

# Where Is Free Trade Going?

By Masakazu Toyoda

Free trade has always been recognized as an essential and important policy tool for realizing sustainable economic development worldwide. Sadly, the WTO which is acting as the arbitrator of trade rules, is now dysfunctional. On the legislative front, the Doha Round of trade negotiations shows no signs of reaching any conclusions and on the judicial front, the Appellate Body which is the higher of the two-tier tribunal system, is still without appointed members. Without the Appellate Body, the WTO remains in a situation of empty appeals as the lower panel deliberations cannot be resolved.

Why did this happen? Undeniably, the power and strength of the United States had been crucial to push forward the 'postwar' international rule-making process. Its vast power has diminished so much in the last several years that the U.S. is now considered a "relative" power. The term "global multipolarity" reflects the existence of multiple centers of power for influence.

Another important factor is that China, with its state-led rather than a market-led economic system, clearly benefitted from access to free trade over the last twenty years. With its different set of rules, China is now approaching two-thirds the economic size of the U.S. Incidentally, when China joined the WTO in 2001, its GDP was 30% of that of Japan and 10% of the United States. It is now three times the GDP of Japan. As a result of such growth, the views of the U.S. and the G7 nations are becoming only "one" view relative to those of China and of the emerging nations of the Global South. The multipolarity is making it difficult to forge a consensus on the legislative front.

In addition, it seems that with every election cycle, the U.S. itself is increasingly looking inward, making it clear that with free trade there are winners and losers. Measures for the losers, such as unemployment insurance, support for reskilling, etc. are essential and the U.S. has in place a Labor Adjustment Law which has not yet been used sufficiently.

On the other hand, in the dispute resolution mechanism, the Appellate Body has often ruled differently from the U.S. way of thinking. For example, in trade remedy rules such as anti-dumping and subsidy agreements, the U.S. has complained and expressed the view that it is acting based on its own interpretation of matters, not explicitly provided for in the agreements. As a result of those differences, the U.S. has not approved nominations to the Appellate Body and there has been no members since 2019.

So *where is free trade going?* There are at least four scenarios.

First, leave it as it is.

Second, increase the number of regional or even plurilateral free trade agreements, using the basic rules of the WTO.

Third, from the perspective of economic security, decouple from countries that present different economic rules. That would at the very least, reduce or maybe remove the risks.

Fourth, expand the membership of high-level free trade agreements, such as the CPTPP, to include the EU, the US, and even China. Furthermore, the CPTPP rules could be transplanted into the WTO as a WTO-wide agreement.

Let us consider the characteristics of each scenario and the maximum effort measures for free trade.

The first scenario of "*leaving it as it is*" would only lead to a return to the pre-war chaos. Some efforts should be made to minimizing the impacts and one such effort could include the MPIA (Multi-Party Interim Appeal Arbitration Arrangement). So far, the number of participating countries/regions is limited to 53, including the EU, China, Japan, and others participating. It is unlikely that the U.S. would join, but it is important to encourage Asian countries to join as well as seek the participation of middle powers that cannot afford to play power games. In doing so, it is important to maintain the discipline that was originally meant to be upheld by the WTO's Appellate Body, including not allowing the arbitrary interpretations of ambiguous rules.

The second scenario of "*increasing the number of free trade agreements*" would at the very least exert influences. For Japan, an FTA between China, Japan, and South Korea, as well as one between the Middle East and major countries would be essential. Plurilateral agreements on specific topics, such as digital technologies, would particularly be important but, there is a sense that we are approaching the end of the road on those.

The third scenario that considers "*the viewpoint of economic security*", is also likely to advance inevitably amid the current seriousness of the U.S.-China confrontation. It will take some time, but it will become clear that it is not in anyone's interest to allow a division of world trade. I believe that some kind of proximity/approchement between market-driven and state-driven economic systems will eventually develop.

The fourth scenario of "*expanding to a high-level free trade agreement*" is not necessarily an unrealistic path. With the UK's accession, the number of participating countries to the CPTPP has increased to 12, and it must be possible to further increase that number by attracting not only Asian countries but also the EU. At some point in the future, the U.S. might join but China, which has already showed an interest in joining, may have difficulties because fundamental reforms would be first required. The provision of opaque subsidies and loans to state-owned enterprises, the preference for domestic production in government procurement, data protectionist measures, and forced labor must first stop. However, if achieved, this would lead to a correction of the state-driven economy.

The four scenarios clearly and obviously differ in their time frame. If we believe that free trade is an important policy tool for realizing the economic development of individual countries and of the world, we must not hesitate and start taking action anytime, anywhere.

JS

Masakazu Toyoda is chairman and CEO of the Japan Economic Foundation (JEF). He previously served as chairman and CEO of the Institute of Energy Economics, Japan, after having been vice minister for International Affairs at the Ministry of Economy, Trade and Industry.