



The Future of Multilateralism in the Post-pandemic World

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Abstract

This paper applies an endogenous institutional framework to understand the evolution of the rules-based international trading system since the end of World War II. We argue that the initial success of the General Agreement on Trade and Tariffs and re-enforcement that led to the formation of the WTO can be explained by three major factors: the hegemonic position of the US, the belief that international trade would foster prosperity and peace, and Cold War politics. However, declining US hegemony along with a shift in global comparative advantage in labor-intensive manufacturing led to a shift from multilateral towards preferential trade agreements since the 1990s. Today, the WTO faces several new challenges, including increasing geo-political competition between the US and China, increasing digitization of commerce, and disrupted supply chains following COVID-19. A functioning WTO that facilitates global economic re-integration remains crucial to ensure a strong recovery from the pandemic and continued long-term prosperity and stability of the global economy.

Keywords: endogenous institutional change, GATT, international trade, institutions, WTO

JEL codes: F13, F15, N40

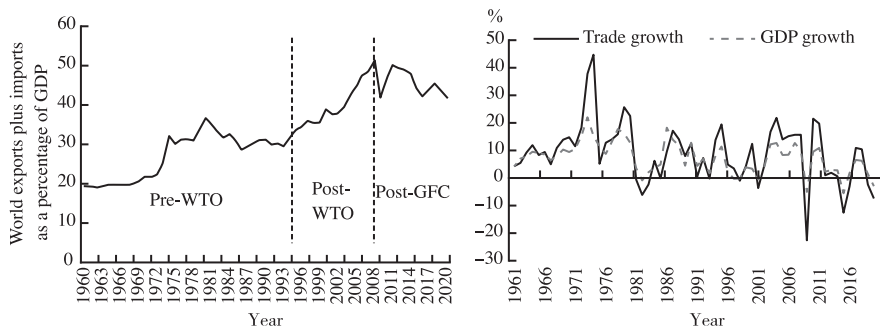
I. Introduction

For decades following the end of World War II (WWII), multilateral trade institutions exemplified by the General Agreement on Trade and Tariffs (GATT) provided an avenue for countries to commit to restraining unilateral trade or trade-related policies in return for similar restraint by trading partners. In a monumental achievement in world politics, member countries re-enforced the GATT rules, leading to the formation of the WTO in 1995 which committed member countries to a non-

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optional and binding dispute settlement system overseen by a panel of international legal experts. The decade following the formation of the WTO saw a rapid increase in global economic openness, with the share of global trade (exports plus imports) as a percentage of global GDP rising from 31 percent in 1994 to a peak of 51 percent before the Global Financial Crisis (GFC) in 2008 (Figure 1). However, since the GFC the pace of growth in global trade has slowed considerably, with global GDP growth outpacing global trade growth, resulting in global economic openness falling to 41 percent in 2020.

Figure 1. The rise and fall in global economic openness, 1960–2020



Sources: UNCTAD statistics (see: <https://unctadstat.unctad.org/>); World Development Indicators (see: <https://databank.worldbank.org/>)

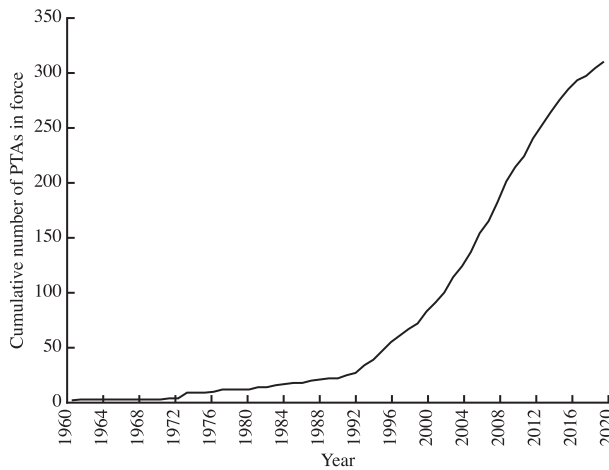
Note: GFC, the Global Financial Crisis.

Despite the initial success of the WTO, the failure of countries to successfully close the Doha Round of multilateral trade negotiations began a general trend of pessimism towards trade multilateralism. In recent years, the WTO has been further weakened particularly with the beginning of a trade war between the two largest economies in the world, the US and China, and several institutional regressions such as the inability of countries to appoint judges to the WTO Appellate Body. This has resulted in a more fractured trade environment with the proliferation of inward-looking preferential trade agreements (PTAs), which have increased from less than 30 active agreements in 1991 to over 300 such agreements in 2020, further undermining the multilateral trade institutions (Figure 2).

The WTO is a crucial public good that enhances the stability and certainty regarding international trade policy, which in turn resulted in greater predictability for international investors and allowed for an easing of institutional constraints to global production sharing based on comparative advantage. More broadly, as put by Koopman et al. (2020, p. 830),

the WTO provided a range of economic benefits including “more transparent and informed economic transactions, more secure and predictable economic relations, more cooperative or ‘win–win’ economic outcomes, and, perhaps above all, more open exchanges of ideas, information and knowledge – including knowledge about how to better manage economic interdependence itself.”

Figure 2. The rising number of preferential trade agreements (PTAs) in force, 1960–2020



Source: WTO RTA Database (see: <https://rtais.wto.org/>).

In March 2020, the World Health Organization (WHO) declared the novel coronavirus outbreak (COVID-19) as a global pandemic, which led to several countries restricting economic activity and resulted in the most severe global economic downturn since the 1930s. Overall, global GDP contracted by 3.2 percent and the volume of international trade of goods and services contracted by 8.3 percent in 2020 due to a disruption of trade networks resulting from the cessation of production and hampered logistics and transportation.¹ The initial response of governments to the pandemic has included widespread implementation of export curbs, particularly of medical supplies and medicines (Evenett, 2020). This resurgence of trade protectionism risks an unravelling of the multilateral trading system, the failure of which would have catastrophic consequences for global economic growth and prosperity.

¹Available from: <https://www.imf.org/en/Publications/WEO/Issues/2021/07/27/world-economic-outlook-update-july-2021> (online; cited October 2022).

In this paper, we apply an endogenous institutionalist framework developed by Greif and Laitin (2004) and Greif (2006) to help understand the initial strengthening of the multilateral trading system in the form of the GATT and the WTO followed by its recent undermining in favour of PTAs. Using this game-theoretic framework, we identify crucial changes in “quasi-parameters” that re-enforced the system following WWII but have since undermined the system in the 21st century. We identify the challenges faced by developed and developing countries in the post-pandemic world and discuss the possibility of a new wave of globalization that builds on regional PTAs to chart an agenda for WTO reform. Lastly, we discuss the role of China, now the largest economy in the world in Purchasing Power Parity (PPP) terms and the largest trading nation in the world, in ensuring that a new phase of global re-integration recommences.

II. Understanding trade multilateralism: An endogenous institutionalist perspective

The central transaction concerning international trade cooperation can be characterized as the commitment by individual countries to restrain unilateral trade and trade-related policy decisions in exchange for reciprocal restraint from other countries. For countries to agree to limit their sovereignty on trade and trade-related issues, it is necessary for them to have “internalized beliefs” about potential gains and losses associated with trade cooperation (Greif, 2006). Internalized beliefs refer to the “mental models” of policymakers that guide their thought processes when evaluating the objectives and effectiveness of trade cooperation. The international trade, relations and law literature have argued for different objectives from trade agreements ranging from domestic political economy concerns, which include the political economy and commitment school of thought, and external spill-overs concerns, which include the terms of trade or other cost-shifting externalities theories, or systemic reasons, which include neorealist and strategic trade theory (WTO, 2007).

In addition to internalized beliefs, behavior in the central transaction is motivated by “behavioral beliefs”, that is “beliefs and expectations about the behavior of others in various contingencies that directly influences one’s behavior, whether or not behavior occurs” (Greif, 2006, p. 36). In the case of multilateral trade cooperation, the belief that other countries will provide access to their markets in a non-discriminatory manner motivates individual countries to do the same. On the other hand, in the case of preferential trade cooperation the belief that other countries will provide access to their markets but on a discriminatory but deeper basis motivates individual countries to do the

same. These beliefs are about behavior – providing discriminatory or non-discriminatory access to markets – that occurs given these beliefs. However, behavioral beliefs that do not transpire behavior also influence behavior, that is the belief that protectionist unilateral trade policy will lead to similar retaliation by other countries reduces the motivation to do so even though retaliation has not occurred.

For internalized and behavioral beliefs to generate regular behavior in the central transaction, it is necessary for agents to develop beliefs in several auxiliary transactions, that is transactions that “facilitate the generation of beliefs about behavior in the central transaction” (Greif, 2006, p. 47). If the behavior in auxiliary transactions adheres to (deviates from) the rules and beliefs that perpetuate the auxiliary transactions, beliefs, and patterns of behavior in the central transaction will be re-enforced (undermined). In other words, repeated interaction in auxiliary transactions will provide either positive or negative feedback that determines future beliefs (both internal and behavioral) and thus motivation in the central transaction. In the case of international trade cooperation, these auxiliary transactions include periodic monitoring and reviews to ensure countries are fulfilling their commitments, trade dispute settlement mechanisms, and modalities for further negotiations. Unless countries believe that they will be able to keep monitoring opponents, enforce previous commitments, or re-negotiate terms if the situation changes, beliefs in the benefits of the central transaction of exchanging commitments to restrain unilateral trade policy will be undermined.

Generating regular multilateral trade cooperation requires beliefs and norms that model multilateral rules-based cooperation as a positive-sum game to motivate such cooperation, rules which correspond to these beliefs by specifying concepts such as non-discrimination and the appropriate behavior in particular situations, and organizations that facilitate auxiliary transactions such as dispute settlement and channels for retaliation which perpetuate the same beliefs. Together these set of inter-related elements form a self-enforcing institution, that is, each country responds to these elements and behaves in a manner “that contributes to motivating, guiding, and enabling other [countries] to behave in a manner that led to the institutional elements to begin with” (Greif, 2006, p. 53).

How does this framework account for endogenous changes in behavior to occur? How can we explain the emergence of PTAs from a structure that perpetuated self-enforcing multilateral cooperation? In other words, in what ways do past institutions affect the trajectory of future institutions? Greif (2006) argues that the “institutions-as-equilibria” approach can be integrated with the study of endogenous institutional change through the use of two additional concepts: quasi-parameters and self-reinforcement. Equilibrium behavior can gradually, over the long term, alter some

aspects of the situation that were being considered parametric to the central or auxiliary transactions. Although it is proper to consider such aspects as “parameters” when studying self-enforceability in the short run, “parameters” which are changed endogenously in the long run due to the self-enforced institution are better termed as “quasi-parameters.”

As put in Greif and Laitin (2004, p. 634), “rather than restrict the institutional analysis to parameters, that is features exogenous to the institution in consideration, and variables, those which are endogenous, quasi-parameters account for those features of the situation that should be considered parametric in studying self-enforceability in the short-run but as variables in studying institutional dynamics in the long-run. Those parameters that are endogenously changed in the long run due to the self-enforced institution are termed quasi-parameters. However, the distinction between parameters, quasi-parameters and variables is not rigid but based on empirical observations. If a self-enforcing institution affects certain parameters in a manner that would lead to long-term behavioral change, these parameters are best re-classified as quasi-parameters.”

An institution is reenforcing when the self-enforcing behavior it entails, through its effects on quasi-parameters, increases the range of parameter values (that is the “situations”) for which the institution is self-enforcing. On the other hand, if such quasi-parametric changes constrict the range of parameter values for which the institution is self-enforcing, then the institution is undermined. It is important to note that changes in quasi-parameters do not necessarily lead to a change in the equilibrium behavior or expected behavior. When these quasi-parametric changes are self-reinforcing, exogenous shifts which would otherwise have led to institutional change do not have this effect. Conversely, self-undermining quasi-parametric changes restrict the range of parameter values for which the institution is self-enforcing, but institutional change only occurs when these undermining processes reach a critical level such that past behavior is no longer self-enforcing. Using such a framework, institutional change and stability occur due to the endogenous processes which cause quasi-parametric change, exogenous shocks, or combinations of both.

The emergence of the GATT in the post-war period as a set of self-enforcing rules that linked central and auxiliary transactions regarding trade cooperation was significantly shaped by the hegemonic position of the US in the global economy, beliefs of key policymakers regarding trade cooperation arising out of the experience of the inter-war years, and Cold War politics. Following the defeat of Nazi Germany, the hegemonic position of the US in the global economy meant that “the United States, the undisputed economic and technological superpower in 1950, never really considered

the possibility that several decades later Europe and Japan would catch up with or even challenge its predominance in some respects” (Baldwin, 1985, p. 8). Moreover, the US also had a large comparative advantage in the production of industrial goods with an export surplus in every major industrial group including machinery, automobiles, chemicals, textiles, and other manufactures.

In this context, a set of internalized beliefs that found credence on both sides of the Atlantic during this period was that to avoid future wars it was necessary to foster an open global economy to build the economic foundations of lasting peace. These beliefs were supported by another set of internalized beliefs arising out of the work of international economists led by the work of Paul Samuelson in the 1930s (Dixit, 2012). Samuelson’s work showed that international trade was a Pareto-superior outcome concerning welfare gains as compared to a situation with no trade (or autarky). Samuelson’s work provided a formal presentation of similar ideas put forward by David Ricardo and Adam Smith in earlier centuries and has had a major influence on work regarding comparisons and techniques regarding the issue since (Dixit, 2012).

Internalized beliefs regarding the gains of trade cooperation were complemented by behavioral beliefs regarding the actions of partners in response to US protectionist policies. The US had experienced the negative effects of beggar-thy-neighbor protectionist policies in the 1930s when in response to the Great Depression in the late 1920s, the US had legislated the Smoot–Hawley tariffs which led to an increase in what were already high protective tariffs across the board. The tariffs triggered a similar response by other countries who attempted to insulate themselves from widespread economic decline. Canada, Spain, Italy and Switzerland took direct retaliatory action against the US by raising tariffs while others increase import duties against all trading partners in response (League of Nations 1933, cited in Irwin et al., 2008).

The United Kingdom (UK) which had generally supported free trade also imposed higher tariffs in 1931 and passed an Imports Duty Bill in 1932. Moreover, in response to higher US tariffs, the UK and its dominions, Australia, Canada, New Zealand, and South Africa, further consolidated preferential trade agreements among themselves that discriminated against trade with the US, while Germany concluded a series of bilateral trade agreements with Central European countries effectively creating a trading bloc that diverted trade towards Germany. Lastly, in Asia, Japan attempted to create a “Greater East Asia Co-prosperity Sphere” which would divert trade towards itself. Irwin et al. (2008, p. 7) state that the outcome of protectionist and discriminatory trade policies was “not just a contraction of world trade, but a severe breakdown in the multilateral trade and payments system ... [and] political consequences, undermining

faith in democratic governments to manage their economies and hence abetting a turn to more authoritarian regimes in Germany and elsewhere.”

The experience of countries retaliating strongly against US protectionism and the ensuing negative economic and political consequences helped form behavioral beliefs among US policymakers regarding how other countries would respond and the consequences thereof if similar action was taken by the US in the post-war years. Having initiated the wave of protectionism around the world, the US was one of the first countries to reverse its protectionist policies by passing the Reciprocal Trade Agreement Act in 1934. The Reciprocal Trade Agreement Act gave the president power to reduce American tariffs with countries with which it previously had trade agreements by up to 50 percent without Congress oversight, as well as reducing the threshold of political support required to enact new tariff-cutting agreements.

Lastly, along with the set of internalized and behavioral beliefs discussed above, the political circumstances of the post-war period, particularly the beginning of the US–Soviet Cold War had important implications on the emerging global trading system. As documented by McKenzie (2008, p. 87), “US trade policy [in the postwar period] was only partly defined by domestic and economic pressures and was instead mostly used as a diplomatic tool to advance geopolitical ends, including the creation of a free world coalition founded on a liberal world economic order.”

Rather than insulating economics and politics into different spheres, the GATT emerged as a new arena in the battle between liberal capitalism among Western Allies and communist regimes led by the Soviet Union. The political imperatives of the Cold War further contributed to the US acceptance of imperfect adherence by allies to principles of non-discrimination and reciprocity that underpinned multilateral cooperation, particularly the grandfathering of preferential policies by European countries to their former colonies.

In the post-war period, the GATT as an institution, that is, a set of internalized beliefs regarding the gains of free trade, a set of behavioral beliefs that others would cooperate, and norms and rules such as non-discrimination and national treatment, was re-enforced through continued trade liberalization and rapid global economic growth. The economic recovery in Europe and Japan, along with the emergence of new Asian economies such as South Korea and Chinese Taiwan through active participation in the GATT assured that a rules-based international trading system provided mutual economic gains. However, these trends led to quasi-parametric changes which resulted in an undermining of the global trading system since the 1980s, particularly declining US hegemony, and a shift in global comparative advantage in labor-intensive manufacturing.

III. Challenges for developed countries: The US shift away from multilateralism

The framework discussed in the previous section, particularly the concept of quasi-parametric changes, provides answers to why the US, particularly under the Trump administration, abandoned multilateralism in favor of PTAs. Two quasi-parametric changes are of key importance: the declining hegemonic power of the US alongside a shift in global comparative advantage in labor-intensive manufacturing. As Europe and Japan recovered in the post-war era, and smaller countries, particularly in East Asia, grew economically, the US hegemony in the global economy began to decline. As the US lost its place as the global hegemon, it was no longer beneficial for the US to continue solely bearing the costs of providing a public good like multilateral trade institutions, especially if other countries continued to be exempt from imposing restrictions on their trade policies. While initial PTAs pursued by the US were with close political allies like Israel or countries in their neighborhood (that is North and South America), the end of the Cold War further reduced the political imperatives for the US to continue to allow other trading partners to continue being exempt from restrictions on trade policy imposed by the WTO rules.

The decline of the US hegemony was accelerated by China's accession into the WTO. After 15 years of negotiations, China was instated as a full member of the WTO in 2001 under a set of significant requirements that decreased the role of the state in China's domestic economy and required China to establish liberal international trade policies. This resulted in the rapid integration of China into the global economy and fueled the rapid growth of the Chinese economy. Although, as a result of China's WTO accession, the US consumers and firms too benefited from cheaper consumption goods and intermediate inputs (Amiti et al., 2020; Wang et al., 2018), the relative gains were skewed towards China as the country started from a much lower base. The rise of China as a strategic competitor to the US has contributed to the incorporation of strategic and relative-gains arguments in the mental models of the US policymakers regarding the payoffs associated with multilateral rules-based trade (Greico, 1990). Several areas of strategic competition have also intensified between the US and China, with increasing tensions in areas of the South China Sea, the South Korean peninsula, the Chinese Taiwan strait, the Middle East and cyber security.

Alongside changing geo-political circumstances, the unequal consequences of freer trade on the US economy, particularly through its effects on import-competing sectors in the US that produced labor-intensive goods. While the share of manufacturing employment in the US economy had been steadily declining since the 1960s, the

integration of Chinese labor into the global economy possibly exacerbated this trend facilitated by mandated technology transfers that contrived WTO rules (Swenson and Woo, 2019). Between 1987 and 2007, “China’s US import presence – the share of Chinese imports in total US expenditure on goods – increased from less than 0.2 percentage points in 1987 to 4.8 percentage points in 2007,” a 24-fold increase (Autor et al., 2015, p. 623). Chinese import penetration possibly accelerated the decline in labor-intensive manufacturing in the US and led to reduced labor force participation and a decline in manufacturing wages (Autor et al., 2013; Acemoglu et al., 2016; Swenson and Woo, 2019).

The rapid increase in US–China trade has also possibly had political consequences, specifically a rise in political polarization. Dorn et al. (2020, p. 3139) find “strong though not definitive evidence of an ideological realignment in trade-exposed local labor markets that commences before the divisive 2016 US presidential election.” They find that US electoral districts which experienced a relatively larger increase in Chinese import penetration experienced a simultaneous increase in ideological polarization, that is, increased support for far-right and far-left views. A survey done by the Pew Research found that unfavorable opinions of China increased substantially between 2005 and 2011, particularly in regions affected strongly by Chinese imports (Swenson and Woo, 2019; Dorn et al., 2020). The surprise election of Donald Trump further heightened the political partisanship along racial and ethnic lines as well as along conventional divides such as income and education, leading to a rise in populist and nationalist sentiments.

Although rising trade with China has possibly reduced labor-intensive manufacturing and increased political polarization, it is not obvious that de-coupling with China will reverse these trends. This is primarily because there are other forces, particularly the rise in technological innovations that increases automation of work, that have also contributed to these trends in equal measure if not more acutely. Swenson and Woo (2019) report that job losses in manufacturing due to technological innovations is 0.37 percentage point per year in the 1960–1979 period, globalization added 0.01 percentage point loss in 1979–2000, and the “China WTO factor” added another 0.05 percentage point to that trend in 2000–2007. Similarly, Feenstra and Sasahara (2018), Feenstra et al. (2019) and Eriksson et al. (2021) also argue that rather than increased trade with China, technological innovations were primarily responsible for the loss in manufacturing employment in the US and other industrialized nations (Swenson and Woo, 2019). Lastly, WTO (2017) analyzes the joint impact of trade and technology on labor market outcomes and concluded that although trade and technology are inextricably linked, the evolution of labor markets remains highly

diverse across countries, suggesting that country-specific factors play a pivotal role in the functioning of the labor market.

IV. Challenges for developing countries: The tension between reciprocity and development

Since the Kennedy Round of negotiations in the 1960s, one of the major issues plaguing multilateral trade negotiations has been the integration of least-developed countries (LDCs) “in ways that increased their export opportunities without requiring full reciprocity” (Koopman et al., 2020). As more developing countries have joined the WTO and their bargaining power has increased, a key quasi-parametric change has been increased tension between developed and developing countries to agree on rules that maintain consistency between the development goals of LDCs and global market integration. In a recent review of the literature on the effects of trade liberalization on poverty in developing countries, Winters and Martuscelli (2014, p. 493) conclude that although the general conclusion that trade boosts income and reduces poverty is upheld by recent studies, this finding is not true for LDCs, and that “liberalization has very heterogeneous effects on poor households, depending, *inter alia*, on what trade policies are liberalized and how the household earns its living. Working in the export sector predicts gains and working in the import-competing sector predicts losses, a finding that is reinforced by studies of the effects of liberalization on wages.”

Small-scale producers in developing countries, particularly agricultural producers, have increasingly advocated for “Fair Trade” with an aim of “lifting poor smallholder farmers out of poverty by providing them with premium prices, availability of credit, and improved community development and social goods” (Dammert and Mohan, 2015, p. 855). However, the evidence on the efficacy of Fair Trade movements on prices, income, productivity, and market access is mixed. In a review of the literature, Dammert and Mohan (2015) find a positive impact on producers’ prices and income, but limited effects on developing country market access and changes in productivity. Despite the vast amount of literature on the topic, they conclude that there remain several areas of theoretical and empirical research on the impacts of Fair Trade that need to be explored further.

Labor standards, environmental issues, and intellectual property rights (IPRs) have also emerged as central issues of conflict between developed and developing countries in international trade negotiations, once again highlighting possible inconsistency between the development goals of LDCs and global market integration. Although the Singapore Declaration of the WTO formally established the separation of trade and

labor in international law, Delgado (2019) argues that the WTO continues to address labor standards and policy extensively. Delgado (2019) concludes that the “WTO has approached this nexus without real engagement with the existing international labor standards framework beyond sporadic references to core labor standards. As a consequence, any positive result from a call for coherence or integration of both regimes seems unlikely” (pp. 459–60).

As the global climate change situation has become ever more hazardous with the “frequent occurrence of extreme weather events, the melting of glaciers, and the rising sea levels” (Zhang and Xie, 2021, p. 227) which threaten human survival, the role of the WTO in ensuring sustainable development has come more into focus. However, the primary goal of WTO is not to safeguard the global environment, and its ambit is restricted to “trade-related environmental policies” (Santarius et al., 2004; Baron and Garrett, 2017; Zhang and Xie, 2021). Rather the ambit of environmental protection and its linkage to international trade has shifted to regions and individual countries as the European Union (EU) has passed a proposal to levy carbon tariff policies through a carbon border adjustment mechanism in March 2021 and other developed countries including the US are also considering similar proposals. However, it is likely that such a mechanism will come at “the cost of developing countries that are at the stage of energy-intensive industrial development and are seeking to increase their share of global industrial and manufacturing production” (Zhang and Xie, 2021, p. 234).

The recurring debate between developing and developed countries regarding IPRs has once again come into focus with the COVID-19 pandemic as several developing country members led by India and South Africa proposed a waiver to the WTO’s Trade-Related Aspects of Intellectual Property Rights (TRIPS) Agreement “in order to speed up the access to affordable medical products for the prevention, containment or treatment of COVID-19 to all member countries” (Cabatbat, 2021, p. 1), which has also received support from the US. The economic argument for IPRs states that strong protections ensure that innovators are adequately compensated which results in higher economic growth. While developing countries have largely opposed strong IPRs in the WTO, it is possible that strong IPRs could increase technology transfer through licensing leading to lower production costs in developing countries, thereby increasing exports (Yang and Maskus, 2009). However, excessively strong IPRs have the potential to limit competition and welfare and slow down the catch-up process of growth in developing countries (Boldrin and Levine, 2002; Yang and Maskus, 2009).

The extent to which developing countries can comply with increasingly complicated WTO rules and obligations, best exemplified by the highly complex TRIPS Agreement, and take advantage of the WTO’s dispute settlement mechanism

depends critically on developing country capacities. Before the Seattle Ministerial, the WTO in 1998 released a briefing note which acknowledged that “developing countries lack the financial and human resources to fulfil their commitments such as the complex requirements of the intellectual property agreement.”² As WTO rules have become increasingly complicated, another quasi-parametric change, the burden on developing countries has increased proportionally, which requires ever more resources on the part of developing countries. Similarly, developing countries, particularly LDCs, in many cases do not have the technical capacity and financial resources to effectively participate in the WTO’s dispute settlement, with only 1 percent of cases involving an LDC (Tania, 2013).

Lastly, the definition of what constitutes a “developing country” is an issue which has become increasingly important as countries have seen their economies grow dramatically in the two decades since the WTO was established, partly due to their membership in the WTO, thus qualifying as another quasi-parametric change. Currently, the WTO has no exact definition of a “developing country” and countries are allowed to declare themselves as either developed or developing. However, other countries are allowed to challenge the decision of a country to exploit the provisions granted to developing countries. This issue has come into focus, particularly with China’s emergence, and, although it has few practical implications, has led to allegations of the misuse of WTO rules to gain an unfair advantage in global trade.³

V. Emerging challenges to multilateralism in the post-pandemic world

The COVID-19 pandemic has shaken the global economy and to some extent further undermined the WTO, with critics asserting that “the WTO was largely missing in action, as many members resorted to unilateral imposition of export restrictions for medical supplies and personal protective equipment” (Hoekman, 2020, p. 338). Beyond the immediate response to the pandemic, the changes in the global economy brought about by the pandemic pose several new challenges to trade multilateralism, particularly dealing with adjustment costs and deepening global structural changes, the re-strengthening of global value chains (GVCs), confronting the institutional challenges posed by rapid technological change, and overcoming the constraints of

²Available from: https://www.wto.org/english/thewto_e/minist_e/min99_e/english/about_e/05impl_e.htm (online; cited April 2022).

³Available from: <https://www.eastasiaforum.org/2019/10/15/chinas-developing-country-status-brings-it-few-benefits-in-the-wto/> (online; cited April 2022).

geo-political considerations. How the WTO responds to these challenges will determine the extent to which multilateralism can be revived and aid the launch of a new wave of globalization.

One of the major shifts brought about by the pandemic has been the rapid shift to remote work, enabled by new technologies that allow workers to continue to process and share information, and interact and cooperate with others without face-to-face contact, particularly in the services sector. Baldwin (2019) argues that the services sector has so far been shielded from globalization because services required face-to-face contact. However, hastened by the necessities brought about by the pandemic, the emergence and acceptance of effective digital technologies make it increasingly likely that this no longer will be the case in the future. Given the relative wage differences between developed and developing countries, it is likely that a large proportion of service firms will resort to “tele-migration”, that is, exploit these relative wage differences, leading to a large shift in trading patterns between developed and developing countries.

The contemporary global economy today is a highly interconnected one, with most production processes being conducted through an interconnected network of GVCs. This observation is supported by the high proportion of international trade that occurs in intermediate goods and services, with one estimated being above 60 percent of global trade (Strange, 2020). In normal times, the economic utility of GVCs is manifold, providing cost advantages, overcoming domestic capacity constraints, and resilience against domestic disruptions. However, the pandemic has led to widespread disruption of the international movement of goods and labor, thereby increasing the transaction costs that made GVCs attractive in the first place. In response, several governments have stressed the need for countries becoming self-reliant to ensure that the production of critical goods and services remains domestic and thus resilient to future global shocks like the pandemic, reflective of a possible trade-off between efficiency and resilience of GVCs (Alfaro and Faia, 2020; Galston, 2020; Goldberg, 2020; Song and Zhou, 2020).

The pandemic has also led to an acceleration in digital trade and e-commerce between countries. As digital technologies and global data flow proliferate, it is incumbent on governments to harness the benefits of these new technologies but also preserve the integrity of their domestic regulatory mechanisms. The current trend towards digitization has resulted in an increase in data localization requirements by governments, such as the EU’s General Data Protection regulations. While such provisions may be important for privacy and cybersecurity purposes, it is important to recognize the trade-offs associated with such regulations, as they may reduce the

economic benefits that these technologies provide. It is also important to acknowledge that data localization efforts may also have protectionist goals of protecting domestic firms from foreign competition, which violates the spirit of the national treatment principles of the WTO.

Lastly, changing geo-political circumstances, especially increased strategic competition between the US and China in the Indo-Pacific region and the ensuing trade war, continue to become ever more tense leading to an undermining of multilateral trade cooperation. As discussed earlier, the emergence of China can be understood as a quasi-parametric change with China's accession into the WTO underpinning its successful export-oriented growth strategy. Together with increasing geo-political tensions, the rise in nationalist and populist sentiments across many countries also poses a risk to multilateral cooperation as governments turn inwards and eschew international cooperation for domestic political goals.

VI. The role of regional groupings: Building blocks to new multilateralism?

As multilateral negotiations have stalled, bilateral and regional trade agreements (RTAs) have proliferated and emerged as an alternative for like-minded countries to continue to cooperate on international trade in pursuit of continued economic growth. These groupings allow countries to continue pursuing an internationalist economic agenda and cooperate on issues that are not easily resolved in a multilateral setting such as the WTO. However, three aspects of RTAs have raised concerns: that they would increase trade diversion, that broader trade liberalization would stall, and that they would undermine multilateralism (Freund and Ornelas, 2010).

Empirical analyses of RTAs, however, suggest that concerns regarding trade diversion have largely been excessive, with trade creation rather than diversion being the norm (Freund and Ornelas, 2010). Moreover, as multilateral negotiations have stalled, RTAs have been the only tool through which trade liberalization has progressed as such agreements have increased manifold. The answer to whether or not RTAs favor or impede multilateralism so far remains inconclusive. While some authors stress that regionalism has led to an undermining of multilateralism (Levy, 1997; Krishna, 1998; McLaren, 2002), others have argued that this does not need to necessarily be the case (Baldwin, 1995; Riezmann, 1999; Ornelas, 2005). Rather, the effect of regionalism on multilateralism is closely tied to whether regional groupings are open or not, with regionalism being a stumbling bloc if they are open to new members but not otherwise (Freund and Ornelas, 2010).

Despite the ongoing debate on the effects of regionalism on multilateralism, three observations favor the view that RTAs can function as a building block of the next wave of multilateralism. First, WTO rules provide the legal basis for countries to pursue RTAs and require RTAs to “cover substantially all trade – unless they are under the Enabling Clause – and help trade flow more freely among the countries in the RTA without raising barriers to trade with the outside world.”⁴ Second, while a large number of RTAs are bilateral agreements, recent RTAs involve a larger group of countries, such as the Comprehensive and Progressive Trans-Pacific Partnership (CPTPP) involving 11 countries, and the Regional Comprehensive Economic Partnership (RCEP) involving 15 countries. Third, along with a larger number, RTAs have a much larger scope compared to WTO rules and provide a template for trade cooperation to be multilateralized.

VII. The agenda for carrying out the WTO reform

In the section titled “What we do”, the WTO website categorizes its main functions into five main categories: trade negotiations, implementation and monitoring, dispute settlement, building trade capacity, and outreach.⁵ As described earlier, the central transaction of the WTO is to ensure that countries commit to restraining unilateral trade and trade-related policy decisions in exchange for reciprocal restraint from other countries. Each of the functions described above can then be thought of as the specific auxiliary transactions that support the central transaction to ensure that member countries have the incentive to follow WTO rules and that the WTO as an institution is re-enforced. However, the failure of the WTO to carry out these auxiliary transactions lowers the incentive for members to continue to follow WTO rules, thereby undermining the WTO as an institution.

With trade negotiations being stalled since the beginning of the Doha Round, one of the ways forward has been the expansion of “plurilateral negotiations” which involve only some countries rather than the entire WTO membership (Jones, 2021). Being a consensus-driven organization, it is difficult to proceed with negotiations as individual countries possess veto power to stall negotiations, as was witnessed through India’s blockage of the implementation of the “Bali package” agreed upon in 2013, a modest agreement that primarily involved a Trade Facilitation Agreement that lowered the transaction costs of international trade through a simplification of

⁴Available from: https://www.wto.org/english/tratop_e/region_e/scope_rta_e.htm (online; cited April 2022).

⁵Available from: https://wto.org/english/thewto_e/whatis_e/what_we_do_e.htm (online; cited April 2022).

customs rules and processes. One way to reduce the likelihood that negotiations are impeded by a very small group of countries would be to replace the consensus approach with voting rules, which allow agreements to proceed if a large proportion of countries are on board. However, such a move may result in an undermining of the legitimacy of the WTO and in the marginalization of the WTO's smallest and poorest members.

The implementation and monitoring mechanism of the WTO is equally important towards ensuring that the central transaction of the WTO is re-enforced as members have to be confident that they are fulfilling their obligations. The monitoring mechanism of the WTO involves a large number of specialist committees. While seemingly straightforward, monitoring is complicated by the differing level of development between members as poorer members often lack the capacity to provide up-to-date notifications of their trade policy. For example, the chair of the subsidies committee in 2019 highlighted that “77 WTO members [had] not submitted subsidy notifications for 2017, 62 members [had] still not submitted subsidy notifications for 2015, and 55 members still had not submitted subsidy notifications for 2013.”⁶ Ensuring that developing countries have the technical and financial support required to notify the WTO of developments in trade policy, therefore, remains an important reform priority for the WTO.

The dispute settlement arm of the WTO has perhaps been the most controversial auxiliary transaction, one which is crucial to help resolve trade disputes and re-enforce members' confidence in the institution. However, the dispute mechanism has come under increasing criticism from members due to “delays in the adjudication process and disagreement over the AB's [Appellate Body] competence” (Akman et al., 2020, p. 7). While cases under the purview of the AB have proliferated, the rulings of the body have been criticised for being arbitrary due to the “ambiguity of the extant rules” (Bhagwati et al., 2014, p. 24). Under the Trump Administration, the US Trade Representative has forcefully criticized the AB stating that “the conduct of the Appellate Body has converted the WTO from a forum for discussion and negotiation into a forum for litigation.”⁷ With the failure to appoint new judges to the AB in 2019, the AB is no longer active, resulting in a lack of a forum to resolve trade disputes and increasing the chances of continued trade wars. As a stop-gap solution, 10 members notified the WTO of the formation of a Multi-Party Interim Appeal (MPIA)

⁶Available from: https://www.wto.org/english/news_e/news19_e/scm_30apr19_e.htm (online; cited April 2022).

⁷Available from: <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2020/february/ustr-issues-report-wto-appellate-body> (online; cited April 2022).

arrangement to resolve disputes. Reforming the AB and expanding the MPIA to ensure that members have a forum to resolve disputes remains a high-priority agenda for WTO reform.⁸

For the WTO to embark on an ambitious and successful reform agenda requires leadership across various forums, including the G20, the G7, as well as individual support from major economic players such as the US, the EU, Japan, China, and India. As highlighted by Akman et al. (2020, p. 2), the “G20 represents a critical mass of world trade and must play a collective leadership role with deliberate dialogue to provide a coherent approach that identifies divisions and creates solutions.” The importance of WTO reform was recognized in the 2018 G20 Leaders’ Communique which stated that “international trade and investment are important engines of growth, productivity, innovation, job creation and development. We recognize the contribution that the multilateral trading system has made to that end. The system is currently falling short of its objectives and there is room for improvement. We therefore support the necessary reform of the WTO to improve its functioning.”⁹ Identifying critical roadblocks and working together to resolve issues is therefore crucial for the reform agenda to be sustained and for the beliefs in the WTO to be re-enforced.

VIII. The role of China in promoting global reintegration

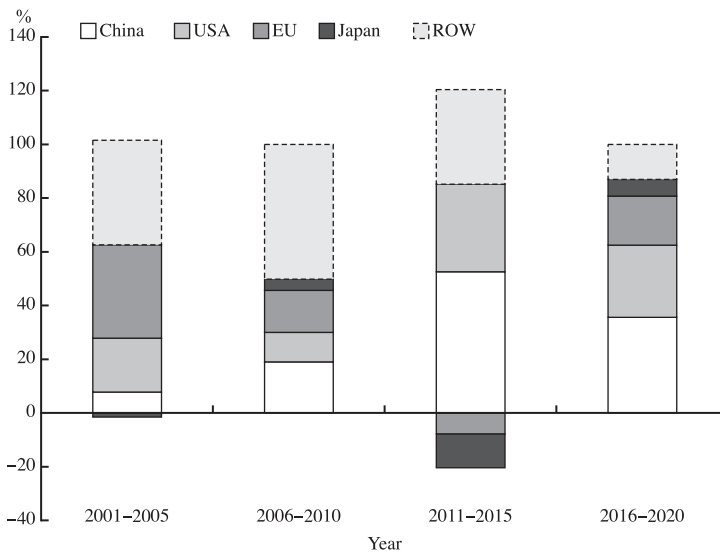
China’s emergence as one of the largest economies in the world means that any successful reform of the WTO will require the full backing and support of the Chinese government. China’s accession to the WTO in 2001 was a historical move in the middle of domestic economic reform, allowing China to act based on a rules-based system. China’s contribution to global growth has increased substantially in the post-GFC period, from less than 10 percent between 2001–2005 to over 50 percent in 2010–2015. While reducing in the latter half of the decade (2016–2020), China’s contribution to global growth has remained high at 36 percent (Figure 3). As China has grown, the international spillovers of China’s domestic economic policy have also increased proportionally, thus making the need for coherence between domestic policy to comply more fully with WTO rules ever more important.

⁸Available from: <https://trade.ec.europa.eu/doclib/press/index.cfm?id=2176> (online; cited April 2022).

⁹Available from: https://www.consilium.europa.eu/media/37247/buenos_aires_leaders_declaration.pdf (online; cited April 2022).

It is also crucial to recognize that a multilateral approach is consistent with China's long-term goal of continued economic growth and development. Since China embarked on its economic reform agenda in the late 1970s, there has been a large increase in China's integration with the global economy alongside an increase in private sector participation in the Chinese economy. The US–China trade war has resulted in a reduction in production in both China and the US, with Itakura (2020) estimating a reduction in GDP of around 1.4 percent for both countries. The current re-balancing of the Chinese economy from an investment and export-led strategy towards domestic consumption also requires continued economic growth which is impeded by the uncertainty of trade policy regulation. As growth in China continues to slow down as the fruits of catch-up growth diminish, continued engagement with the global economy is crucial for China to continue to reap the benefits of global innovation and technological growth in boosting domestic economic growth and consumption.

Figure 3. China's contribution to global growth has increased substantially



Source: World Bank, World Development Indicators (see: <https://databank.worldbank.org/>).

Note: ROW, rest of the world.

In order to revitalize both the Chinese economy and the multilateral rules-based trading system, it is therefore important that domestic reform in China concerning state-owned enterprise reform, competition neutrality and intellectual property rights align

closely with WTO rules. China's recent application to join the CPTPP would require China to adhere to rules that are even more stringent than those required by the WTO. In this context, it is consistent for China to carry out or deepen domestic reform as a precondition for entering high-level regional groupings such as the CPTPP as well as for enhancing multilateral arrangements.

One area where China can show its commitment towards a multilateral and collaborative approach is to ensure that it follows a rules-based approach in its Belt and Road Initiative (BRI). So far, the BRI has largely followed a transaction-based approach and has largely been focused at the bilateral and regional levels (Zhou, 2020). However, as the BRI becomes larger and encompasses more countries, it will become more exposed to existing international rules and standards. To ensure that the BRI does not divide the world into "spheres of influence" and competing for trade blocs, it would be crucial that China formulates the future of the BRI from a rules-based and multilateral perspective.

Over the upcoming decade, China has the opportunity to be a responsible, inclusive, and cooperative global power. At the United Nations General Assembly in September 2020, President Xi Jinping stressed the "indisputable reality" of economic globalization, stating that "We should see each other as members of the same big family, pursue win-win cooperation, rise above ideological disputes, and not fall into the trap of 'clash of civilizations' ... We should pursue open and inclusive development, remain committed to building an open world economy, and uphold the multilateral trading regime with the World Trade Organization as the cornerstone."¹⁰ For a revival of multilateralism, it is important that this rhetoric is reflected in the reality of China's economic relations with its trading partners to ensure that both China and the global economy continue to benefit from each other.

IX. Conclusion: Challenges ahead with a dynamic view on future multilateralism

In this paper, we pointed out a number of quasi-parametric changes, the rise of China and resulting US–China strategic competition, changing global comparative and relative prices, rapid technological change and increasing complexity of trade rules, that are once again pushing the world away from trade multilateralism. These ideas are summarized in Table 1.

¹⁰Available from: https://www.fmprc.gov.cn/mfa_eng/zxxx_662805/t1817098.shtml (online; cited April 2022).

Table 1. Theoretical framework applied to the case of the GATT/WTO

Case	Institution (Transaction covered by the institution)	Shared institutional elements	Differentiating institutional elements	Quasi-parameters	Why self-enforcing	Why not self-enforcing
GATT	Trade multilateralism (collective restraint on unilateral trade policy)	Organization: countries as fundamental units	Beliefs: trade promotes peace and prosperity; Norms: informal negotiations and dispute settlement	Relative economic size of countries, relative prices of goods, technological change	Trade helped WWII recovery in Europe and build US hegemony during the Cold War era increasing the US willingness to bear the costs of public goods. East Asian economies benefited from trade encouraging other countries to join GATT	
WTO			Beliefs: trade creates winners and losers and may not promote peace; Norms: formalized negotiations and dispute settlement			Trade reduces (increases) relative size and comparative advantage in the manufacturing of the US (China) leading to less incentive for the US to bear the costs of public goods. Trade drives technological change and increases the complexity of rules. An increasing number of countries makes consensus building difficult

Notes: GATT, General Agreement on Trade and Tariffs; WWII, World War II.

The last time the world experienced rapid de-globalization was when, in response to the Great Depression increased tariffs by the US were met by retaliatory tariffs by a host of other countries. The result was a further slowdown in both the US and global economy and the break-out of WWII. Similar to the inter-war period, there has also been a rise in populist and nationalist sentiments across the world that are making governments eschew open trade and look increasingly inward.

What do these trends imply for the future of multilateralism and globalization? It seems safe to say that it is unlikely that the patterns of hyper-globalization driven by multilateral cooperation seen between the 1980s and 2008 will not be repeated. While COVID-19 has disrupted GVCs and brought into focus an apparent trade-off between efficiency and resilience, the unwinding of GVCs will also not be a straightforward task as most production processes have become widely distributed. Overall, the most likely scenario is that globalization may proceed in a much more limited way, with large regional groupings emerging as more countries look for alternative ways to cooperate on specific issues.

The revival of multilateralism in our view depends greatly on whether the changes in quasi-parameters can be reversed. First, although US–China competition has increased, on specific issues such as climate change there has been a revival of cooperation between the two superpowers, which may spill over into other areas including trade cooperation.

Second, the heterogeneous impacts of trade in developed countries can be met by better re-distribution that can provide support for communities that are hurt by globalization. While economists have often supported trade as a mutually beneficial transaction between countries, there is also increased appreciation of the reality that trade creates winners and losers within countries. The unequal impact of trade has been felt acutely in the US and the UK, where communities that have been hurt by trade have rallied politically leading to a populist movement against economic integration (Jones, 2021; Hoekman, 2021). Ensuring that populist movements in developed countries do not derail further globalization requires that communities in these countries that are hurt by integration are involved more closely in the dialogue and compensated fairly when and if they bear economic losses.

Third, developing countries have benefited immensely from globalization, and a rapid trend of de-globalization may now provide an impetus for developing country leaders to help overcome the challenges that have plagued the WTO since the launch of the Doha Round. The COVID-19 pandemic and climate change are global problems, getting through which will require global cooperation across a number of dimensions, including public health, trade, investment, and the environment, to ensure that the gains of the past three decades are not lost. A dynamic view of trade multilateralism requires that global leaders view the global trading system in relation to the broader international governance system, and work together to revive both multilateralism and globalization. What the world community does now matters more than ever, for the health of the public, the economy, and the environment.

These changes can be a catalyst to reverse the quasi-parametric forces discussed in this paper which have undermined the multilateral trading system over the last two decades. While US–China competition may intensify in several areas, the two superpowers must transcend differences in ideologies, geopolitical considerations, or even narrowly defined national interests when it comes to revitalising trade multilateralism. Following their lead, other major powers such as the EU, Japan, and India and other developing countries can help to re-enforce the system or at least prevent it from collapsing due to the undermining forces. These changes could then further the range of parametric values of multilateralism under which the system is re-enforced.

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(Edited by Lin Zhang)