

What the Covid-19 Crisis Means for the WTO Trading System

By Kiichiro Fukasaku



Author Kiichiro Fukasaku

Concerns Over the Functioning of the WTO Trading System

A yellow flag was raised to the World Trade Organization (WTO) on March 12, 2020, one day after Covid-19 was declared as a pandemic. Director-General Roberto Azevêdo announced that it would be no longer feasible to organize the 12th Ministerial Conference (MC12) – the organization’s highest decision-making body – scheduled for June 8-11 in Nur-Sultan, the capital of Kazakhstan. Then the WTO decided to suspend all meetings until the end of April, disrupting the critical phase of trade negotiations in the run-up to MC12. This was followed by Azevêdo’s sudden announcement on May 14 that he will step down on Aug. 31.

Coronavirus has no respect for borders. Sooner or later, all infected countries have had to grapple with acute shortages of essential supplies and protective gear for health professionals working on the front lines, let alone life-saving ventilators for hospitalized patients requiring intensive care. They have enforced social distancing, lockdowns, and widespread closures to avoid viral transmission and safeguard healthcare systems. The social and economic damage entailed will be unprecedented, as we must likely wait for a vaccine or cure for the next 12 to 18 months. The burdens fall heavily on those least able to carry them. As soon as the spread of coronavirus is brought under control, they begin to phase out containment measures and reopen their shattered economies. According to the IMF’s latest *World Economic Outlook* published in April, the global economy is projected to contract by 3% in 2020, before growing by 5.8% in 2021 in its baseline scenario in which the pandemic fades in the second half of 2020 and economic activities are back to normal with strong government support measures.

But as the report acknowledges, it is extremely uncertain whether post-pandemic global recoveries will be swift and strong. Much depends on epidemiological pathways and human responses to economic reopening in the coming months. We should prepare for a worse scenario that global recoveries might be staggered and unbalanced, as some countries would be struggling more than others, due to a recurrence of an epidemic not seen since the great influenza pandemic of 1918-20. Economic nationalism has been flaring up around the globe during public health crises, despite an appeal for global solidarity made by the director-general of the World Health Organization (WHO) at the G20 Extraordinary Leaders’ Summit in late March. What concerns us today in such a global

environment is the functioning of the WTO trading system tomorrow.

World Merchandise Trade During Public Health Crises

The novel coronavirus, which originated in Wuhan in November-December 2019, had spread very quickly both within and outside China and exploded into a pandemic by March 2020. (The origin of the SARS-CoV-2 virus that caused the Covid-19 pandemic has been disputed, but we take note of the experts’ view as seen on <https://nextstrain.org>.) The pandemic has exposed all infected countries to public health crises, and then supply and demand shocks, driving their economies into freefall.

Global Supply Chains Get Clogged

Since late March, the WTO has regularly updated a list of trade measures implemented by members in the context of the Covid-19 crisis. This list points to two determining features of world trade today. First, the number of temporary export restrictions on certain medicines and medical devices is substantial and increasing. A proliferation of export restrictions and a drastic fall in international transport services have combined to get global supply chains clogged for medical products. A Global Trade Alert report concludes that “[t]he incoherence between national trade policies and medical response threatens the lives of people at home and abroad, including those of front-line health professionals” (<https://www.globaltradealert.org/reports>).

Import Tariffs on Medical Supplies and Protective Gear Remain High

Second, the number of temporary eliminations or exemptions of import duties on medicines, medical supplies, and ventilators is on the rise – a welcome development. Imports of medicines are already duty-free or subject to low rates in many countries. WTO data show the average most-favored-nation (MFN) applied tariff on medicines is 2.1%, with 72 members maintaining duty-free access (https://www.wto.org/english/news_e/news20_e/rese_03apr20_e.pdf). This is partly thanks to the WTO Pharmaceutical Agreement, a reciprocal tariff elimination agreement (so-called “zero-for-zero initiative”) concluded by major producing countries during the Uruguay Round negotiations. The current participants in the Agreement are Canada, the European Union, Japan, Macao, Norway, Switzerland, and the

United States. Among other categories of medical products, trade in medical equipment enjoys relatively low duty rates (3.4% on average), as a substantial part of technology-intensive medical equipment has been covered by the expansion of the Information Technology Agreement (ITA) in December 2015. On the other hand, the average MFN applied tariff rate remains relatively high for medical supplies (6.2%) and personal protective equipment (11.5%).

Table 1 shows the world tariff profiles of three specific products – diagnostic reagents (HS 382200), medical ventilators (HS 901920), and hand sanitizer (HS 380894) – based on the WHO classification reference for Covid-19 medical supplies at the six-digit level of the Harmonized System. As for the first two products, many countries, rich and poor, maintain similar tariff profiles with duty-free imports adopted by 81 out of 134 WTO members included in Table 1 for diagnostic reagents and by 67 members for medical ventilators. On the other hand, the world tariff profile for hand sanitizer is different: only 36 members allow duty-free imports, while 16 members – mostly African countries – maintain high duties of more than 15%. These developing members may wish to ramp up domestic production under high import protection, but it raises the question of whether such trade protection lives up to their objectives.

TABLE 1

World tariff profiles for 3 specific medical products

HS 6 Digit Code	382200	901920	380894
Tariff Range	Diagnostic Reagents	Medical Ventilators	Hand Sanitizer
Number of WTO Members per Average MFN Applied Tariff Band			
15 < t	2	1	16
10 < t <= 15	1	3	22
5 < t <= 10	18	18	17
0 < t <= 5	32	45	43
t = 0	81	67	36
Simple Average of MFN Applied Duties	2.7	3.3	7.0
Standard Deviation of MFN Applied Tariffs	4.2	4.3	6.7
Maximum Tariff Rate	26.0	26.0	26.0

Source: Compiled by the author from WTO, Integrated Database (IDB) notifications (accessed on April 3, 2020)

Trade Locomotives Are Broken

According to the WTO report published in April, world trade volume is likely to fall between 13% and 32% in 2020, depending on two distinct scenarios, optimistic and pessimistic (https://www.wto.org/english/news_e/pres20_e/pr855_e.htm). What trajectories world trade will take during the second half of 2020 and beyond is anybody's guess. Nonetheless, the WTO's scenario analysis leads us to anticipate that world trade after the pandemic is unlikely to return to its previous trend, as in the case of the global financial crisis of 2008-2009. This time, world merchandise trade is likely to be much less responsive to world GDP growth, due to disruptions in global supply chains and a drastic fall in traded services, except for information technology services. To this should be added that world merchandise trade was already slowing or even falling before the pandemic hit major trading nations (Table 2). For example, world import volume was showing negative trends in advanced economies since November 2019. Similarly, the monthly growth of China's import volume was decelerating to register a negative growth of 7.3% in January 2020. Also notable is that the pandemic struck China's export juggernaut, pulling it down to a decline of 11.6% in the same month. The export shock hit all emerging economies, with a fall of 4.3%. For both Latin America and Africa and the Middle East, the trade impact of Covid-19 has been relatively mild so far, but it is expected to show a bigger negative impact as the viral infection continues. Therefore, trade locomotives are all broken this time.

Nonetheless, according to the latest data, China, and other Asian economies were showing some early signs of recovery from the worst trade slump, which may reflect their different responses to the public health crisis. It remains to be seen whether such trade recovery will continue and spread to other regions.

7 Questions on the Future of the WTO Trading System

WTO members are confronted with a broad set of questions, many of which have been discussed over the past two years, such as at the G7 Leaders' Summit at Charlevoix on June 8-9, 2018. The Covid-19 pandemic has added a sense of urgency, as well as some emerging challenges. I will focus on seven questions to see whether the WTO trading system can function as effectively as it should in this extraordinary time.

Decision-Making and Procedural Guidelines

Decision-making by consensus is the *modus operandi* of the WTO and its predecessor, the General Agreement on Tariffs and Trade (GATT). Members are obliged to meet through teleconferences during the pandemic. Although the latest technologies enable them to do so, they also present many hurdles to be overcome for

TABLE 2

Trends in world merchandise trade (volumes, seasonally adjusted)

Regions/Countries*	percentage changes, month on month					
	2019m10	2019m11	2019m12	2020m01	2020m02	2020m03
World trade	0.4	-0.8	0.4	-1.6	-0.7	-1.4
World imports	0.1	-0.8	-0.2	-1.0	-1.7	-0.9
Advanced economies	-0.6	-1.7	-0.2	-0.1	-1.0	-3.1
US	-1.8	-1.4	2.8	-2.1	-1.9	0.3
Japan	-2.0	-1.6	1.1	-2.3	-8.7	13.5
Euro Area	-0.6	-0.6	-1.9	0.9	0.6	-7.6
Other advanced economies	0.7	-3.7	-0.7	0.8	-0.8	-3.4
Emerging economies	1.1	0.6	-0.1	-2.4	-2.6	2.3
China	2.6	2.0	0.1	-7.3	-3.2	6.2
Emerging Asia (excluding China)	0.6	0.8	-0.3	-0.6	-3.5	3.2
Eastern Europe/CIS	0.3	0.6	3.2	-3.6	0.0	-2.1
Latin America	0.8	-2.3	-1.0	1.1	-1.5	-2.5
Africa and Middle East	0.2	0.1	-0.5	-0.2	-0.1	-2.3
World exports	0.8	-0.9	0.9	-2.1	0.2	-1.8
Advanced economies	0.6	-0.9	0.1	-0.4	1.0	-6.0
US	-0.4	0.5	1.2	-1.7	2.0	-4.9
Japan	-0.8	-1.0	0.9	-2.2	2.1	-3.4
Euro Area	1.5	-1.9	-0.3	0.3	1.0	-7.7
Other advanced economies	-0.0	0.2	-0.2	-0.2	0.1	-4.7
Emerging economies	1.1	-0.9	1.9	-4.3	-0.9	3.8
China	-0.6	-0.7	5.4	-11.6	-2.2	12.4
Emerging Asia (excluding China)	2.3	-1.0	2.1	-2.4	-0.3	0.7
Eastern Europe/CIS	-0.6	-2.7	-1.9	0.0	-1.1	-1.8
Latin America	0.0	-1.9	-0.2	-0.1	-0.8	2.3
Africa and Middle East	4.3	1.8	-1.4	-0.2	0.2	1.3

* Regional aggregates are computed with shares in world imports.

Source: Calculated by the author from CPB World Trade Monitor database: <https://www.cpb.nl/en/cpb-world-trade-monitor-march-2020> (accessed on May 26, 2020)

ministers and senior officials from the 164 members to meet virtually and take big decisions in a ministerial conference, which takes place normally once every two years and lasts for several days involving many backdoor consultations and corridor meetings. This consideration leads us to anticipate that, as long as the coronavirus stays with us, the General Council will play a more important role than ever, as it “shall meet as appropriate” at the level of ambassadors and other officials in Geneva, conduct its functions “in the intervals between meetings of the Ministerial Council”, and “establish its rules of procedure and approve the rules of procedure for the Committees” (Article IV: 2 of the Agreement Establishing the WTO). A proposal for “Procedural Guidelines for WTO Councils and Committees Addressing Trade Concerns” has been tabled to the General Council for adoption. It aims to streamline meeting arrangements, make deliberations more responsive to emerging trade concerns, and resolve them informally at the level of committees without recourse to the formal dispute settlement mechanism (see below). This is intended to respond to the often-

heard criticism of the WTO that it has become a “litigation-centered” organization. Are WTO members ready to move ahead with such new procedural and decision-making arrangements in the time of Covid-19?

Transparency and Notification

Enhancing the transparency of members’ trade and trade-related policies is fundamental to sustaining an open and rules-based multilateral trading system as embodied in the WTO Agreements. At no time is this more critical than during the pandemic. Based on notification by members and information obtained from other public sources, the WTO Secretariat has created and updated a database of trade measures concerning the coronavirus-relevant medical and other products, such as food. This database can assist members in their efforts to stand still and roll back export prohibitions and restrictions that were imposed *temporarily* during the public health crises. In the past, many members have tended to leave notification obligations under the different WTO Agreements unattended because of capacity constraints or for other reasons. Proposals have been tabled to ameliorate such situations by allowing cross-notifications from other members, and in egregious cases, by imposing certain penalties on members concerned. The WTO Secretariat is being increasingly called upon to

assist members fulfilling notification obligations and voluntary submissions during the pandemic. Are current WTO staff and resources large enough to help members meet such transparency requirements?

Fairness

Fairness is one of the most important principles of the WTO trading system. The Covid-19 pandemic has raised a few questions about fairness in world trade today. First, as we discussed above, governments have responded to public health crises by enforcing export restrictions on medical supplies and personal protective equipment, while at the same time amassing them for domestic use. A global shortage of face masks, for instance, is a telling episode: a combination of export ban, hoarding and price gouging by some powerful countries has made it difficult for others to import such essential products at affordable prices. As a result, these medical products have become scarce commodities everywhere. Current WTO rules, under the so-called general exceptions, provide broad

space for members to adopt restrictive trade measures necessary to protect public health within their jurisdictions. However, export restrictions and aggressive procurement practices are counterproductive to the global fight against the pandemic, and contrary to the spirit of solidarity proclaimed by G20 Leaders. WTO members should consider rules for fair conduct of international transactions based on the Covid-19 experience.

Second, governments have often used contingency protection – the mix of instruments, such as countervailing, anti-dumping and safeguard measures, which are triggered contingent on certain circumstances, such as subsidization, dumping and import injuries. Countervailing and anti-dumping duties have been frequently applied to protect domestic firms and workers in agriculture and certain manufacturing industries, like iron and steel, from “unfair” foreign competition. This is another area of concern in the post-pandemic economic environment, as governments are susceptible to domestic political pressures for import protection arising from those coronavirus-affected industries that are suffering from evaporating demand due to social distancing and prolonged lockdowns.

A third area of concern is the distortions caused by “non-market practices” in which governments intervene to distort market competition in favor of domestic firms by way of administrative guidance and other directives. The Trilateral Initiative by the EU, Japan, and the US, which began in December 2017, has been instrumental in advancing discussions on industrial subsidies, state-owned enterprises and forced technology transfer. The US has recently made a proposal, entitled “The Importance of Market-oriented Conditions to the World Trading System”, to the General Council. How to deal with “non-market practices” in the WTO is an important issue in the context of Covid-19, as government intervention in resource allocation and economic management is on the rise.

Electronic Commerce and Digital Trade

Affordable access to information and communication technology is critical for people to work, communicate, and go shopping online during the coronavirus pandemic. The digital way of our daily life is likely to continue even after the current crisis is over. This has two ramifications for the future of the WTO trading system. One is that WTO members must accelerate negotiations on a new plurilateral agreement on trade-related aspects of e-commerce, which was kicked off formally at Davos in January 2019. A year later, the number of participating members has increased from 71 to 83, representing over 90% of global trade (<https://www.meti.go.jp/press/2019/01/20200124004/20200124004-2.pdf>). The success of this negotiation is key to the credibility of the WTO itself, and especially of a plurilateral approach to trade negotiations, often referred to as *flexible multilateralism*. To be sure, e-commerce is not

new for WTO members. They agreed in 1998 to launch a “Work Program on E-Commerce”, but since then the rulemaking in the WTO, with the exception of the time-bound moratorium on customs duties on electronic transmissions, has been lagging far behind the digitalization of the global economy.

Another ramification is the urgent need for global trade rules suitable for the 21st century, as the digital revolution is still in its initial stage. Big Data, artificial intelligence (AI) and the Internet of Things are likely to transform almost all manufacturing industries. A case in point is the automobile sector that is finding itself amid major technological and business transformations, widely known as CASE (Connected, Autonomous, Sharing, and Electronic). Thanks to digital technology, financial services are also in the middle of major transformations. For instance, it has helped East Africa play a pioneering role in providing mobile banking for those individuals being denied bank accounts before.

Every country, therefore, has a big stake in WTO rulemaking on e-commerce and digital trade. While certain issues involved are highly political as well as economic, such as protection of personal data, free cross-border data flows, prevention of forced data localization, and prohibition of disclosure requirements for source code and encryption keys, they are not insurmountable. What is fundamental to rulemaking in the WTO is to enhance transparency in members’ policies in the digital age and benefit from greater economies of scale that global market operations can offer. For example, forced localization of storage and data processing does not necessarily increase data protection, as it exposes local data centers to the higher risk of cyberattack. Nor does it facilitate the distribution of information on a global scale, which makes it difficult to realize greater economies of scale.

Development and Differentiation

Development constitutes a core element of the WTO trading system. Yet, nowhere in the WTO Agreements is developing-country status defined, except for the least-developed countries (LDCs) being recognized as such by the United Nations. It is conventional that a member is permitted to self-declare its development status in the WTO. This was perhaps not unrealistic 25 years ago when the WTO was founded, but it is hardly justifiable today when the global economy has become multipolar. The “developed-developing” dichotomy in the WTO membership does not reflect this reality. Nor does it help in negotiations on future trade agreements, which include as an essential component provisions on special and differential treatment (SDT) for developing and least-developed members.

To be sure, differentiation among developing members (other than LDCs) has been incorporated into the WTO trading system. For example, the Agreement on Subsidies and Countervailing Measures

provides them with time-bound and income-based criteria for SDT that have already lapsed. More recently, SDT has taken a new formulation in the Trade Facilitation Agreement (TFA) which came into force in February 2017. The TFA allows developing and LDC members to self-determine their timelines for implementing specific commitments, which is in some cases linked to receiving technical assistance and capacity-building support from the TFA facility. This formulation provides a promising model for future WTO trade agreements. Furthermore, in September 2018, the European Commission made a proposal to modernize the WTO in which developing members other than LDCs were urged to “move away from open-ended block exemptions toward a needs-driven and evidence-based approach” to providing SDT in future trade agreements. The EU proposal also encouraged them to “graduate” the current SDT entirely or in part. Similarly, the US made its own proposal about certain criteria for graduation to the General Council in December 2019.

Global Commons

WTO members can make a specific contribution to protecting global commons: eliminate harmful fisheries subsidies. WTO negotiations on fisheries subsidies received renewed impetus after the adoption in September 2015 of the United Nations Sustainable Development Goals (SDGs), with a specific reference to Target 14.6, which sets a deadline of 2020 to (1) prohibit certain forms of fisheries subsidies that contribute to overcapacity and overfishing, (2) eliminate subsidies that contribute to illegal, unreported and unregulated (IUU) fishing, and (3) refrain from introducing new such subsidies, while at the same time recognizing appropriate and effective SDT for developing countries and LDCs. Since then, WTO members have invested huge political capital in these negotiations, as they are the only active multilateral trade negotiations in the WTO. But the negotiations have been far from straightforward because they must strike a delicate balance between sustainability commitments and development concerns. Opinions have yet to converge, among other things, as to whether to introduce a global cap on use of fisheries subsidies in a new agreement with “comprehensive and effective disciplines”, set as a goal to reach by MC12.

Dispute Settlement and Appellate Review

A functioning dispute settlement mechanism, including fair and effective appellate review of legal matters related to panel reports, is essential to sustain the WTO trading system. Yet the Appellate Body (AB) – the standing body for hearing appeals in the two-tier dispute settlement procedure – has ceased to function since Dec. 11, 2019 when it was unable to make a quorum due to the US blockage of appointments of new AB members for more than three years.

Meanwhile, there have been two important developments. On the one hand, the efforts to resolve this long-standing dispute through the informal process of consultations during 2019, which was led by a facilitator under the guidance of the General Council, have failed. Subsequently, the director-general initiated high-level consultations at the beginning of 2020, which were apparently running into a logjam. On the other hand, the EU and 15 other members have put in place a Multi-Party Interim Appeal Arbitration Arrangement (MPIA), which is a “stop-gap measure” adopted pursuant to the arbitration procedure stipulated under the WTO’s Dispute Settlement Understanding. The establishment of the MPIA reflects the fact that many members share the view that an impartial and independent appeal mechanism is essential for the WTO’s dispute settlement procedure to function, but it also highlights a cleavage that exists between them and the US. The US ambassador to the WTO once explained forcefully the country’s position at the Informal WTO Ministerial Meeting in Davos on Jan. 24, 2020, by saying that “the Appellate Body is not a court and its members are not judges”. However, the US has not yet tabled any concrete proposal to reform the AB.

A recent move by the US to block the adoption by the Dispute Settlement Body of the appellate and panel reports in the case of “United States – Countervailing Measures on Supercalendered Paper from Canada” implies that the dispute settlement mechanism remains in limbo without a functioning appellate review. Therefore, it is not clear what remains to be done if the facilitator’s reform proposal cannot be adopted at the General Council.

Preparing for the Next Crisis

Rebuilding trust in the WTO trading system is essential to sustaining global recoveries in the time of Covid-19. Many affected countries have started to reopen their economies step by step, as a sign that virus infections are becoming subdued. It is fundamental to keep markets open *and* fair, as global businesses restore buoyancy. At the same time, WTO members must prepare for the next crisis, a crisis of climate change, because the costs of inaction – higher incidence of natural disasters related to climate change – would be unbearable to many. A small step for members to take in this direction is to restart plurilateral negotiations on an Environmental Goods Agreement which have remained suspended since late 2016. The Covid-19 pandemic indeed poses formidable challenges to G20 Leaders in restoring global trade health in the future. **JS**

Dr. Kiichiro Fukasaku is an international economist, working extensively in trade, investment, and development fields. His career includes various professional posts at the GATT Secretariat (1983-90) and the OECD (1990-2012), before teaching at Keio University (2012-20).