

# Challenges for building a multilateral trading system in the 21<sup>st</sup> century

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# Challenges for building a multilateral trading system in the 21<sup>st</sup> century

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This policy paper reflects discussions of the CEBRI-KAS Project on the future directions of multilateralism.



# Introduction

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The Covid-19 pandemic has intensified the debate on cooperation and governance in the global economy created after World War II and institutionalized through international organizations guided by the multilateral principle.

In the field of trade, the post-war multilateralism was seen as a non-discriminatory treatment in trade relations between countries and a negotiation of rules by consensus. Exceptions to this principle and moments of crisis were part of the history of global trade governance. However, the 21<sup>st</sup> century is witnessing a crisis that raises questions about the survival of the multilateral principle and the functionality of the World Trade Organization (WTO), the guarantor body of this principle.

There are multiple reasons for the crisis (Pereira, 2020). Firstly, the partial identification of multilateralism with the Western liberal economic order. In this case, China's rise and its failure to "unrestrictedly adhere to that order" is the source of trade tensions. Another reason is related to the emphasis given to the WTO reform in order to accommodate negotiations involving 164 members with different priorities and the inclusion of new topics such as the digital economy, e-commerce and pending issues, such as services. The current system of multilateral governance is not adequate to address these new issues. The issues are not mutually exclusive. However, if the multilateral principle is identified as the institutionalization of deliberative spaces that accommodate the plurality of opinions and identities, the theme of multilateralism goes beyond the issue of the WTO reform<sup>1</sup>. Multilateral spaces of varying numbers of countries and themes may be considered and the question of whether or not they will be part of the WTO's institutional framework is another issue.

The objective of this article is to expand some points analyzed in the Policy Note written by the author (Pereira, 2020). Therefore, some of the premises and analyses already described in that

text were reproduced here, such as the following paragraph.

"Several authors (Gilpin, 2001 and Rodrik, 2011) consider that the multilateral system within the scope of the international political economy has been in crisis since the late 1990s. The main issue for these authors is the relationship between international/multilateral regulations and the interests of states. This is an issue that is present throughout the debate on the multilateral system. As Fonseca Jr. (2008) observes, a system of multilateral rules presumes a balance between the national interest and the collective rule. The collective rule may reflect the interests of the hegemonic state in terms of political and economic power, but there must be a real or constructed perception so that other countries do not perceive it as violating their national interests" (Pereira, 2020 p. 4).

This article is structured as follows. We analyze the main issues that guide the debate on the multilateral crisis. The first section addresses global trade governance between 1950 and 2000. The second section analyzes the issue of multilateralism in the 21<sup>st</sup> century. The third section highlights the main topics regarding the WTO reform and the fourth section concludes with the possible scenarios proposed and considerations about this debate for Brazil.

We start from the premise that a look at the past helps understand the almost consensual hypothesis that the multilateral system in the 21<sup>st</sup> century requires new negotiating arrangements and pacts. However, there are disagreements regarding the content of this proposal. The purpose of this article is to analyze these differences and propose possible scenarios for 21<sup>st</sup> century multilateralism.

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1. Lima and Albuquerque (2020) quote Milani's assessment on the role of multilateralism.

# 1 The global trade governance between 1950 and 2000

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According to Lavalle (2020), multilateralism is not an ideological aspiration, but a pragmatic method for dealing with issues of interdependence and economic and security coexistence between countries. However, in the analysis of the governance of international organizations it is necessary to start from the observations of Gilpin (2001). Governments define the rules of functioning of their domestic markets according to their objectives, institutional frameworks and demands from sectors of society regarding the role of the state. These factors define national systems of political economy. The Bretton Woods multilateral system was a construction of coexistence of national systems of political economy where there was a set of interests and common values between the hegemon, United States, and Western European economies (Pereira, 2020, p.4). A brief history of the multilateral trading system illustrates these issues.

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## FROM 1947 TO 1980

The underlying motivations of the guiding principles in the constitution of multilateralism in the governance of global trade help understand its later history and its crises.

The creation of a multilateral organism based on liberal principles defended by American and British negotiators derived more from political and strategic motivations than from economic calculations based on advantages derived from free trade (Finger, 1986). In addition, we note that historically American society has favored liberal principles over policies of direct state interference in the economy. From the point of view of immediate interest, however, the tensions between the United States and the Soviet Union promoted the American position in the defense of commercial liberalism. The strategy of consolidating commercial ties between allied partners and, thus, strengthening the growth of market economies was a defense mechanism

against possible Soviet advances towards new areas of influence.

Another point refers to the selection of the principle of multilateralism in world trade. This can be explained by the very form of insertion of the United States in the world political and economic scenario. While European countries had a long history of forming preferential ties with each other or with their former colonies, the consolidation of the United States's leading role theoretically required the multilateralization of political and trade relations.

The global trade governance proposal presumed the creation of an international organization, the *International Trade Organization* (ITO). This, however, never came into force.<sup>2</sup> In the absence of ITO, the General Agreement on Tariffs and Trade (GATT) became the benchmark for multilateral trade relations.

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2. The American Congress did not approve the Charter in 1948 and, motivated by the perception that it was extremely unlikely to approve it, in 1951 the Executive branch announced that it would no longer submit it for approval.

The agreement's structure highlights the "pragmatism" of multilateral negotiations. The guiding principle was the Most Favored Nation Clause, which guaranteed non-discriminatory treatment in trade relations, that is, multilateralism. At the same time, GATT's Article XXIV admitted the formation of preferential areas of trade by recognizing the possibility for countries to negotiate free trade areas and/or customs unions; a necessary exception to include the interests of European countries and their ties to former colonies, pragmatic multilateralism.



The underlying motivations of the guiding principles in the constitution of multilateralism in the governance of global trade help understand its later history and its crises.



According to Pereira (2020), "there is a relative consensus in the literature on the apparent success of the multilateral system between 1950 and the mid-1970s. The Cold War subjugated the interests of the United States' commercial policy to the interests of its foreign policy. When politically strong domestic sectors felt threatened, solutions were offered, even if they went against the rules of the GATT system, as was the case of the exclusion of the agricultural sector from negotiations", that should cover all global trade without adopting quantitative restrictions.

At the same time, the United States and the European countries accommodated the interests of agricultural exporting developing countries by accepting a greater degree of flexibility than the GATT rules allowed. An example was the policy of import substitution from Latin countries, which violated the rule of prohibiting quantitative restrictions. It was more important to secure countries' adherence to the Cold War than questions about commercial issues. Countries were participants with a low degree of influence on world trade.

## THE 1980'S MULTILATERALISM CRISIS

At the end of the 1970s and during the 1980s, the developed countries applied several quantitative protectionist practices bilaterally<sup>3</sup>, countering GATT's principles.

During the same time, the European Single Market project for 1992 was launched, trade and investment ties between Asian countries intensified, led by Japan, and the United States began to use its trade legislation unilaterally to determine what it considered "unfair behaviors" of the partners.<sup>4</sup>

GATT was in crisis and the world was fragmenting from three axes from a trade perspective: United States, the European Union and Japan.

There are several reasons for what is conventionally called "the new protectionism", but the following stand out: changes in the distribution of comparative advantages between countries; the weak performance of most developed countries during the 1980s; macroeconomic imbalances; the entry of newly industrialized countries into the global trade of manufactured products; and the end of the United States' hegemonic position in global trade with the rise of Japan.

Between 1980 and 1987, the United States' trade deficit increased from US\$ 25.5 billion<sup>5</sup> to US\$ 159 billion. The appreciation of the dollar driven by the rise in the United States' interest rate in the first half of the 1980s and the expansionary fiscal policy were the main macroeconomic reasons for this result. However, the Reagan administration's discourse was that the deficit reflected "unfair trade" and the small adherence of partners to the rules of the multilateral system. The main target was Japan, but countries like Brazil and India were also identified as *free riders* in the multilateral system.

At the same time, the 1980s marked the beginning of the second globalization wave (Irwin, 2020 and Janeway, 2020) driven by new information technologies, communications technologies and the growth of new areas such as biotechnology. The expanded range of marketable products and services reduced transportation and communication costs. In this context, the agenda for the multilateral system proposed by the United States and endorsed by the QUAD<sup>6</sup> was composed of two themes.

The first refers to the inclusion of new topics - services, investments and intellectual property rights - in the negotiations that would allow the advancement of the integration of global trade. The central issue was to ensure a scenario of harmonized rules in global trade to reduce the transaction costs of the new wave of globalization.

The second refers to the preservation of the multilateral system that required full adherence by the members to the agreed rules in order to curb the behavior of *free riders*<sup>7</sup>.

The discourse of the United States' trade policy in the 1980s did not condemn the multilateral system, what it demanded was a revision of the rules to serve the American interests and discipline those they saw as "unfair competitors". Although Japan was sometimes described as a threat, it accepted US rules and, from 1990, it went through a crisis and left the country's priority trade agenda.

3. The main instrument were the voluntary export restrictions (Pereira, 2018).

4. The number of investigations on dumping and countervailing duties increase and voluntary export restriction agreements were mainly directed to Japan but also reached other countries, such as Brazil in the case of steel products. In addition, Section 301 is expanded and allows the Executive to impose unilateral sanctions in the event that US interests in services, intellectual property, investments, among others, are considered harmed.

5. The highest deficit registered before was US\$ 33 billion, in 1977.

6. The QUAD, composed by the United States, the European Union and Japan, was the group identified as the main core to form consensus in the GATT negotiations.

7. *Free riders* correspond to countries that benefit from greater access to markets through tariff reduction negotiations, but do not offer reciprocity, i.e., more favorable conditions for entering into their markets.

## THE 1990's AND THE BIRTH OF THE WTO

According to Pereira (2020), “the Uruguay Round of negotiations coincides with the fall of the Berlin Wall, the end of the Soviet Union and the adoption of programs of trade and financial liberalization and privatization in several developing countries, as those in Latin America. There were advances in negotiations on regulatory issues and the World Trade Organization was created, which was hailed as a sign of the strengthening of multilateralism.”

However, the 1990s already signaled the limitations of the Bretton Woods system to address new trends in global trade. The increase in preferential trade agreements that began in the 1980s is intensified, even with the creation of the WTO, which would be a permanent negotiating forum. How to explain this trend?



Therefore, in the 1990s it seemed that a new era had begun in the global trade governance system. The issue of agreements as *building blocks* or *stumbling blocks* for the multilateral system seemed to be overcome with the creation of the WTO.



For Bhagwati (2008), the propositions for preferential trade agreements in the United States, starting in the late 1980s, reflected the demand for negotiations that more comprehensively met the country's sectorial interests.<sup>8</sup> According to the author, especially regarding new topics (services, investments and intellectual property rights), the preferential agreements allowed the United States to influence rules that were not met at the multilateral level. The ultimate goal would be to multilateralize these rules.

In the case of Latin America, the topic of open regionalism was included in the new trade policy guidelines. Preferential trade agreements, such as Mercosur, were based on the premise that the objective was to strengthen the regional space in a context of greater integration with global trade. The agreements should promote reduction in protectionist practices and adherence to the rules of multilateral organizations.

Therefore, in the 1990s it seemed that a new era had begun in the global trade governance system. The issue of agreements as *building blocks* or *stumbling blocks* for the multilateral system seemed to be overcome with the creation of the WTO. From the point of view of market rules, the world was integrated with the end of the Soviet Union.

This, however, is a reading that ignores the late 1990s, when the issues of the 21st century debate on multilateralism were already emerging in the global context.

8. In this case, in addition to the negotiation of the North American Free Trade Agreement that included Canada and Mexico, it was proposed the Initiative for the Americas, in 1990, and then the Free Trade Area of the Americas, in 1994.



## 2 Multilateralism in trade in the 21<sup>st</sup> century

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The idea that the multilateral trading system was outdated in relation to the transformations brought about by the new technologies, the new forms of production organization (the global value chains) and the new themes of the global agenda were already present since the end of the 1990s. At the same time, commitments required by the rules of the Uruguay Round were understood as restricting the freedom of national economies, especially by developing countries in choosing strategies for their development. In addition, commodity-exporting developing countries demanded the completion of the pending agenda for the liberalization of world agricultural trade.

**T**he WTO's Doha Round, launched in 2001, was announced as the "Development Round" and should meet this broad agenda. The impasse in agricultural negotiations paralyzed the process in 2003 and in 2008. However, the central issue for the multilateral system was the growing consensus that the system needed to be "updated", which incorporates several interpretations.

### The debate on multilateralism in trade encompasses two perspectives:

One of them focuses on the international political economy and analyzes the subject based on the changes in national states' positions in the world economy and the forms of organization adopted for the expansion of trade and the internationalization of production.

**THE QUESTION THAT ARISES IS:** Do the changes that occur in the topics referred to in the 21<sup>st</sup> century allow the construction of a common multilateral negotiating space, such as the one that prevailed after World War II? What are the possible arrangements?

The second perspective focuses on the topic of the WTO reform to respond to these new challenges, which is the topic of the third section.

**THE QUESTION IS:** What needs to change in the institution's way of negotiating in order to accommodate these changes?

The issues are not mutually exclusive, but to consider them separately helps build the possible scenarios for the 21<sup>st</sup> century multilateralism.

## CHANGES IN THE DISTRIBUTION OF POWER IN GLOBAL TRADE AND IN PRODUCTION ORGANIZATION

### The rise of China

China entered the WTO in 2001 and has since increased its participation in world trade from 4.3% to 13.2% between 2001 and 2019.<sup>9</sup> In the same period, the United States' share fell from 11.8% to 8.7%. These changes show that Chinese gains were achieved by expanding the country's trade with the world, which led the country to the position of largest world exporter and second importer.

The topic of China's rise has been analyzed mainly based on conflicts with the United States. Despite the Trump administration's rhetoric identifying China as a communist enemy, there is a degree of consensus among American international relations scholars that the issue is not ideological. As Colby and Kaplan (2020) point out, even if China was a democracy, its rise and the possibility of the country being the regulating and determining pole of Asia's technological standards, would lead the United States to react. The country does not accept to be removed from the Asian market.

Another perspective criticizes the Trump administration's decision to leave the Trans-Pacific Partnership that could compel Beijing to be a "rule-taker" instead of a "rule-maker".<sup>10</sup> In abandoning this project, the United States has to accept the idea that spheres of influence are part of the new geopolitics (Allison, 2020). This analysis assumes that changes in the direction of the United States' policy can reverse this situation.

Similarly, though demanding a permanent change in the United States' position, other analysts defend the idea that the country must accept that it no longer leads all areas of influence in the world.<sup>11</sup> In this case, the multilateral system is fragmented by topics and the interests of states.

Xuetong (2019) agrees that the core of the United States-China bipolarity issue is not ideological. In addition, neither country has a global narrative or vision of a new international order, as happened when the post-war multilateral system was created. The author considers that the main competition between the two countries is and will continue to be for some time, over consumer markets, technological advantages, investment rules, exchange rates and intellectual property rights. In this case, the bipolarity in terms of adherence to one or another power is not clear. China supports the strengthening of the multilateral system like the European Union and other countries, but it does not mean that its proposals are always aligned with these players in relation to all the topics of negotiation.<sup>12</sup> According to the author, the scenario would continue to be one of tensions focused on specific points.

### Regulatory standards

The transformations brought about by new technologies lead to competition for technological leadership and, in association, to the definition of regulatory standards. It is not just about new technologies, but about standards related to topics that have become part of the global agenda, such as climate change and, nowadays, public health.

With the fall of traditional border protection measures over the years, trade negotiations are dealing with regulatory standards. These reflect society's values and choices and demand negotiations that escape the "mercantilist spirit" of trade in accessing markets (Lamy, 2015). An issue that is clearly present in the negotiations on phytosanitary standards in the agricultural sector, where there is often a gray area to limit the use of some types of pesticides, for example.

9. WTO Database.

10. The Trans-Pacific Partnership encompassed Brunei, Chile, New Zealand, Singapore, Australia, Canada, Japan, Malaysia, Mexico, Peru, the United States and Vietnam. In 2017, the United States withdrew, but other countries closed negotiations in 2018.

11. See Krasner (2020).

12. The author also makes a distinction between security and commercial strategic interests in the countries' alliances with China and the United States.

In the case of climate change, despite the growing consensus on the issue's relevance to ensure sustainable development, its inclusion in trade agreements and in the WTO is questioned by several countries.

In the field of new technologies, the clash between China and the United States reflects the race for defining new standards and norms, as is the case with 5G. For Xueting (2019), as technological innovation becomes the main driver of wealth accumulation, it is inevitable that countries intensify measures to protect their intellectual property rights and do not abdicate of how they wish to stimulate their innovation capacity.

Rodrik (2020), when analyzing the case of Huawei, defends a posture compatible with his analysis on the globalization paradox. For him, any trade governance system must balance the gains from harmonization of rules with the gains in regulatory diversity defined by the national policies of each state. In this case, the United States has the right to close its market for Huawei, but cannot impose its restrictions on other countries.

The balance proposed by Rodrik (2011) is based on his analysis of the globalization paradox. Full globalization requires harmonization of rules to facilitate the flow of goods, services and regulatory frameworks that ensure investors' rights in terms of legal protection and intellectual property. The discussion is not new and was already present in the 1990s, but has intensified with the expansion of global value chains.

Baldwin (2012) defends a WTO review based on the adhesion of those who so desire for the set of rules that would minimize transaction costs for the operation of global value chains. For Rodrik, the harmonization of rules limits the options of national policies and reduces the degree of freedom of governments to meet the demands of sectors within their society. In an ideal world, harmonization or a greater degree of regulatory convergence should be accompanied by "supranational governance" that would implement the necessary compensatory policies to mitigate adjustment costs. As this scenario is not part of a predictable future, it is necessary to balance the degree of globalization (or regulatory convergence/harmonization) with the degree of freedom for the states.

According to Pereira (2020), "the Covid-19 pandemic brought up abruptly the debate about globalization expressed in the interdependence of global and regional value chains. The topic of chain decoupling, especially in the relationship between the United States and China, gained priority (...). Total decoupling of the interdependence of trade flows along the production chains is unlikely in the short or medium terms. There are impacts on production costs and it requires changes in consumer preferences. However, measures to stimulate policies to diversify the origin of imports and increase national chains in sectors that have come to be considered strategic, such as public health, can be expected."

We believe that this is the main challenge for the governance of the current multilateral trading system. The reconciliation of the collective rule with national interests does not depend only on the member's perception that their interests are not being violated by the hegemonic nation. In the current world of commerce, the distribution of power tends to be multipolar.

Therefore, reaching a balance that ensures coexistence with different hubs of technological leadership and an expressive presence in the same space of the world economy will not be a trivial task. The issue of trade conflicts with China is not exclusive to the United States. A balance of the interests of the United States, China and the European Union in the field of trade is a necessary condition. In addition, it is necessary to ensure that the interests of developing countries are represented as well.

# 3 The WTO Reform

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Has the multilateral trading system failed? We argue that the focus of the debate should shift from “the death of the World Trade Organization” to analyses and proposals that support updating the WTO for the 21<sup>st</sup> century. We base our premise on the principle that multilateralism must continue to be the foundation of trade governance. Similarly, Woods (2020) argues that multilateral organizations are not collapsing, but changing. It is noteworthy that China’s objective is to increase its degree of influence on organizations, especially because its growth has benefited from existing structures.

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## THE WTO’S PILLARS

WTO governance is based on three pillars: negotiator, dispute settlement and monitoring.

### The Negotiating Pillar

#### A) A variable geometry of interests and groups of countries in forming consensus

The WTO negotiating process through consensual decision is no longer functional for the multilateral system. It is difficult to form consensus with 164 members and assume that rules will be multilateralized for countries with different interests and different degrees of development. The principle of *single undertaking* defended as the way to guarantee the balance of negotiations ended up being one of the factors that contributed to the stagnation of the Doha Round. What has changed?

In the Uruguay Round, QUAD countries (United States, European Union, Canada and Japan) were the protagonists in building consensus in the negotiations. The 5<sup>th</sup> WTO Ministerial Conference held in Cancun in 2003 marked the end of QUAD. The attempt by the United States and the European Union to repeat their Uruguay

Round behavior with the presentation of a closed agreement in the agricultural area was rejected by a group composed of 20 developing countries with different interests in agricultural negotiations. Brazil was part of this group with offensive agricultural interests in terms of opening markets and China and India had defensive interests. In common they had a proposal for agricultural liberalization that addressed the interests of the main developing countries. Coalitions with variable geometry of countries according to thematic interests are formed and start to coexist in the WTO.

The principle of *single undertaking* as a measure to guarantee the balance in negotiations needs to be rethought. In the Doha Round, difficulties in the agricultural negotiations halted the progress of all other negotiations. In practice, the principle was abandoned with the signing of the Trade Facilitation Agreement in 2013.

## B) The Most Favored Nation (MFN) Clause and the plurilateral agreements

Several experts support the idea that the multilateral system can proceed with plurilateral agreements. The MFN principle has not been abandoned, but different forms of plurilateral negotiations are allowed (Mesquita, 2020 and Schneider-Petsinger, 2020).

As the authors point out, there are different types of plurilateral agreements within the WTO. According to Mesquita (2020), the first type, guarantees MFN treatment to all WTO members. In this case, to avoid problems with *free riders*, the agreements must be signed by a “critical mass” of members, between 85% and 90%, related to the negotiated topic. The Information Technology Agreement is an example in which all rights granted by participants can be extended to non-participants. It is necessary to note that for the fulfillment of these agreements it is essential that the main players in the negotiated market are part of the agreement.<sup>13</sup>

In the second type of agreement, such as the Government Procurement Agreement, members, by consensus, accepted that the rights and obligations assumed therein are limited to participants.

As Mesquita (2020) points out, in the case of plurilateral agreements under negotiation (investment facilitation; services domestic regulation; trade facilitation for small and medium-sized enterprises; or electronic commerce), the issue arises in different ways in terms of critical mass participation, which may influence the negotiation’s final format.

## C) Special and Differential Treatment

In 1964, a new chapter/section was introduced in the General Agreement on Tariffs and Trade (GATT), which dealt with developing countries and recognized that they were exempted from granting reciprocal concessions in negotiations - the principle of “*less than full reciprocity*.” In the

Tokyo Round (1973/1979) the principle of “*Special and Differential Treatment*” (SDT) for developing countries (DCs) was consolidated.

Countries have the autonomy to request or waive SDT, that is, to declare themselves as developing countries. The diversity of members of the DC group, which includes China, has raised criticism especially from the United States, who proposes the definition of rules to identify the group of DCs.<sup>14</sup>

The WTO has sought to respond to this issue as shown in the 2013 Trade Facilitation Agreement, where concessions are not based on DCs, but on voluntary offers made by member countries in relation to the terms of the agreement: full membership, transition period and, time for transition and technical assistance. In this case, both China and Brazil have chosen to give up SDT.

Instead of proposing general classifications, commitments by agreement may be the solution. In addition, if the trend towards plurilateral agreements persists for specific topics, this issue tends to be resolved according to the interests of each country.

In short, the MFN clause continues to be the WTO’s negotiating pillar, but plurilateral agreements should be encouraged to unlock the negotiations, especially in the case of novel topics. In addition, negotiations that necessarily need full adherence of obligations by WTO members can be distinguished, and therefore assume MFN clause, from those that can be fully multilateralized but start with a plurilateral negotiation.

## The Dispute Settlement Pillar

The new design of the Dispute Settlement System is considered one of the main contributions of the Uruguay Round of negotiations. It allowed for disputes between countries with a high degree of asymmetry in terms of economic power and participation in world trade to resolve their differences based on WTO rules.

13. Mesquita (2020) draws attention that in the plurilateral agreement on electronic commerce, although the critical mass has reached around 90% and 84 members, India does not participate, despite its importance in this matter.

14. The United States has defined a set of rules for a country to be excluded from the group of developing countries: belonging to the Organization for Economic Cooperation and Development; belonging to the financial G-20; being in the World Bank’s high-income group of countries; and having a share of at least 0.5% of world trade.

According to Lafer (2020), “the pillar of the dispute settlement system was very successful. It was widely used and, as a consequence, provided a significant addition to the WTO’s “living law” jurisprudence.” This is the problem as pointed out by several authors (Esserman and Howse, 2003).

The United States has paralyzed the functioning of the Appellate Body by blocking the appointment of new members or their renewal since mid-2017.<sup>15</sup> It is important to note that the efficiency of the dispute settlement system presupposes that the normative function of the WTO is operative so that the “dispute” is resolved based on what WTO members have agreed on in their negotiations. It is not its job to create jurisprudence and, in this regard, other countries also show concern for the functioning of the system and proposals for its reform. Until a consensus is reached on the mechanism’s reform, the European Union has proposed, with the adherence of 14 countries, the creation of a “Multi-party Interim Appeal Arbitration Arrangement” to fulfill the role of the Appellate Body.<sup>16</sup> It is noteworthy that of the 14 countries involved, seven are in Latin America, including Brazil, which reinforces the importance of the multilateral system for the region.

## The Monitoring Pillar

The WTO is not a global policeman, but it must advise its members through the disclosure of reports on their respective practices in relation to the topics contemplated by the organization. The *Trade Policy Mechanism Review* fulfills this role. However, it is necessary that member countries are active in notifying adopted measures. Transparency and monitoring help create a stable scenario in global trade.



The WTO is not a global policeman, but it must advise its members through the disclosure of reports on their respective practices in relation to the topics contemplated by the organization.



## THE WTO AND THE CHALLENGES OF 21<sup>ST</sup> CENTURY MULTILATERALISM

The multilateral system must advance and not be paralyzed by the clash between China and the United States, which goes beyond the scope of the WTO and which will surely endure in a horizon full of uncertainties. And here, the European Union and the main Latin and Asian economies can lead this process.<sup>17</sup>

A change in the US government’s stance in favor of the multilateral system would help in this process, as well as China’s commitment to abide

by rules agreed upon its entry into the WTO.

China, however, has been active in formulating proposals for the WTO reform but refuses to be treated as a developed country, insisting on the maintenance of the “indelible clause” that gives it the right to special and differentiated treatment. From our point of view, and based on Rodrik’s analysis, China wants to ensure greater freedom in the implementation of its policies, especially in terms of promoting technology and financing.

15. Each member of the Appellate Body has a 4-year term that can be renewed. With the United States’ blockage, in December 2019, it lost the quorum of at least three members so that it could work.

16. In addition to the European Union, the following countries endorsed the creation of the temporary mechanism: Brazil; Canada; China; Chile; Colombia; Costa Rica; Guatemala; Hong Kong; Mexico; New Zealand; Norway; Singapore; Switzerland; and Uruguay.

17. See the webinar “Crise e Governança Global” promoted by CEBRI and the Konrad Adenauer Foundation with the participation of the European Commission’s representative to Brazil, Ambassador Ignacio Ybáñez: <https://www.youtube.com/watch?v=glXSXe69z9k>.

The label of “developing country” in commercial multilateralism guarantees this degree of autonomy. Plurilateral agreements and with variable geometries of topics and components may enable accords where exceptions and transition periods are negotiated in a more balanced way.

The 2008 crisis made the world’s main economies pursue a common agenda, through the G-20, in order to mitigate the damages caused by the financial crisis. In that scenario, the proposals led by the BRICS (Brazil, Russia, India, China and South Africa) for reforms in multilateral organizations gained prominence, although little progress was made after the peak of the crisis had passed. However, during the height of the 2008/10 crisis, governments honored their commitment not to repeat 1929, when protectionist policies, competitive exchange devaluations, fiscal and monetary restrictions prevailed.

The current crisis associated with the Covid-19 pandemic is not comparable to that of 2008. In addition to the tragedy of deaths caused by the virus, it poses challenges for the formulation of policies that ensure the livelihood of the most fragile groups in face of the paralysis of major economic activities. In the statement released by the financial G-20 at the March 26 meeting, countries declared their commitments: to protect lives; guarantee people’s jobs and incomes; preserve financial stability; rekindle growth; minimize interruptions in international trade; aid countries in need of assistance; and, coordinate public health and financial measures. The letter of intent is positive, but the agenda for how these objectives will be accomplished is missing.

Post-World War II Europe defended the topic of food security that allowed the exception in the GATT text in terms of quantitative restrictions for the agricultural sector. Subsequently, the United States was able to exempt the quota elimination obligations of the sugar sector and, finally, the entire agricultural sector was left out of the multilateral negotiations until the Uruguay Round.

There is a risk of intensification of protectionism even after the pandemic is gone. The pandemic, which is by definition a global problem, requires common responses and cooperative environments. However, if cooperation efforts in the scientific arena are taking place, it is not clear how countries will understand the expansion of their protection networks in the health sectors and the possible expansion of the concept of “strategic security”.

The multilateral system is crucial to ensure that temporary restrictions associated with combating the pandemic are eliminated and to discipline the scope of “new strategic security areas”. The pandemic has exposed inequalities within domestic spaces and between countries. Trade financing packages and expansionary fiscal policies mitigate crises in developed countries. The WTO, through its discussion groups on trade financing and support for small and medium-sized enterprises in developing countries (considering their diversity), has a new task to fulfill.

Finally, the WTO has to enter the debate on the distribution to all countries, without the charge of patent rights, when the vaccine against Covid-19 is discovered. How private laboratories will be compensated is an issue to be faced. In addition, it is necessary to support initiatives aimed at strengthening the multilateral system, based on an updated view that includes topics such as sustainable development and the digital economy.

## 4 Additional remarks

The WTO is a space for negotiation and its rules reflect the interests of its member countries. The world is going through a period of transformation and great uncertainty. The reform of the WTO's negotiating pillar requires a commitment to the rules in the dispute for leadership in defining technological standards and regulatory convergence on issues such as services, investments, and subsidies, among others. In addition, it also presupposes a consensus on new topics related to sustainable development so that issues such as climate change and public health security measures that affect trade in goods and services are part of the multilateral agenda.

Can issues such as trade agreements contribute to sustainable development? How to ensure a mode of production that warrants the transition to low-carbon economies? Should these topics be part of the trade agenda?

Even if the pace of globalization is reduced in terms of trade and investment flows, these issues are part of global trade. Countries trade what they produce and, therefore, their exportable supply reflects ways of dealing with sustainable development issues.

These questions are inserted in the possible scenarios regarding the new global order. Feroci et al. (2020) propose three basic scenarios for the global order that are not exclusive to trade:

i) Fragmentation of the global order described with a scenario with different zones of influence. These zones would tend to go "inward" and would use a weakened multilateral system when needed. This is the most likely scenario, according to the authors.

ii) The resurgence of Western power, with a change in Washington's orientation, renewing its commitments to multilateral organizations. However, as the authors and Schneider-Petsinger (2020) point out, when analyzing the topic of trade multilateralism, an alignment between the United States and the European Union is a necessary but not sufficient condition. It is not possible to ignore the Asian axis, especially the role of China.

iii) A new multilateralism for the 21<sup>st</sup> century built from coalitions of states, non-governmental organizations, regardless of their political affiliations, but with a progressive bias in terms of thinking the world in global terms. In this case, there is no single standard, but agreements of varying geometry depending on the different objectives.

Pereira (2020) proposed similar scenarios when analyzing the topic of world trade governance.

### **i) Fragmented regulatory framework systems**

In this world, China, the United States and the European Union would be the pivots for the definition of regulatory frameworks for their regions. The possibility of an agreement between the European Union and the United States is not ruled out. There is an assumption that China would get all partners in the Asian region to join, which is not trivial.

A totally fragmented world requires changes in communication and business strategies. Gains in scale economies would be revised and the concentration of income at the global level could be accentuated.

However, studies on the total "decoupling" of Chinese and American ties show that this strategy is not easy and has high costs for both countries. It also makes no sense to isolate innovation systems (Farrel and Newman, 2020). Furthermore, as Pereira (2020a) analyzes, the degree of interdependence between China and the United States in the financial field has increased.



## ii) Selective fragmentation

A “less drastic” scenario would be the fragmentation of regulatory frameworks on specific segments, such as smartphone apps or other sectors where technology experts can make viability assessments.

In this fragmentation scenario, the multilateral system inherited from Bretton Woods is revised, which requires abandoning the unrestricted application of the most favored nation clause principle. In their place, plurilateral agreements will tend to be used more frequently in WTO negotiations. At the same time, formal and/or informal multilateral agreements can be signed in areas where the transit of people and the externalities brought about by the synergy of exchanging information and expertise are necessary.

This scenario depends, however, on a change in the United States’ confrontation policy towards China. And it supposes greater flexibility in WTO rules.

## iii) Global Commons in the multilateral trading system

For Rodrik (2020), the pandemic will favor the shift from an international system that privileged the “fundamentalism of the principles of market efficiency” to a system that reinforces the role of the state in promoting national interests. However, this role of the state should not be confused with mere state intervention in the markets, but with policies that favor the green economy, quality jobs and ensure the improvement in income distribution.

It is an optimistic scenario and presupposes a common effort by the states to face existing challenges and those brought to the center of the world economy by the pandemic. However, it is not yet clear if the multipolarity in the distribution of economic power can translate into a set of multilateral rules that accommodate the national interests of all countries.

What is the most likely scenario? In this world of uncertainty, stakes are “guesswork”, but scenario (ii) is feasible, as long as the dispute between the United States and China does not intensify.

## And what is the agenda for Brazil?

Brazil needs a multilateral trading system to ensure a favorable environment for its growth in global economy. Although China accounts for about 30% of Brazilian exports, the country has a diversified agenda in terms of interests and regions. It is necessary to build proposals that reflect the interests of the Brazilian sectors and encourage dialogue at the WTO. For example, initiatives such as the Punta del Este Group (2019). In this context, the project promoted by CEBRI (Brazilian Center for International Relations) and the Konrad Adenauer Foundation (KAS) is another important front that joins the efforts to preserve the multilateral system.

Alliances with Latin countries, which like Brazil have little bargaining power in world trade and favor the multilateral system, should be embraced. They also enable the formation of trade networks and production chains in a scenario of potential increase in protectionism across the world.

There is an expectation that with the Democratic victory in the US election, the country will again support the WTO. Even so, issues regarding changing rules in the Dispute Settlement System and the guidelines for the WTO negotiating process will remain on the negotiating table. Therefore, the construction of proposals for the WTO reform will continue a priority for those who understand the importance of the multilateral system for Brazil. In this context, it is necessary to identify the interests of the Brazilian sectors, as already mentioned, and consider that the alliances may have variable geometries. China is welcome to defend the multilateral system, but in matters of discipline of state-owned companies and subsidies, Brazil has greater affinity with the European Union, for example.

The world is going through a period of transformation and great uncertainty. At the moment, it is better to ensure the “possible WTO” than pursue the “ideal WTO”.

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The Brazilian Center for International Relations (CEBRI) is an independent think tank that contributes to building an international agenda for Brazil. For over twenty years, the institution has engaged in promoting a pluralistic and proposal-oriented debate on the international landscape and Brazilian foreign policy.

In its activities, CEBRI prioritizes themes with the greatest potential to leverage the country's international insertion into the global economy, proposing pragmatic solutions for the formulation of public policies.

It is a non-profit institution, headquartered in Rio de Janeiro and internationally recognized. Today, its circa 100 associates represent diverse interests and economic sectors and mobilize a worldwide network of professionals and organizations. Moreover, CEBRI has an active Board of Trustees composed of prominent members of Brazilian society.

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