

# The Changing Role of Multilateral Cooperation in the GVC Age

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# Signature Features of the 21<sup>st</sup> Century Economy

- Production Fragmentation:

*Global Value Chains knit countries together as never before.*

- Labor Market Disruption:

*Overall economic gains are not shared by all, and many workers feel left behind.*

- Driven largely by new technologies, both present fundamental challenges (and opportunities?) for the multilateral trading system.



# Overview of Today's Talk

- I. Big picture review of recent research:
  - GVCs as a trade policy “game changer”
  - Preferential Trade Agreements as both threat and river guide
  - Rising inequality and falling labor share as potential driver of discontent, populism, protectionism
  
- II. Discussion of what it means for the WTO:
  - New challenges and opportunities
  - Making “sustainable and inclusive” work



# GVCs as a Trade Policy Game Changer



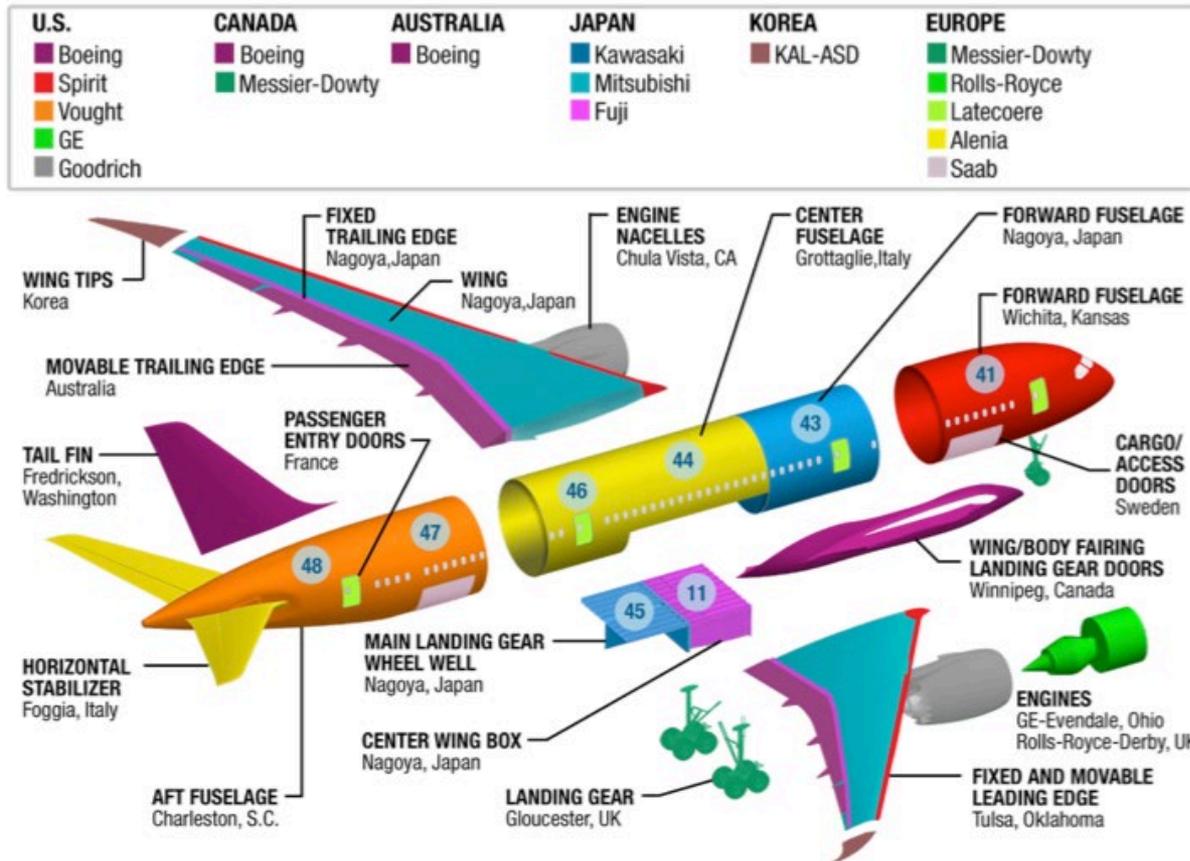
# The GVC Revolution

*We don't make things the way we used to.*

Production fragmentation allows more countries, firms, and workers to participate in global production, by carving out new (and often narrow) slivers of expertise and excellence in global value chains.



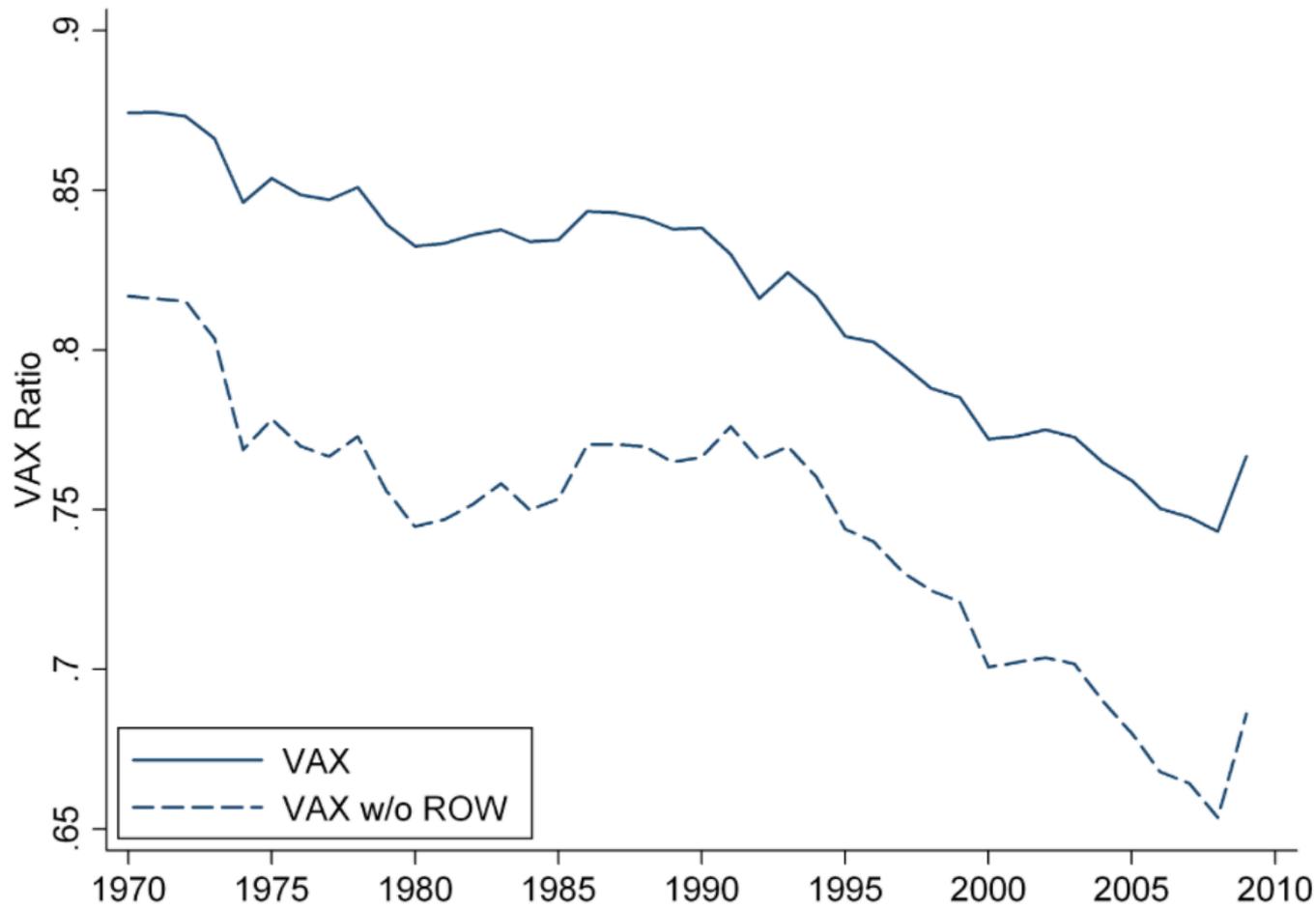
# The GVC Revolution, illustrated



**19 Sections, 17 Design Teams, 10 Countries,  
Thousands of Engineers, 1 Airplane**

SOURCE: THE **BOEING** COMPANY

# The GVC Revolution, in data



*VAX Ratio:  
the ratio of  
value  
added  
trade  
to gross  
trade*

Source: Johnson and Noguera (2017)



# What Do GVCs Mean for Trade Policy?

- Starting observation: GVCs (and FDI) drive a wedge between countries' national *economic interests* and their *geographic borders*.
- GVCs create new, often subtle linkages between markets, firms, workers, and consumers within and across borders.
- GVCs also introduce new vulnerabilities to global disruptions.



# Key Insights from Recent Research

1. GVCs change governments' incentives over traditional trade policies – tariffs and non-tariff barriers.
2. GVC linkages may increase the role (and demand) for “deep” behind the border provisions.
3. GVCs induce PTAs and vice versa
4. GVCs magnify the impact of global shocks.



# 1. Revisiting Market Access with GVCs

GVCs change incentives over traditional trade barriers:

*Key Idea: importers internalize interests of foreign producers*

- GVCs → domestic value added embedded in foreign goods and foreign value added in domestic goods
- Global Sourcing → access to foreign suppliers is increasingly critical to firm success
- New motivations to reduce trade barriers unilaterally,
- ...but also increased incentive to *target* trading partners, industries, or even firms (e.g. via TTBs)



# 1. Revisiting Market Access with GVCs

Significant empirical evidence that these forces already influence tariff preferences and use of TTBs:

- US tariff preferences (esp. GSP) tied to MNE activity  
(Blanchard and Matschke (2015) *Review of Economics and Statistics*)
- GVCs → more generous tariff preferences and lower TTB use among countries with more integrated GVCs  
(Blanchard, Bown, and Johnson (2016) *CEPR & NBER working paper*)
- Global Sourcing → market access important for firms  
(e.g. Antras, Fort and Tintlenot (2017) *American Economic Review*; Freund (2017) *PIIE*; Conconi et al 2019)



## 2. New GVCs Linkages and Deep Agreements

GVC linkages can be both complex and murky:

- complex linkages → complex vulnerabilities to opportunistic behavior Firms call for stronger behind the border protections;
  - An argument for (some) ISDS provisions?
  - IP Protection and data security increasingly important.
- murky linkages → murky information between producers and purchasers; consumers and downstream firms demand stronger behind the border regulations.
  - Do GVCs call for a new “global code of conduct” with global labor, environmental, and regulatory standards?

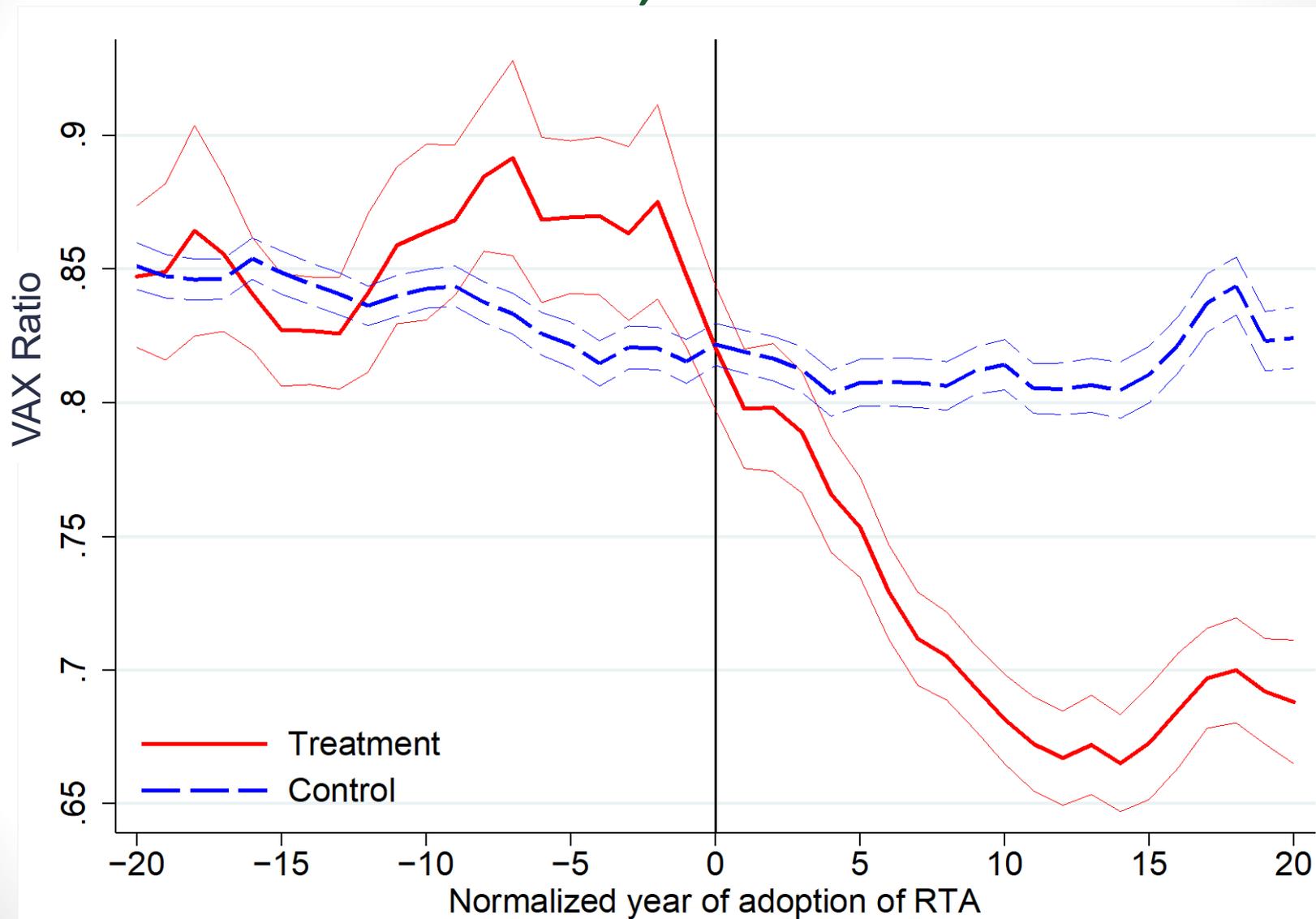


### 3. GVCs and the Proliferation of PTAs

- Reinforcing cycle: GVCs → PTAs → deeper GVCs



### 3. GVCs and PTAs, in the data



Source: Johnson and Noguera (2017)

### 3. GVCs and PTAs: Concerns

- Reinforcing cycle: GVCs → deep PTAs → deeper GVCs
- But the same mechanism may leave some regions out: fear is increasing trade and investment diversion, growing asymmetry
- Greater regional integration may could induce balkanization.



### 3. GVCs and Deep PTAs

Proliferation of preferential agreements may also reflect latent demand for behind-the-border protections by:

- Firms operating in the GVC landscape, who want regulatory coherence, customs efficiency, national treatment, IP and data protection, etc.
- Consumers, who care about not just about products, but *process* (protections against child labor; worker rights, environmental protection, consumer safety)



# 4. GVCs Magnify the Costs of Global Shocks

- Economic fall-out from a trade war is broadly dispersed. (e.g. Kamal, Handley, and Monarch (2020))
- Likewise, costs of natural disasters are broadly shared (e.g. Carvahlo et al (2016); Boehm et al (2016))
- COVID-19?
- Upshot: benefits of coordinated responses and multilateral cooperation are greater than ever.



# Rising Inequality, Labor market Disruption, and the Return of Protectionism

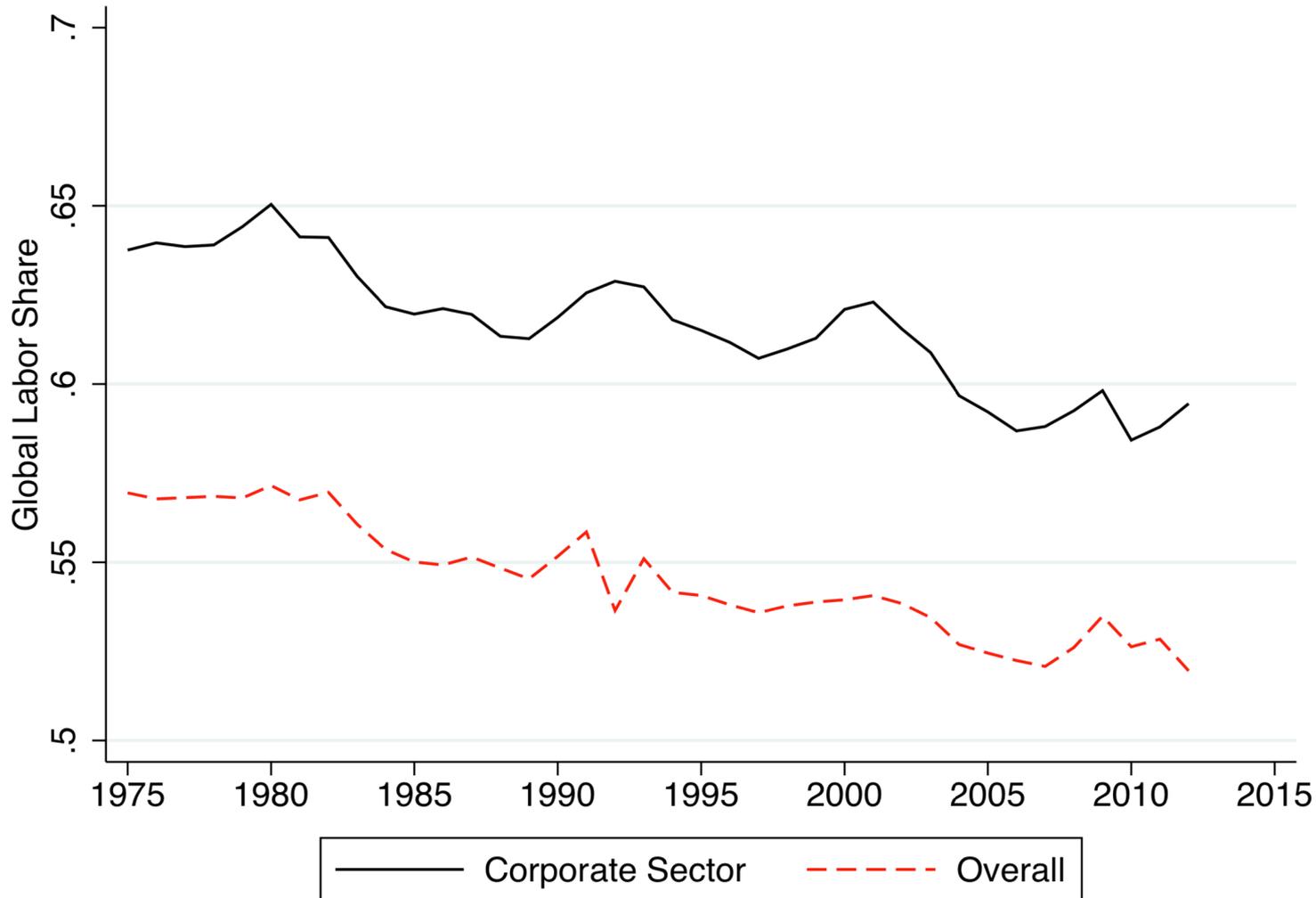


# Labor Market Disruption as Protectionist Trigger

- Quick overview of the evidence (some countries):
  - Falling labor share of income
  - Rising inequality
  - Slowing economic mobility
  - Vanishing middle class
- Rising protectionism



# Falling Global Labor Share of Income

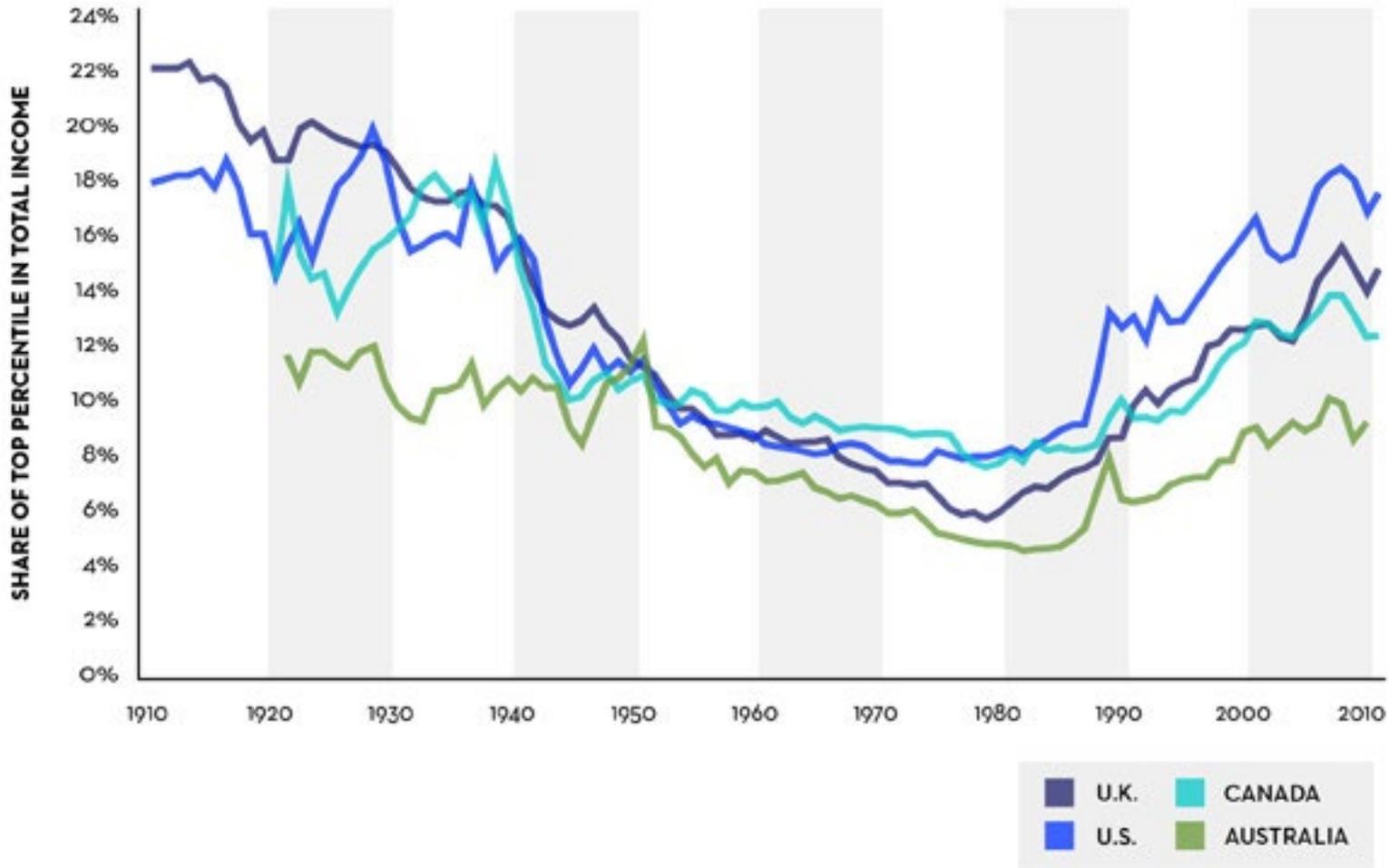


Source: Neiman et al (2013 QJE)



# Rising Inequality

### INCOME INEQUALITY IN ANGLO-SAXON COUNTRIES, 1910-2010

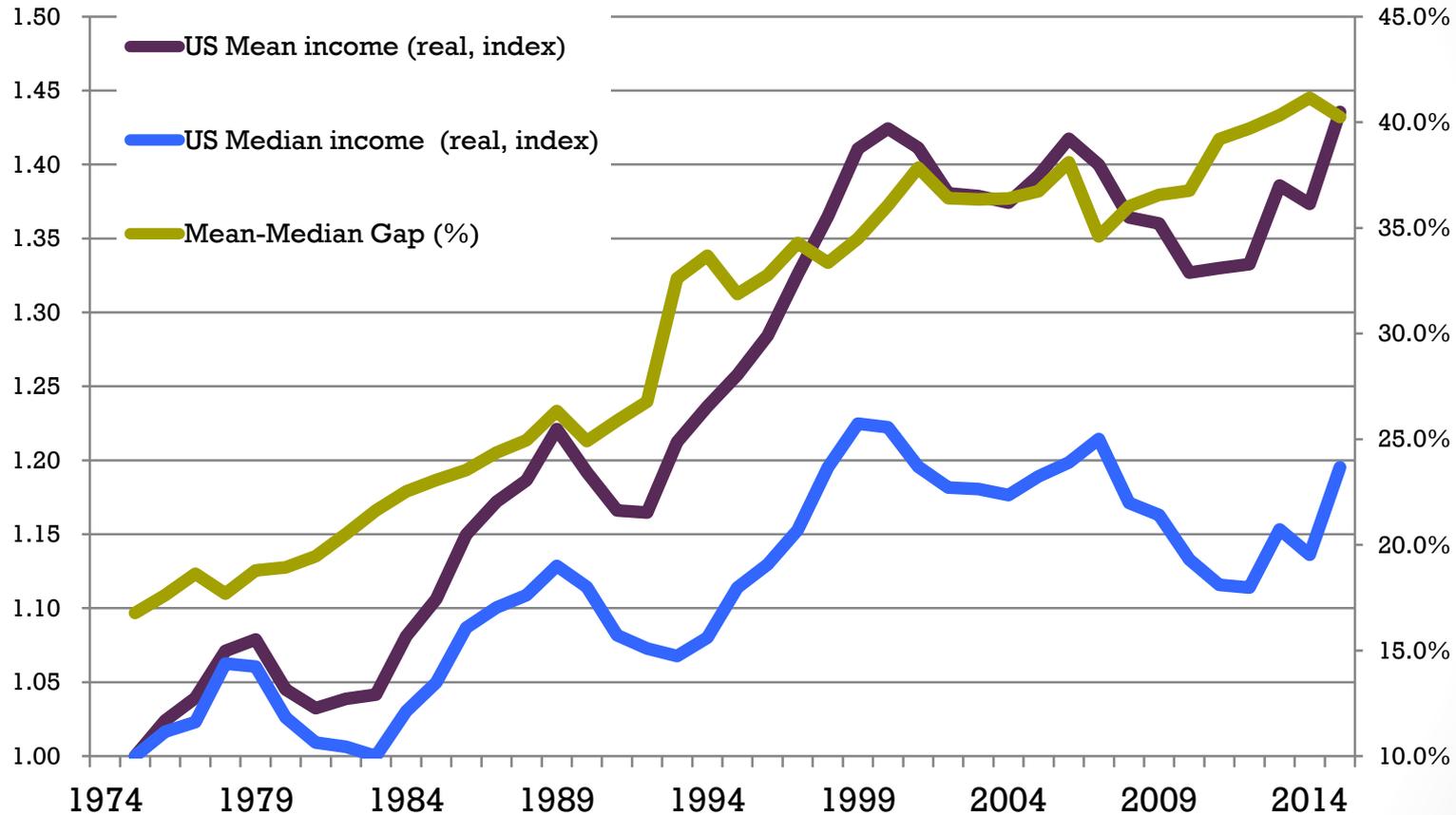


Source: Piketty (2013) via *The New Yorker*



# Rising Inequality, addendum

## U.S. Mean and Median Real Income Since 1975



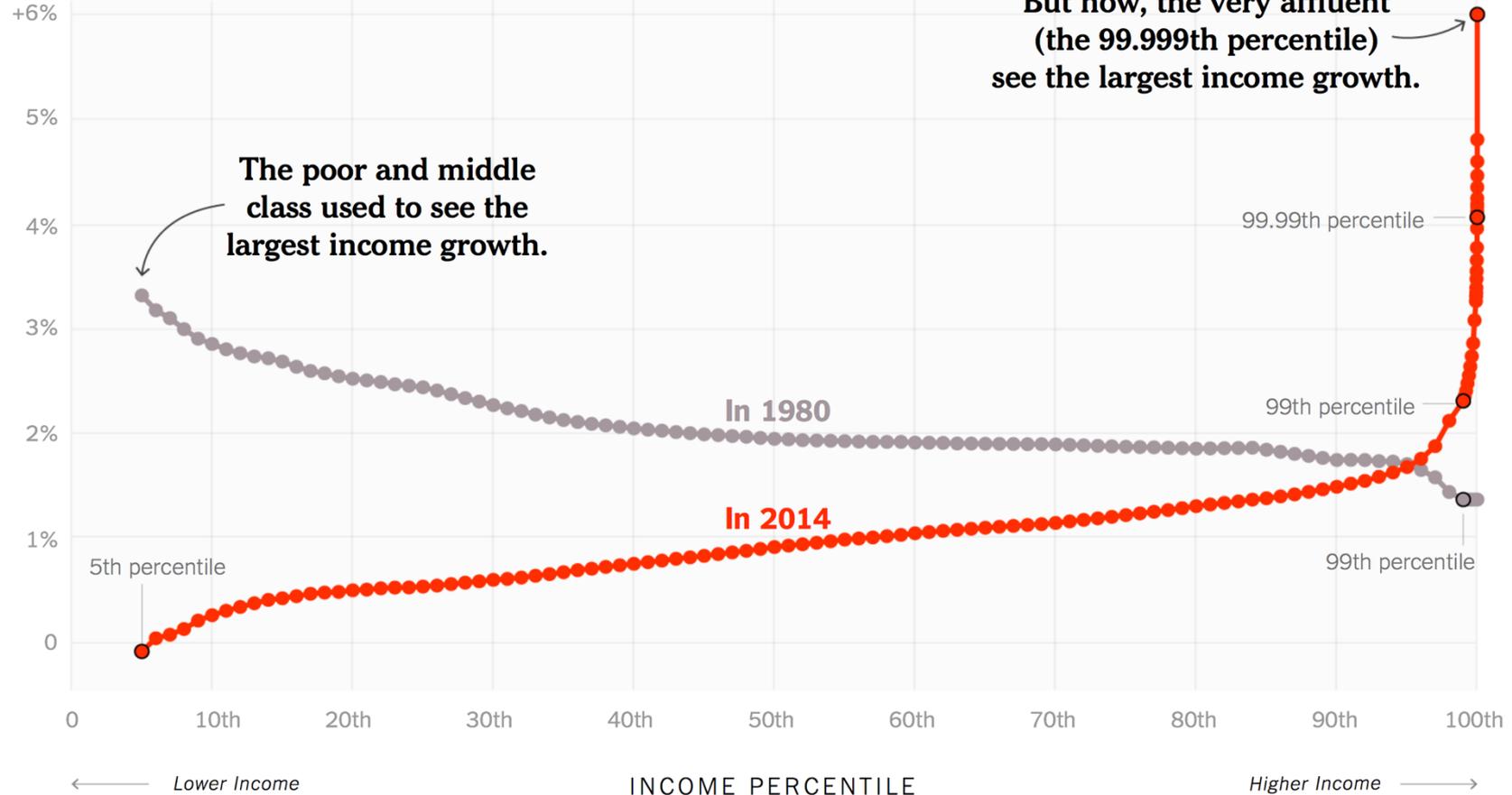
Source: Blanchard and Willmann (2018) using U.S. Census data



# Slowing Economic Mobility

## INCOME GROWTH

Over previous 34 years

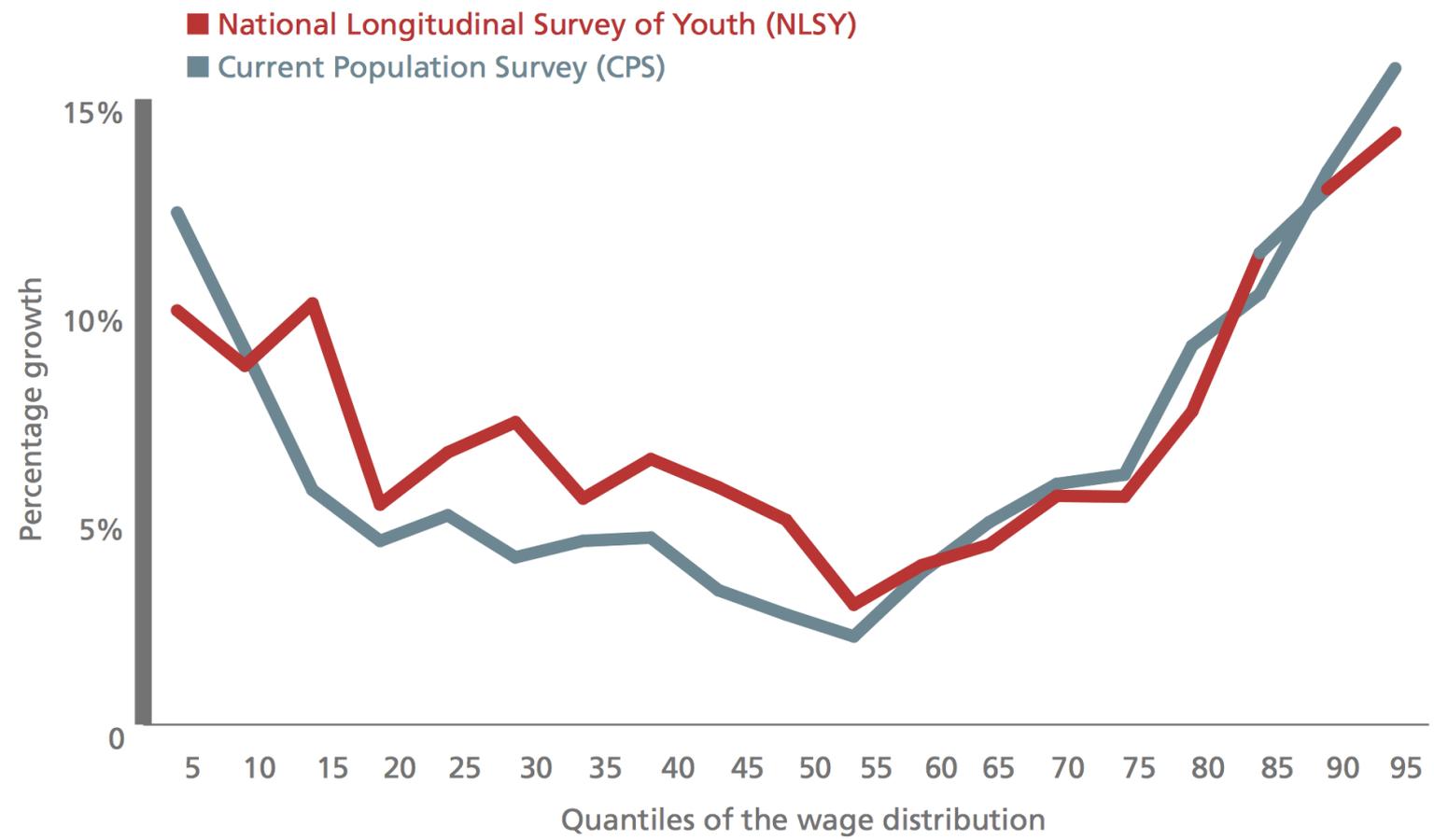


Note: Inflation-adjusted annual average growth using post-tax income.



# Vanishing Middle Class

Percentage growth of the quantiles of the US wage distribution since the end of the 1980s



Source: Boehm (2013)



# Protectionism as Political Consequence?

Technology, Preferences, Trade, and Policy *all* contribute.

- The upshot: the market distribution of income (and wealth) seems to be diverging from 20<sup>th</sup> century norms, what many believe is “fair”.
- The upshot in a democracy.... Change.
  - New domestic economic market interventions: crucially, many workers demand “jobs, not handouts”
  - New skepticism about global markets, firms,



Cover Story: The Economist, February 14, 2019

The resurgent left

# Millennial socialism



Photo: Jo Banks



# Implications for Multilateral Cooperation:

*Never let a crisis go to waste*



# 21<sup>st</sup> Century Challenges for the WTO

The world has changed:

- “Old” market access policy tools limit relevance in the GVC Era.
- Deep PTAs divert both trade *and policy attention*.
- Rising Protectionism, trade wars, and economic nationalism feed skepticism of multilateral institutions

*Fundamental question: Defend the past or forge the future?*



# A Pivot to the Future

## 1. Craft a “Global Code of Conduct.”

*Can members use plurilateral agreements build on the best aspects of new mega-regional PTAs to address IP protections, ISDS, minimum labor and environmental standards?*

- Study and learn from recent deep agreements.
- Leverage flexibility via open-access plurilaterals
- Adopt a “value and values-added” mindset: *what are the economic and social values embodied in trade?*



# A Pivot to the Future

## 2. Take the Lead.

*Can WTO members develop a fair, equitable, and market-driven response to the climate crisis?*

- Advance efforts to study the potential role of “climate clubs” or a “green BAT”: the WTO has unique experience and tools to understand the intended and unintended consequences of new carbon policies.



# A Pivot to the Future

## 3. Be a Catalyst.

*How can the WTO best support its' members' domestic policy initiatives in this era of rapid labor market change?*

- Embrace new ideas and approaches.
- Anticipate and enable domestic policy initiatives.
- Serve as a repository for best practices and new ideas.



# An Optimistic Spin on a Most Unusual Moment

The world is healthier, more educated, wealthier, **and more connected** than ever before.

*We are struggling with how to embrace new technological advances, and deepening global linkages – and the messy, hard, questions they raise. **It may not be pretty, but the opportunities are vast.***

