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Reimagining trade: Can mutual benefit be restored?

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Trade has not been an idyllic panacea. No other single factor has driven greater gains in global economic development and rising standards of living.

Introduction

It is not an exaggeration to say that trade has transformed the world, especially during the latter half of the 20th century. In less developed countries, trade helped to lift hundreds of millions of people out of poverty. In developed countries, trade increased real income through access to quality products at lower costs. Of course, trade has not been an idyllic panacea. There have also been damaging dislocations and unfair practices that have not been adequately addressed. But overall, no other single factor has driven greater gains in global economic development and rising standards of living.

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Today, trade is under siege. Protectionist policies are on the rise. Global trade governance has been derailed. The two largest economies in the world remain locked in the most significant trade war in 90 years, while smaller trade spats are breaking out across the globe. The trade landscape looks like a battlefield.

We are approaching an inflection point. Trade cannot continue under these terms. If we hope to continue to derive transformative benefit in the decades to come, trade relationships will need to be reimagined. Our best path forward might be discerned by reacquainting ourselves with the principles that guided the establishment of our current global trade system seven decades ago. In particular, the seemingly outdated concept of mutual benefit needs to be revisited.

A system founded on mutual benefit

In the aftermath of World War II, the United States was in a position of unprecedented economic and strategic hegemony. It accounted for half of global GDP[1] and enjoyed a seemingly insurmountable technological and military edge. Yet the US sheathed its sword and attempted to make its power safe for others through the establishment of cooperative multilateral governance institutions. These included the United Nations, the World Bank, the International Monetary Fund, and the General Agreement on Tariffs and Trade.[2]

The Charter of the United Nations (UN) – the founding document of the UN – was signed by 50 nations on June 26, 1945 in San Francisco, and came into force on October 24, 1945.

Figure 1 – Major international organizations established post-WWII

United Nations (UN)	General Agreement on Tariffs and Trade (GATT)	International Monetary Fund (IMF)	Organisation for Economic Co-operation and Development (OECD)	World Bank

It opened its consumer markets and allowed war-ravaged economies from Europe and Asia to rebuild their economies largely on the back of exports to the US. It drove the construction of a rules-based trade system. It embraced trade rules that gave the little fish just as much power as the big fish. The US recognized that a sustainable trade system could not be built solely on the basis of US interests. The trade system needed to be built on the basis of mutual benefit.

None of this is to over-idealize the conduct and motivations of the United States. There is no shortage of examples of the US acting in duplicitous, self-serving, and hypocritical ways. Over the years, the US has been no less guilty of unfair trade practices than many other large trading nations. But it speaks volumes that the US' founding vision for the post-war trade system intrinsically recognized the need for others to benefit.

Importance of trust

Intentionally or unintentionally, this approach also produced an indispensable by-product: trust. Trust has been the invisible glue holding the global trade system together. Trust ensured a mutual buy-in into something larger than purely individual self-interest. It engendered a sense of common cooperative endeavor in which the interests of other parties were recognized and legitimized. These visionary foundational precepts laid the groundwork for the unprecedented trade-driven development that was to follow in subsequent decades.

Trust has been the invisible glue holding the global trade system together.

Today, those founding principles seem like quaint relics from a bygone era. Trade is now being pursued with a more adversarial, zero sum spirit than at any other time in the post-war era. In some cases, trade is even being wielded as a club to punish insufficiently malleable partners. The fact that the two largest economies in the world, the US and China, are also engaged in a mounting geo-strategic rivalry only heightens the adversarial atmosphere in the trade realm. But what has this approach wrought thus far? More importantly, where is it leading us in the future? It is time to consider whether some restoration of the concept of mutual benefit in trade is desirable and achievable.

A closer look at mutual benefit

The concept of mutual benefit in trade implies a recognition that the terms of the engagement must confer sufficient reciprocal benefit on your partner. One-sided trade agreements and one-sided trade relationships cannot work. Coercion, economic or strategic pressure, and unbalanced exploitation of comparative advantage will ultimately be unsustainable.

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Trade is a voluntary undertaking. The ideal should be to establish enduring relationships that are sustainable over time because they consistently and satisfactorily meet the needs of both parties. The relationship cannot be viewed as a series of one-off transactions that can somehow be "won". Access to the global trade system cannot be viewed as a one-way street in which benefits flow in only one direction.

A wider definition is needed

Importantly, the concept of mutual benefit in trade needs to be broadened beyond simple economic terms. Trade needs to be acceptable and beneficial for both parties across a much wider set of considerations and criteria.

For instance, even if trade is attractive to both parties in purely economic terms, it will not be mutually beneficial if it generates unacceptable environmental degradation. Trade that generates corporate profits but contributes to geo-strategic instability is not mutually beneficial. Nor will trade be mutually beneficial if production facilities that churn out exports engage in abusive labor practices that violate the social mores of the importing country. Trade relationships built on predatory dumping, which delivers inexpensive products but creates damaging global supply gluts, is not mutually beneficial. Trade is not mutually beneficial if imported products help entrench new standards and norms that run contrary to the values of the importing country.

On the most basic level, trade is not mutually beneficial when it creates overdependence on a single country. In all these instances, any short-term economic benefits will be more than offset over the long term.

Faustian bargains

Countries which wish to see trade relationships flourish will need to be cognizant of and responsive to these wider considerations which define mutual benefit. And countries which foolishly accept trade on lopsided terms will find they have made a Faustian bargain that will eventually rebound to their detriment.

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In fact, it is a desire to redress earlier Faustian bargains which is fueling some of the upheaval in trade we are currently experiencing. This is apparent, for example, in the desire to uproot and diversify supply chains or impose restrictions on sensitive technology trade. In these cases, the economic efficiencies that accrued are now judged to have been outweighed by the vulnerability created by overdependence or the security concerns raised by dual use technologies in an era of rising geostrategic competition.

Mutually beneficial trade is not always possible, but it does exist

Despite the increasingly contentious trade landscape today, we do see examples of mutually beneficial trade.

The Australia-New Zealand Closer Economic Relations Trade Agreement (ANZCERTA) provides a good illustration of the desire to prioritize mutual benefit.

While no agreement or relationship is perfect, the Australia-New Zealand Closer Economic Relations Trade Agreement (ANZCERTA) provides a good illustration of the desire to prioritize mutual benefit.[3] Indeed, Article 1 of the accord establishes the "mutually beneficial expansion of free trade between New Zealand and Australia" as a core objective.[4]

The agreement substantially reduced or eliminated barriers and facilitated an even deeper economic integration. Of course, as barriers dropped and competition increased, inevitable dislocations followed. But overall, an assessment of the agreement's results led both parties to voluntarily accelerate its terms. While many trade partners seek to forestall tariff reductions, Australia and New Zealand voluntarily agreed to eliminate tariffs five years ahead of schedule. The ANZCERTA was conceived, and is being implemented, in a cooperative spirit that has produced benefit for both parties.

The renegotiated North American Free Trade Agreement (NAFTA), despite the confrontational circumstances under which it was launched, also illustrates the ability of three countries to find common ground and sufficient mutual benefit in trade.

The dynamic of the renegotiation was such that Mexico and Canada acceded to modifications that neither had sought, in particular in dairy and automotive trade. But both countries recognized the need for mutual benefit and the imperative to address the problematic aspects of NAFTA for the United States. A tripartite agreement that is not working for one party is not working for any of the parties.

Economists and trade experts will debate for years the wisdom and actual impacts of the various modifications that were agreed. Ultimately, they may or may not deliver the hoped-for results. But at a minimum, the renegotiated US-Mexico-Canada Agreement (USMCA) demonstrated a recognition of the need to achieve mutual benefit in trade agreements and trade relationships.[5]

Although a renewed focus on mutual benefit in trade is desirable, we need to be practical and realistic about its implications. There will inevitably be some areas where trade partners cannot find sufficient common ground to allow mutually beneficial trade to take place. The intensifying rivalry between the US and China, for instance, is testing the extent to which trade and investment can flourish between countries with divergent values and ideologies.

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Prioritizing the need for mutual benefit means that in some instances trade and investment could shrink. But at least the relevant parties will be clear-eyed about which incompatibilities are too great to overcome. The relationship will likely be stabilized by the clear knowledge of where the red lines lie.

How does China see mutual benefit?

China sees its engagement in the global trade system almost entirely in terms of how it can be leveraged to support the achievement of its specifically delineated economic development goals and broader geo-strategic objectives.

Across decades worth of government policy papers, official statements, and five-year plans, China has been remarkably transparent in spelling out its views on the role of trade. China sees its engagement in the global trade system almost entirely in terms of how it can be leveraged to support the achievement of its specifically delineated economic development goals and broader geo-strategic objectives. There is little or no accounting in this formulation for the interests and needs of trade partners. This has led to unbalanced outcomes and growing disillusionment on the part of China's partners.

Advanced manufacturing and cutting-edge technologies are an especially high priority for China. The Made in China 2025 strategy provides a case in point. The plan aims for China to achieve global preeminence in 10 key strategic sectors by 2025.[6] Engagement with foreign companies is a cornerstone. Yet, the plan approaches relationships with foreign partners entirely in terms of how benefit can be extracted for China.

Foreign companies are to be shoehorned into joint ventures with local partners that require the transfer of critical technologies. As foreign technologies are absorbed and assimilated, this will give rise to world-beating China companies, the so called "national champions".[7] A panoply of tools will be deployed to support this objective, including massive subsidization, localization targets, high market barriers for foreign firms, China-specific standards, and a policy of civilian-military fusion. Unfortunately, blatant intellectual property theft and cyberespionage are also sometimes part of the formula.[8]

Mutually beneficial for foreign partners?

This whole-of-government approach allows national champions to achieve economies of scale with unprecedented speed and capture large slices of global market share. The unapologetic objective is to ultimately reduce the need for foreign partners.

The past two decades are replete with examples of foreign companies finding themselves squeezed out of the China market after having transferred technology and managerial know-how to local partners.

This raises obvious and justifiable concerns. The past two decades are replete with examples of foreign companies finding themselves squeezed out of the China market after having transferred technology and managerial know-how to local partners. To add insult to injury, they are then often outcompeted in third markets by the very same competitors from China that they empowered through technology transfers.

Although many foreign companies have profited handsomely from the China market at least in the short-term, this is hardly an arrangement that could be considered mutually beneficial over the long-term. Foreign technology companies are permitted access to China's market for as long as it takes to empower the local companies that will replace them. Ultimately, growth, sales, and share value will all decline.

Decoupling capital markets?

China's effort to limit the need and scope for foreign partnership is being extended to financial markets. In this case however, domestic companies in China are finding their access to US markets circumscribed by Beijing. The recent crackdown on Didi, the Chinese ride-hailing firm, signals at least a partial decoupling in capital markets.

Days after Didi's launch on the New York Stock Exchange, China's cybersecurity regulators announced an investigation into potential breaches of data security and national security laws.[9] Didi was prohibited from adding new users and the app was removed from app stores in China. Predictably, its share price plummeted.

A clear and unmistakable message was sent. This considerably more guarded regulatory stance towards Chinese technology companies pursuing IPOs in the US will have a chilling effect across the entire sector. The process has now become fraught with risk and uncertainly. Significantly more time and money will need to be expended. Consequently, companies in China will be less likely to seek US listings and opt instead for domestic alternatives.

For the past several decades, the overall trendline has been towards a deepening economic integration between China and its developed world partners. That trend has now weakened and in some respects is heading in reverse.

WTO entry was not the problem

In recent years, as the predatory nature of China's approach to trade became more evident, the US and other developed economies have reappraised their trade relationships with China. In many quarters, China's entry into the World Trade Organization (WTO) in 2001 is now viewed as a strategic miscalculation.

More importantly, the US and others failed to insist on the need for mutual benefit, as worrisome indicators of China's intent began to manifest.

The mistake was not in approving China's accession to the global trade body. The misstep was in neglecting to enforce what had been agreed. More importantly, the US and others failed to insist on the need for mutual benefit, as worrisome indicators of China's intent began to manifest.

Many Western countries expected China to soon liberalize and transform into an open market economy after the country's accession to the WTO on December 11, 2001. Global trade has undergone profound changes since.

Maintaining the system

China has benefited more than any other country from access to an open global trade system. One might therefore have expected China to be its most fastidious caretaker. That has not happened. If China wishes to continue to derive benefit from an open global trade system, it needs to begin to invest more in its upkeep. Its current approach, which holds little regard for mutual benefit, is helping to drive us towards a far more confrontational trade system in which might makes right.

Like any country, China has its own legitimate economic development objectives which should be respected. But if its pursuit of those objectives leaves partners feeling bullied and exploited, those partnerships will crumble. This is already happening.

Consternation over China's conduct has become so high that countries with common grievances are attempting to coordinate their responses.

Increasingly, China's partners are concluding that trade relations with China have yielded unbalanced, unacceptable outcomes. This has led to a greater willingness to forcefully challenge China, and where possible, to diversify trade. Consternation over China's conduct has become so high that countries with common grievances are attempting to coordinate their responses. This increases leverage and could potentially cushion the economic blow of foregoing trade with China.

Australia makes its case to the G-7

Australia recently felt China's ire. It has been hit with stiff trade sanctions on products from wine to wheat, to which China has offered dubious trade-related justifications. It is evident that these moves were really a thinly veiled punishment for Australia having the temerity to suggest that it would be useful to understand the origins of Covid-19.[10]

Australia has signaled its intention to pushback aggressively. It has already challenged China in the WTO. At the recent G-7 meeting in the UK, Prime Minister Scott Morrison made an impassioned plea for the grouping to stand up more forcefully to what he characterized as China's bullying.[11] Lest anyone miss the point, Morrison would later tell the Organization for Economic Cooperation and Development (OECD) that, "The global trading system and rules-based order is under serious strain and threat. Meeting these challenges will require a degree of active cooperation not seen for many decades."[12]

Although there are varying views among G-7 members, the closing statement was considerably more critical of China than anything in the past. There is no reason to think the G-7 will devolve into an "anti-China" club. The group may, however, be more willing to call out and confront unacceptable practices and policies. In fact, the wider EU grouping has pressed the pause button on its much-ballyhooed Comprehensive Agreement on Investment with China due to human rights concerns. Despite the anticipated economic upsides, the human rights issue apparently led the EU to conclude that the agreement was not mutually beneficial on balance.

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The significant blowback facing China should give policy makers in Beijing reason for reflection. Are these one-sided policies and practices really working in China's best interests? President Xi Jinping's recent call for China to present a more "lovable" face to the world indicates a recognition that China has a problem.[13] But a public relations campaign unaccompanied by substantive changes will accomplish nothing.

A joint statement of the G-7 leaders after a three-days summit in June 2021 called for greater unity against trade and human rights challenges posed by China. Analysts said it had been the most forceful statement made by the group on China to date.

Biden holds the line

Across the Atlantic, the Biden administration was widely expected to be far less combative than the Trump administration on trade. The previous US President had infamously stated that trade wars were "good and easy to win" and accused China of being the "worst" offender in unfair trade practices.[14] His administration ultimately applied punitive tariffs on over two-thirds of China's exports.

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It is noteworthy therefore that there has been little discernable change in China policy from the Biden White House. The tariffs have remained in place. In fact, both the US Trade Representative and the Secretary of Commerce have spoken positively about their impact and indicated that they are in no rush to see their removal.

The just-completed 100-day supply chain review established a trade strike force mandated to recommend trade actions in response to China's unfair practices. At the other end of Pennsylvania Avenue, a bill designed to bolster US competitiveness against China in trade and technology is working its way through Congress.

Does the US have clean hands?

China is certainly not solely responsible for the breakdown in mutual benefit and trust in trade. The hands of the US are not entirely clean. Especially in recent years, America's proclivity to resort to punitive unilateral trade actions, often taken on questionable grounds, has eroded trust and a sense of mutual benefit. Despite being the primary architect and proponent of the global trade system, recently the US has seemed more intent on dismantling it. The US must bear its share of responsibility for the woeful state of affairs in trade.

At least some of these actions were taken to address unresolved grievances that had eroded the US' belief that trade was mutually beneficial. Predatory practices that WTO rules were powerless to curb have created enduring economic distress, especially in manufacturing communities. These could no longer simply be brushed aside as short-term "trade adjustments". Even the harshest critics of the unilateral trade actions taken by the Trump administration often conceded that the underlying grievances were legitimate.

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The challenge for the US will be to restore a greater degree of mutual benefit to its trade relationships without letting the pendulum swing too far in the opposite direction. It will be a difficult balance. President Biden's intention to pursue a 'worker-centric' trade policy provides a useful illustration.[15] Up to a certain point, it would be a necessary corrective and deliver a greater level of benefit to the US workers who were left behind during previous rounds of trade liberalization. Taken to an extreme, it would become an excuse for protectionism and undermine the mutual benefit that US trade partners should reasonably expect to receive. Threading the needle will not be easy.

Not a perfect system, but…

It is pointless to view the history of our current trade system through rose-colored glasses. The reality is that the US has often fallen short of its ideals and rhetoric. And many of the predatory practices that China is being criticized for today were first pioneered by Japan[16] and then the four East Asian Tigers: South Korea, Singapore, Taiwan, and Hong Kong.

Trade nirvana has never existed. But the trade system established in the aftermath of World War II delivered sufficient mutual benefit to ensure the participants' voluntary buy-in and a desire to at least attempt to cooperate. Although easily overlooked, this is no small accomplishment. Today however, that commitment is starting to crumble, as balance and mutual benefit have deteriorated.

Looking ahead

Hardheaded pragmatism should point us towards a greater emphasis on broad based mutual benefit in our trade relationships.

Perhaps the current slide into more adversarial, zero-sum trade relationships will simply continue. Trust and confidence may have been damaged beyond repair. We must reflect more carefully, however, before resigning ourselves to a more Hobbesian trade world. Despite considerable shortcomings which need to be addressed, we have all benefitted immensely from trade. Our individual best interests have been more tightly intertwined with collective best interests than our current approach suggests. While it would be counterproductive to have idealized expectations about a "Kumbaya moment" in trade, hardheaded pragmatism should point us towards a greater emphasis on broad based mutual benefit in our trade relationships.

Leadership will be needed to get us there. At this point, it is unclear who can seize the mantle. Some things are clear. Merely playing the "blame game" for where we find ourselves today is a waste of time that will generate little future value for workers, consumers, companies, and countries. Protectionism and mercantilism have been tried. Although some countries have undeniably reaped short-term benefits, these are poison pills that will eventually kill the patient. If there is hope for a sustainable future in trade – and there is – it will have to be built on a renewed sense of shared ownership and shared responsibility for a trade system that respects and delivers mutual benefit.

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About the author

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Notes

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