long-standing proposition that trade brings peace. Countries are understandably worried about becoming dependent on potential adversaries for critical goods. But as has been made clear, limiting trade to a few partners comes with opportunity costs: higher prices, diminished export options, less productive resource allocation, and new kinds of supply vulnerabilities.

Meanwhile, deep and diversified markets make it harder to weaponize international trade, by reducing countries' dependence on any single source of supply. When the war in Ukraine cut off nearly all of Ethiopia's wheat imports from that country, Ethiopia was able to fill the gap with imports from Argentina and the United States. Europe has made up for the loss of piped Russian gas with imports of liquefied natural gas from other sources. In a reglobalized world economy, a diffuse production base for all manner of goods would mean even fewer potential chokepoints. One prerequisite for reglobalization is a broadly open and predictable global economy, anchored in a strong, rules-based multilateral trading system.

A FORCE FOR PEACE

International trade is neither the silver bullet that can solve all security problems nor the Achilles' heel of the current security architecture. To abandon the many benefits that come with international trade would be foolhardy. There are real problems with the current trading system, but the counterfactual scenario is almost certainly worse: it is difficult to believe that international security would be better served if leading powers had no economic stake in one another's stability and prosperity and no shared institutions in which to engage. Trade between the United States and China benefits people and businesses in both countries enormously and binds the superpowers together, both bilaterally and in international forums, providing an incentive to cooperate where possible and avoid conflict.

Strategic competition is a reality of the modern world. But that world will become unlivable unless there is also strategic cooperation. The WTO's ministerial meeting last summer offered hope that the two can go together. The agreements reached there had the support of

all WTO members. They worked across geopolitical and policy fault lines, each perceiving a national interest in reinforcing the world trading system.

In the three-quarters of a century since the world first embraced multilateral cooperation on trade, the trading system has underpinned rising—if still uneven—global prosperity. It has achieved its original goal of helping governments keep markets open in turbulent times. In the face of mighty shocks, from the global financial crisis to the pandemic, the world did not repeat the 1930s spiral of protectionism and depression, instead allowing cross-border demand and supply to be an engine for recovery.

Today, the multilateral trading system is part of the solution to major global challenges, from climate change to conflict to pandemic preparedness. And a reformed WTO, fit for the twenty-first century, is needed now more than ever, with rules that underpin the stability, predictability, and openness of the global trading system. If the past 15 years have taught us anything, it is that unforeseen crises surely lie ahead and that without the stabilizing force of trade, the world will almost certainly be less able to weather them.