

From the Board: Short-term and Long-term Trade Responses to COVID-19

The economic fallout caused by the Coronavirus disease 2019 (COVID-19) pandemic and the associated lockdown measures enacted in many countries already seems likely to be of extraordinary magnitude. Recent S&P forecasts predicted a reduction of GDP in 2020 by 6% in Germany, 8% in France, and 10% in Italy.¹ Everywhere debt-to-GDP ratios are soaring as a result of the unprecedented fiscal response enacted by States to tackle recession and unemployment, with Italy running an anticipated budget deficit nearing 10% of GDP for this year. As of 30 April 2020 30 million unemployment claims were filed in the US. The International Labour Organization warned that almost half of the global workforce – a staggering 1.6 billion people – are in ‘immediate danger of having their livelihoods destroyed’ by the economic impacts of COVID-19. The 2 billion workers in the informal economy, often on short-term contracts or self-employed, already suffered a 60% decline in their income in the first month of the crisis.²

World merchandise trade growth, which in early 2020 was already under pressure from tariffs escalations and sputtering demand, is tumbling down from a combination of production shutdowns, transportation disruptions, and collapsing global demand. The most optimistic scenario forecasted by the WTO expects trade in goods to shrink by 13% in 2020. In the failure of effective coordinated efforts by WTO Members, however, WTO experts warned that the decline could be as high as 32%.³ Similarly, in 2020, the EU Commission expects an economic contraction resulting in a reduction of 9.2% in extra-EU27 exports of goods and services, and an 8.8% decrease in extra-EU27 imports.⁴ United Nations Conference on Trade and

¹ <https://www.spglobal.com/ratings/en/research/articles/200416-economic-research-covid-19-deals-a-larger-longer-hit-to-global-gdp-11440500> (accessed 7 July 2020).

² International Labour Organisation, *ILO Monitor: COVID-19 and the World of Work*, (3d edn, Updated Estimates and Analysis), https://www.ilo.org/wcmsp5/groups/public/-dgreports/-dcomm/documents/briefingnote/wcms_743146.pdf (accessed 7 July 2020).

³ WTO (2020), *Trade Set to Plunge as COVID-19 Pandemic Upends Global Economy*, Press/855 Press Release (8 Apr. 2020), https://www.wto.org/english/news_e/pres20_e/pr855_e.htm (accessed 7 July 2020).

⁴ Chief Economist Team, DG Trade, European Commission, *The Impact of the Covid-19 Pandemic on Global and EU Trade*, (17 Apr. 2020), https://trade.ec.europa.eu/doclib/docs/2020/april/tradoc_158713.pdf (accessed 7 July 2020).

Development (UNCTAD) has estimated a shrinking of global foreign direct investment by 5–15 %.⁵ Short-term measures and especially long-term measures will be key in determining the economic impact of COVID-19. States' commitment to open trade and to the multilateral trade system will be instrumental in determining whether these figures will be worsening and whether the worst-case scenario predicted by the WTO will in fact materialize.

In particular, the early stages of the global crisis have been characterized by restrictions to trade in goods taken in order to ensure that States do not run short of essential medical devices and equipment. Even within the EU, Members initially reacted by turning inwards. Restrictions to the freedom of circulation of medical and protective equipment were imposed in early March by Germany and France, just to be lifted a few days later. The Commission rapidly issued guidelines recognizing the right of Member States to take protective measures against COVID-19, however, affirming that these measures shall be transparent, proportionate and non-discriminatory. The Commission recognized the crucial importance of free circulation to maintain availability of goods essential to tackle the health crisis. It also warned that measures affecting trade should not cause disruption of supply chains, essential services of general interest, and of both national economies and the EU economy. 'Green lanes' for priority and rapid border-crossing of freight transport have been established, and free and safe movement for transport workers has been ensured.⁶ Other relevant trade-related measures include a temporarily waiver of customs duties and VAT on the import of medical devices and protective equipment from third countries, as well as restrictions to trade by establishing export authorization requirements for medical and protective products.⁷

The reaction of the EU has been overall very profound, with a wide set of measures addressing various economic aspects connected to the crisis. In addition to forms of support tackling unemployment, supporting small and medium enterprises and specific sectors, and a historical activation of the escape clause in the Stability and Growth Pact,⁸ competition rules were leveraged as well. The Commission issued flexible State Aid norms empowering Member States to provide direct economic support to companies and small firms as they may risk closing down.⁹ The European

⁵ UNCTAD, *Impact of the Coronavirus Outbreak on Global FDI*s, Investment Trend Monitor (Mar. 2020), https://unctad.org/en/PublicationsLibrary/diaefinf2020d2_en.pdf?user=1653 (accessed 7 July 2020).

⁶ European Commission, *COVID-10 Guidelines for Border Management Measures to Protect Health and Ensure the Availability of Goods and Essential Services*, C(2020) 1753 final.

⁷ Commission Implementing Regulation (EU) 2020/568 of (24 Apr. 2020).

⁸ For an overview of all relevant measures, see, https://ec.europa.eu/info/live-work-travel-eu/health/coronavirus-response_en (accessed 7 July 2020).

⁹ *Commission Communication on a Temporary Framework for State Aid Measures to Support the Economy in the Current COVID-19 Outbreak*, 2020/C 91 I/01.

Competition Network (ECN) also published an unusual statement providing explicit competition guidance to undertakings. The ECN held that it will not intervene against forms of cooperation between undertakings aimed at avoiding goods shortages, but it will enforce competition rules against collusive or abusive price increases of health-related products.¹⁰ Similarly, the Commission illustrated its enforcement priorities in the domain of medical and personal equipment, and even expressed its intention to resume its pre-modernization practice of informal guidance to undertakings.¹¹

At the global stage, more than fifty different forms of trade restrictions were notified to the WTO, mostly in the form of temporary export bans and quotas, temporary export licensing schemes and export control requirements for personal protective equipment, drugs and disinfectants. These measures reflect a nationalist approach in Members' responses, prioritizing (perhaps understandably) national public health over open trade. Some of these restrictions, such as India's decision to stop exporting the hydroxychloroquine drug, have however been rapidly lifted under the pressure of trading partners. Restrictions have also affected three of the four modes of trade in services, (consumption abroad, commercial presence, and presence of natural persons) as countries shut down air travel, production, hotels, restaurants and other shops, and limit personal travels abroad.

Temporary export restrictions to trade in goods are generally justifiable under Article XI:2(a) GATT in the presence of a 'critical shortage' of 'absolutely indispensable or necessary' products.¹² It remains to be seen whether pre-emptive action aiming at stockpiling materials which are not yet scarce in the regulating Member would be considered as covered by Article XI:2(a). Article XX(b) allows trade restrictions (also non-temporary ones) taken with the aim to protect public health, and grants Members considerable degree of flexibility in setting the level of protection in pursuit of that goal. This may result in the justification of considerably restrictive measures in the presence of a high degree of protection of the Member's public health. Restrictions shall also not discriminate among Members and not represent arbitrary and unjustified discrimination among countries where similar conditions apply. It remains to be seen whether all notified export restrictions are in fact enacted on a Most-favoured-nation (MFN) basis, or are not part of non-transparent bilateral deals.

¹⁰ https://ec.europa.eu/competition/ecn/202003_joint-statement_ecn_corona-crisis.pdf (accessed 7 July 2020).

¹¹ *Commission Communication on a Temporary Framework for Assessing Antitrust Issues Related to Business Cooperation in Response to Situations of Urgency Stemming from the Current COVID-19 outbreak*, C(2020) 3200 final.

¹² Appellate Body Report, *China – Measures Related to the Exportation of Various Raw Materials*, WT/DS394/AB/R WT/DS395/AB/R WT/DS398/AB/R, adopted (30 Jan. 2012), para. 326.

The immediate reaction of the international community in the trade domain was not just limited to inward-looking, protectionist, trade restrictions. WTO Members have notified almost as many measures – in the form of import tariffs elimination, suspension of anti-dumping duties and fiscal exemptions – aiming at facilitating the entry into their countries of life-saving equipment and materials.¹³ Even between the US and China, and in spite of the considerable trade tensions that characterized the relation between the two countries in the past years, previous trade restrictions were lifted to smoothen the trade in medical equipment. A possible ‘second wave’ in COVID-19 infections later in 2020 may find the international community less surprised and less prone to export restrictions. Hopefully, better coordination and cooperation in trade in medical devices, drugs and protective equipment will allocate goods more efficiently where needed and contribute to avoid shortages and unreasonable hoarding.

More problematic are restrictions to the export of food commodities enacted by a number of WTO Members under concerns that supply chain disruptions may result in food shortages. These restrictions have also affected cereals and rice, for which there is no evidence of possible future shortages. These measures generated considerable concerns from WTO Members.¹⁴ They also resulted in a rare joint statement by the Directors-General of the Food and Agriculture Organization, the World Health Organization and the WTO that noted that certain measures were unjustified and that ‘uncertainty about food availability can spark a wave of [additional] export restrictions, creating a shortage on the global market’. The statement called on countries to ensure that their trade-related measures do not disrupt the food supply, and urged a renewed commitment to solidarity and cooperation.¹⁵ Shutting down trade and supply chains, not just those of food commodities, has had profound repercussions for the livelihoods of those depending on smooth global trade flows, both in the Global North and in the Global South. Large demonstrations in Bangladesh have already shown the tragic impact suffered from workers and caused by the shut-down of supply chains such as the garment sector.¹⁶

The short-term trade response of the international communities has been characterized by a mix of restrictions to trade and cooperation. However, the greatest challenge ahead lies in the long run. Its outcome will determine whether economic recovery will be ‘V shaped’, ‘U shaped’, or will instead take the dreaded ‘L shape’

¹³ For a full list: WTO, *COVID-19: Trade and Trade-related Measures*, https://www.wto.org/english/tra_top_e/covid19_e/trade_related_goods_measure_e.htm (accessed 7 July 2020).

¹⁴ General Council Committee on Agriculture, WT/GC/208 G/AG/30.

¹⁵ Joint Statement by QU Dongyu, Tedros Adhanom Ghebreyesus & Roberto Azevêdo, *Directors-General of FAO, WHO and WTO* (31 Mar. 2020).

¹⁶ Arabnews, ‘Starving’ Bangladesh Garment Workers Protest for Pay During COVID-19 Lockdown, (13 Apr. 2020).

typical of great depressions. There is not just a risk that temporary restrictions to trade will turn permanent. The COVID-19 crisis has exposed the vulnerability of interconnected global value chains and the hidden costs of a system based on comparative advantage. Single-source providers and geographical specialization in certain regions create fragility in times of crises, causing global supply chains to break down.¹⁷ Many States began questioning whether they are too reliant on foreign production and trade for essential drugs and medical devices.¹⁸ Also companies in advanced economies may see good economic arguments in re-shoring manufacturing from low-cost countries to higher-cost domestic producers. This would however hardly benefit blue-collar workers at home; the trend is likely to speed up automation and further cause downward pressure on wages, fanning the flames of populism and nationalism.¹⁹ The question is thus whether States will resist the nationalist temptation to repatriate production of strategic goods under the imperative of ‘sovereign capability’.

The vulnerabilities to the global trading system were exposed by COVID-19 amidst a climate of distrust towards global trade and active dismantling of the post-war multilateral trading system. In other words, the timing could have not been worse. In reality, the early stage of the crisis has also demonstrated that many States with manufacturing capacity possess considerable adaptability of production: car manufacturers began producing ventilators, fashion brands made medical gowns and face-masks, and cosmetic producers repurposed their production towards alcohol and other disinfectants.²⁰ Conversion of advanced manufacturing is possible, and often rapid; it is not always necessary to bring production back home. This would allow States to retain essential capabilities without losing comparative advantage and the efficiency gains of global trade. Exclusive reliance on national suppliers would not necessarily limit the threat of ‘black swan’ events; quite the opposite, it would just move risks from the international to the national level. Only global diversification and redundancy of supply, in spite of some costs, would alleviate the problem of dependence from single countries such as China, while bolstering resilience.²¹

In any event, a narrow approach to sovereign capability limited to key drugs and medical products would not be as harmful to trade gains and trade specialization as a

¹⁷ H. Farrell & A. Newman, *Will the Coronavirus End Globalisation as We Know It?*, Foreign Aff. (16 Mar. 2020).

¹⁸ The Economist, *Globalisation Under Quarantine*, (29 Feb. 2020).

¹⁹ N. Roubini, *Here are the Biggest Economic Challenges We Face Over the Next 10 Years*, Project Syndicate (1 May 2020).

²⁰ World Economic Forum, *From Perfume to Hand Sanitiser, TVs to Face Masks: How Companies are Changing Track to Fight COVID-19* (2020), <https://www.weforum.org/agenda/2020/03/from-perfume-to-hand-sanitiser-tvs-to-face-masks-how-companies-are-changing-track-to-fight-covid-19/> (accessed 7 July 2020).

²¹ R. Baldwin, E. Tomiura, *Thinking Ahead About the Trade Impact of COVID-19*, in *Economics in the Time of COVID-19* 68–69 (R. Baldwin & B. Weder di Mauro eds, London: CEPR Press 2020).

broader interpretation – extending, for example, to food products, or to steel and car manufacturing as recent US measures and statements seem to indicate. If that was the case, the COVID-19 crisis could accelerate economic decoupling between China and the US (and perhaps other countries too). As economic linkages between countries are removed, the cost of conflict decreases, thereby potentially furthering geopolitical tensions and even regional military conflict. According to Kaplan, we risk entering a new dark phase of globalization, which is not characterized by free trade, expanding democracy and increasing welfare. Rather, it would be about splitting the globe in great-power blocs with integrated supply chains, dominated by autocracies and class divides fostering nativism and divisions.²² In this scenario, the economic contraction due to supply shock and falling demand caused by uncertainty and unemployment would be compounded by rapidly growing de-globalization and protectionism. In combination with stimulative monetary policies enacted in many countries to counter economic recession (or just to keep the stock market afloat), a turn to trade nationalism would be likely to degenerate in stagflation – with immense social and economic costs.

Faltering trade commitments and multilateralism become very visible when comparing the world's reaction with that following the 2007–8 financial crises. In November 2008, the G20 Washington Summit on Financial Markets and the World Economy marked the start of a coordinated global effort to tackle the crisis. The summit resulted in a declaration affirming all countries' determination to further cooperation, a strong commitment to free trade and open economies, and simultaneous fiscal and monetary expansion.²³ The current lack of multilateral response at the G20 or the UN level is astounding given the unprecedented extent of this crisis, but hardly surprising given the lack of willingness from the US to exercise a leading role to which, for better or worse, the world was accustomed. In any case, the world should absolutely resist the urge of turning inwards in the long run when it comes to trade and economic integration. Isolation and self-sufficiency will not free up or create any additional resource to tackle global challenges such as global pandemics and climate change. They would rather create the perfect conditions for a long-lasting great depression.

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²² R. D. Kaplan, *Coronavirus Ushers in the Globalisation We Were Afraid of*, Bloomberg (20 Mar. 2020).

²³ G20 Summit (2008) *Declaration of the Summit on Financial Markets and the World Economy*, Washington (15 Nov. 2008).