

# G20 Hangzhou Summit 2016

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Proposals for Trade, Investment,  
and Sustainable Development Outcomes



July 2016

International Centre for Trade  
and Sustainable Development

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## Foreword

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Leaders from the Group of Twenty (G20) major economies will gather in Hangzhou, China in September 2016 to address a range of shared governance priorities. Following its initiation in 1999 as an annual forum for finance ministers and central bank governors, the G20 has evolved in the wake of the 2008 financial crisis and mounting global challenges into a premier leaders' forum convened to help advance international economic cooperation.

Successive G20 leaders' communiqués have recognised the importance of trade and investment in driving economic growth, job creation, and sustainable development. In a bid to hold back protectionist tendencies in the face of strong trade contraction followed by sluggish growth, the group has repeated commitments to keeping markets open, and to refrain from raising new barriers to investment or trade in goods and services as well as using World Trade Organization (WTO) inconsistent measures. The G20 has also affirmed the need to work to ensure that trade agreements whether bilateral, regional, and plurilateral contribute to a stronger multilateral trading system.

The Hangzhou Summit will be informed by outcomes from a fourth G20 Trade Ministers meeting held in July and an institutional G20 Trade and Investment Working Group (TIWG) convened for the first time in 2016 under the Chinese presidency of the forum. Terms of reference for the TIWG's work moving forward have now been endorsed by trade ministers. The G20 Summit is well-placed to provide policy guidance and exercise a leadership role amid an evolving global trade and investment architecture. Bringing together developed and emerging economies alike with diverse regional representation, the G20 accounts for 85 percent of global GDP and 80 percent of world trade, as well as half of inward foreign direct investment (FDI) and two-thirds of outward FDI.

Nonetheless, leaders and trade ministers of the G20 meet in 2016 against a complex backdrop. The WTO's Tenth Ministerial Conference held in December 2015 in Nairobi, Kenya concluded with a set of outcomes to be implemented, as well as agreement to disagree on how—or indeed whether—to pursue negotiations under the Doha Round framework. Yet even as the multilateral trade body and its members search for direction, game-changing technologies, new modes of doing business, and fluctuations in the global economy are shaking-up the landscape of production and consumption. New commitments to the ideals of sustainability through an ambitious set of 17 Sustainable Development Goals (SDGs) and the universal Paris Agreement on Climate Change will also require an alignment of trade and investment flows in order to be achieved.

This year's Chinese presidency has identified trade and investment as a key priority for the 2016 summit, interconnected to and supportive of three other focus areas including growth, economic and financial governance, and inclusive and interconnected development. The International Centre for Trade and Sustainable Development (ICTSD) has provided inputs into the G20's consultative process around trade and investment in order to generate ideas for its work in the mid and long term. High-level workshops were organised in partnership with the T20 in Nanjing, China in April and Geneva, Switzerland in June that catalysed informative dialogues between independent experts, officials from G20 countries, and other interested WTO members. I also had the honour to share reflections developed through these activities with the second TIWG meeting held in April.

Some recommendations highlighted on these occasions include consideration of a more proactive leadership role for the G20 within the global trade and investment architecture and efforts to further

analysis on trade and investment coherence. Several options generated through ICTSD interventions are present in the July 2016 G20 Trade Ministers Meeting Statement, including the adoption of guidelines for investment.

The articles collected in this volume serve as a contribution to this consultative process and encourage further reflection on next steps to build on what G20 trade ministers have already accomplished. The volume brings together a series of short papers by leading experts and practitioners that evaluate future contributions the G20 could make to global governance in trade and investment. The pieces variously focus on how the G20 might continue to work towards strengthening and ensuring coherence between the WTO and the wider international trading system, boost global growth, refine investment rules, respond to different views on the speed and nature of economic integration, and foster inclusive global value chains that offer viable development paths, all underpinned by a commitment to sustainable development as a guiding compass for global economic governance and the trading system.

It is our hope that the volume will not only constitute a timely and critical input into this year's G20 process, but may also serve to emphasise and stimulate reflection on the value of the group pursuing trade and investment issues under the TIWG, as well as the German presidency in 2017, and beyond.

A handwritten signature in black ink, appearing to read 'R-M-O', with a horizontal line underneath.

**Ricardo Meléndez-Ortiz**

Chief Executive, International Centre for Trade  
and Sustainable Development (ICTSD)

## List of Abbreviations

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ACWL	Advisory Centre on World Trade Organization Law
AfT	Aid for Trade
AIIB	Asian Infrastructure Investment Bank
APEC	Asia-Pacific Economic Cooperation
B20	Business 20
BRICS	Brazil, Russia, India, China, South Africa
CMA	critical mass agreement
DDA	Doha Development Agenda
DFQF	duty-free quota-free
DSU	Dispute Settlement Understanding
EGA	Environmental Goods Agreement
EIS	Environmental Impact Statement
EU	European Union
FDI	foreign direct investment
FTA	free trade agreement
FTAAP	Free Trade Area of the Asia-Pacific
G7	Group of Seven
G20	Group of Twenty
GATT	General Agreement on Tariffs and Trade
GDP	gross domestic product
GHG	greenhouse gas
GTA	Global Trade Alert
GVC	global value chain
IIA	international investment agreement
IMF	International Monetary Fund
INDC	intended nationally determined contribution
ITA	Information Technology Agreement
LDC	least developed country
MC9	Ninth Ministerial Conference
MC10	Tenth Ministerial Conference
MDG	Millennium Development Goal
MFN	most favoured nation
MIA	multilateral investment agreement
NAMA	non-agricultural market access
OBOR	One Belt, One Road
ODI	outward direct investment
OECD	Organisation for Economic Co-operation and Development
RCEP	Regional Comprehensive Economic Partnership
RTA	regional trade agreement
SCM	subsidies and countervailing measures
SCO	Shanghai Cooperation Organisation
SDG	Sustainable Development Goal
SIA	sustainability impact analysis

SME	small and medium-sized enterprise
TBT	technical barriers to trade
TiSA	Trade in Services Agreement
TPP	Trans-Pacific Partnership
TTIP	Transatlantic Trade and Investment Partnership
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
WTO	World Trade Organization



# China's G20 Presidency: Proposals for the Global Trade and Investment Regime in the 21<sup>st</sup> Century

**Ricardo Meléndez-Ortiz**  
Chief Executive, ICTSD



"What's past is prologue," so goes the saying in Shakespeare's *The Tempest*. After eight years' development, the summit of the Group of Twenty (G20) major economies has gradually become the premium forum for global economic cooperation, now viewed as a critical fixture on the international agenda. Presently, the G20's achievements, criticisms it faces, and recent global market rout serve as an important backdrop for this year's Hangzhou Summit.

China has highlighted "robust trade and investment" as a key theme in a document announcing the priorities for this year's G20 summit, interacting with and complementary to three other focus areas, including "breaking a new path for growth," "more effective and efficient global economic and financial governance," and "inclusive and interconnected development."

This article provides selected ICTSD and E15Initiative policy recommendations to the G20 Hangzhou Summit and beyond, member governments, and relevant stakeholders with respect to the Chinese Presidency's trade and investment theme.

## Enable the WTO to Better Serve and Lead the Global Trade and Investment Regime

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The World Trade Organization (WTO) concluded its Tenth Ministerial Conference (MC10) in Nairobi, Kenya, last December with a pivotal outcome: an agreement to disagree on how, or indeed whether, to continue its Doha Round of multilateral trade negotiations. In practical terms, this has left the international community without a multilateral trade agenda, and raises both challenges and opportunities for the 2016 G20 summit.

Many of the challenges and divisions between members spotlighted in Nairobi are not new, however, but instead stretch back over a decade that has seen the WTO outcompeted in relevance by other fora. On the one hand, major liberalisation has occurred in world trade since 2001, with the World Bank estimating a 30 percent average reduction of tariffs affecting all regions and larger cuts in several major emerging economies. Such liberalisation has two main sources, unilateral policies seeking competitive advantages in a world economy in which imports matter as much as exports, as well as bilateral and regional agreements of deeper integration. On the other hand, the WTO has been faced with tectonic changes in world markets, the rapidly-expanding use of digital technologies, and more efficient transportation. Some of these shifts have been of a major scale, responding to China's rapid insertion into the international rules-based liberal economic order. And some have led to the emergence of international production networks—so called global value chains (GVCs)—with the ensuing significant evolutions of trade and investment relations, and a corresponding need for regulatory cooperation frameworks.

Against this backdrop—characterised by extraordinary changes in the real and political economy of trade and investment and competition from non-WTO fora, including emerging mega-regionals setting new benchmarks for standards and policy coverage—the WTO negotiation function stalled, resulted in the Nairobi outcomes, and is in evident need of reorientation.

If properly deliberated, this challenging environment could provide opportunities for G20 leaders and the trade policy community to rethink and re-craft the future of the multilateral trade system. The G20 should continue to support the WTO, including through helping the institution regain its

centrality by repositioning itself in the broader and complex global trade and investment system of the 21<sup>st</sup> century.

The wider system encompasses both intergovernmental institutional arrangements in the trade and investment areas as well as various voluntary arrangements and rules initiated by private and non-governmental institutions. Broadly speaking, intergovernmental trade and investment arrangements include the multilateral trade system that has the WTO as its backbone, binding regional, plurilateral, and bilateral trade and investment agreements, and other non-binding trade and investment efforts—such as the One Belt, One Road (OBOR) initiative to boost connectivity and economic development in Eurasia—as well as interventions into the trade and investment space from other economic, development, or environment-focused institutions. Non-governmental, voluntary arrangements include a range of social and environmental principles, standards or codes of conduct, such as the Equator Principles for determining and managing social and environmental risks in project financing, or the Group of Seven (G7) decision on responsible supply chains to ensure effective custody of labour and environmental practices of the highest standard.

The G20 can help to shed some light on this shifting and complex trade and investment landscape. Building on decisions in the last two WTO ministerial conferences to ensure the complementarity of regional trade agreements (RTAs) with the multilateral system—rather than regarding these new variables as an intrinsic threat or rival—it can seek to take the next step to position the WTO as a foundation for the wider ecosystem with the capacity to evolve into a leadership role over the regime complex.

With this in mind, priority should be given to strengthening the legitimacy of the WTO by enhancing its inclusiveness, synergy, and effectiveness. Given the current complex political economy that is driving trade talks, WTO members may in the short term explore opportunities to develop various “trade clubs” within its folds to the greatest extent possible; in the mid and longer term they should work towards multilateralising elements of regional and plurilateral arrangements into the non-discriminatory multilateral system. Members of the WTO have an opportunity to align the institution with the 2030 Agenda for Sustainable Development and its accompanying Sustainable Development Goals (SDGs) to help bolster synergies between the multilateral trade system and other governance objectives. Considering the 2030 Agenda’s integrated policy approach, the WTO offers ready platforms to investigate and deliberate on mitigation of the intricate effects that might stem from trade initiatives implemented without appropriate flanking policies. G20 members may also seek ways for the WTO to contribute to the implementation of the new Paris Agreement on climate change. To bolster its effectiveness, the WTO should seek innovative intergovernmental negotiating approaches on the one hand, and, on the other, add new tools to its legal instruments that go beyond negotiated rule-making per se and instead focus on better regulatory cooperation.

To achieve these aims, the following concrete options may be pursued.

First, G20 members can agree to enhance the monitoring and facilitation functions of the WTO, in particular in the areas of data collection and analysis, transparency, and dialogue. For example:

- Enhance the function of the WTO committees by developing these into active platforms for deep analysis and more effective informal dialogue;

- Participate in or lead informal initiatives, such as a proposed public–private Global Value Chain Partnership (see suggestions below) and the OBOR initiative, which can play a similar role in promoting robust trade and investment as formal trade agreements;
- Participate or lead initiatives for regulatory coherence, such as a proposed global investment policy cooperation compact and the RTA Exchange (see suggestions below).

Secondly, G20 members could act at the WTO to pursue more innovative approaches in negotiations and rule-making processes, by promoting certain model elements for regional or plurilateral agreements with a view to integrating these into the multilateral trade system in 10 to 20 years. For example:

- Encourage members to negotiate and agree on principles for plurilateral negotiations that provide assurances to third parties about their openness;
- Support an independent body, such as an "RTA Exchange," to set out criteria for assessments of economic impact of RTAs and undertake the analysis.

Thirdly, the G20 could encourage the formation of a working group to address fossil fuel subsidies concretely at the WTO, through an expansion of existing WTO disciplines that are uniquely placed for international rules-based cooperation on subsidies. The G20 has committed to phasing out fossil fuel subsidies. Under the existing WTO Agreement on Subsidies and Countervailing Measures (SCM), fossil fuel subsidies cannot be challenged based on the environmental externalities generated, in other words greenhouse gas (GHG) emissions. The G20 could consider:

- Including better notification and peer review of such subsidies;
- Working towards an immediate stand-alone phase-out of production subsidies, leading to an eventual ban on all fossil fuel subsidies, while taking the impact of consumption subsidies on the poor into account in the reform process;
- Expanding the category of subsidies that could be subject to an absolute prohibition or a presumption of a prohibition, such as found in the now defunct SCM Article 6.1.

## Boost Global Trade Growth

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International trade and investment contribute to productivity increases in the world economy by facilitating the optimal allocation and use of capital, labour, as well as technology. However, due to both cyclical and structural reasons, global trade growth now sits both below pre-crisis levels and annual Gross Domestic Product (GDP) growth. Sluggish trade expansion has negative impacts on the outlook for economic development and jobs. Building upon the basis of previous summits, the G20 process can move forward two particular initiatives, in order to re-harness trade and investment for global growth.

First, G20 members could support negotiating a plurilateral Digital Trade Agreement, with a view to capitalising on opportunities offered by the rapid expansion of the Internet and other information communication technologies, maximising the contributions of Internet-based trade to economic development and employment, as well as boosting the integration of small- and medium-sized

enterprises (SMEs) into global markets. Many developing countries, including least developed countries and island states, have voiced their support for this type of initiative in post-Nairobi debates. Key aspects might include:

- A focus on the core concepts governing cross-border data flows given that data regulation can be a disguised restriction on trade. Inspiration can be taken from rules and principles emerging in some regional and bilateral trade agreements;
- Negotiating the deal in an “open plurilateral mode,” whereby talks take place in the WTO with an open invitation for non-G20 members to sign up, would allow the benefits to be extended on a most favoured nation (MFN) basis once a predefined “critical mass” participation threshold is surpassed;
- Activating and expanding the function of the existing WTO E-commerce Working Group so as to provide more analytical and administrative support for a feasibility study and possible negotiations in future.

Second, the G20 can promote and develop a comprehensive framework for services trade facilitation so as to thoroughly explore the potential contributions of services to trade growth and creation of quality jobs. Services can enable developing countries to leapfrog the traditional manufacturing route. However, services exports continue to make up less than 25 percent of total world exports, despite strong annual trade growth now outstripping that of goods. The discrepancy between the size of such exports and services importance to economic growth points to a major untapped potential in services trade. The following proposals are suggested:

- Deepen regional regulatory cooperation in financial services, including through the creation of regional credit bureaus and rating agencies, facilitation of free data flows and offshoring, and standardisation of documents and documentation requirements;
- Simplify visa and work permits for service providers and set up “innovation zones” that allow researchers and other professionals to enter freely for up to ten years.

## Promote Inclusive, Interconnected, and Sustainable Global Value Chains

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With intermediate goods making up roughly 60 percent of world total imports, GVCs have emerged as significant international networks of production, information, innovation, and services. As previous G20 summits have correctly pointed out, the better integration of SMEs into GVCs—both regional and international—will bolster local development, global trade, and economic growth. Participating in GVCs relies not only on economic “hardware”—such as transportation, communication facilities, and so on—but also on “software”—including institutional management, quality and safety standards, and custom procedures. As GVCs continue to expand, the inclusiveness, sustainability, and rules governing these are important questions for the G20 agenda. This year’s G20 can propose relevant actions as follows.

First, set up a “Global Value Chain Partnership” as a public–private platform to enable the efficient functioning of supply chains and sustainable participation. The partnership could perform the following functions, including:

- Serve as a strategic and pragmatic platform for governments who intend to further integrate their economies into GVCs to meet and cooperate with foreign enterprises looking for new partners;
- Act as a value-oriented platform for improving the inclusiveness and sustainability of GVCs by involving professionals, civil society groups, and other relevant stakeholders in dialogue;
- Provide research and information facilities, for example, by mapping sectoral GVCs, identifying particular national barriers with regards to linking to GVCs, and providing advice for governments and international agencies.

Second, provide clarity on and bolster the rules-based system in which GVCs must operate in order to simplify business operations, create new opportunities, and enable better participation. This can include the following actions:

- Simplify over 400 RTAs and work towards convergence on salient elements. The G20 could support an independent "RTA Exchange" as a public information platform to enhance the transparency of RTAs, better understand similarities and differences between these, support mutual learning, encourage the use of best practices, and identify rules that could eventually be multilateralised to bolster the international trading system;
- Simplify over 3,200 international investment agreements (IIAs). The G20 could use the Investment Policy Framework for Sustainable Development, recently issued by the United Nations Conference on Trade and Development (UNCTAD) as a basis to develop and promote a new international model agreement—this template would be formulated as a best practice available for voluntary adoption, with the idea to spur modernisation and harmonisation of bilateral investment rules from the bottom up;
- Launch a work programme aimed at fusing the disparate elements of various international trade and investment rules into a more coherent and integrated system; existing policy silos dealing with goods and services, trade and investment, competition policy, intellectual property rights, and multiple aspects of regulation should be brought together and rendered mutually consistent and supportive;
- In order to facilitate the integration of the least developed countries (LDCs) into GVCs, all developed countries should offer duty-free quota-free (DFQF) treatment to all exports from this group; developing countries should follow the example of China, India, and Brazil by offering DFQF treatment for 97 percent of tariff lines in the next five to ten years;
- G20 countries should also follow Canada's example by offering all LDCs an extended cumulation approach to rules of origin requirements for trade preferences; this would significantly stimulate exports from LDCs, judging from the evidence of similar rule of origin changes in the past, and make global supply chains work better for development purposes;
- With respect to capacity building, the G20 can both support supply-side capability in developing countries—for instance to help producers and service providers meet international and voluntary standards—and help to reduce trade costs by investing in economic and legal infrastructure and in public services.

## Enhance Global Investment Policy Cooperation and Coordination

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Like international trade, cross-border investment is an important engine for economic growth and development. While multinational enterprises have accumulated between US\$1.5–5 trillion in cash, this investment potential has not been unlocked due to recent instability in financial markets, tumbling commodity prices, slow growth in emerging economies complemented by continued stagnation in major markets such as the EU, investment policy uncertainties, and trade protectionism, among other issues. This is not good news for developing countries, in particular low income economies, as they face a US\$2.5 trillion annual investment gap in key SDG sectors.

Against this backdrop the G20 has rightly paid increasing attention to investment issues. Trade ministers this year have endorsed Guiding Principles for Global Investment Policymaking, among other things. Further work could build on these achievements in order to boost investment for sustainable development and improve confidence in the IIA universe.

First, the G20 members could propose a more comprehensive global investment policy cooperation compact. This would:

- Encourage G20 members and the international community to base investment deals on an agreed model investment agreement, which would enable IIAs to better serve the sustainable development goals and elaborate fundamental investors' rights and obligations;
- Enhance capacity building in the area of investment policy, for example by expanding and upgrading the existing Aid for Trade (Aft) programme into an "Aid for Trade and Investment" initiative, which could be focused on improving much-needed capital flows to infrastructure, climate mitigation and adaptation, and upskilling the labour force;
- Launch a feasibility study for negotiating a plurilateral investment promotion agreement among some G20 members, in one or several strategic sectors, for example environmental services, energy, transportation, or professional services, among others.

Second, improve international investment dispute prevention and settlement to rebuild trust in the system and strengthen its legitimacy. The following actions could be taken:

- Encourage G20 members to set up investor–state conflict management schemes to prevent, manage, and solve disputes, for example, setting up national investment ombudspersons and interministerial committees. The World Bank has started to help some countries set up such schemes that can be used as a reference for G20 members;
- Start a feasibility study for the establishment of an international appeal system or a world investment court; if there are disputes over the arbitration, they could resort to the ad hoc appeal scheme, composed of judicial experts accredited by the international framework;
- Set up an Advisory Centre for International Investment Law, using the Advisory Centre on WTO Law (ACWL) as a reference, to provide legal services for developing country governments that lack legal capabilities, such as helping to negotiate big investment contracts, defend in legal disputes, among other things.

## Conclusion

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The G20 is shifting its approach from issue-centred to outcome-oriented as reflected in China's announcement of the Hangzhou Summit's themes and key focus points. Particularly in the area of promoting robust international trade and investment, the G20 could make several breakthroughs, in addition to maintaining an important cooperation mechanism through the Trade and Investment Working Group.

Supporting the multilateral trade system should remain a priority for the G20 agenda. However, due to a widening trade governance gap, the G20 should no longer support the global trade body as an isolated institution. The G20 could instead develop the WTO's leadership role in the newly-emerging broader ecosystem of the global trade and investment regime, fusing it more coherently to the broad collection of binding and non-binding intergovernmental trade and investment arrangements, as well as a burgeoning array of voluntary standards and rules developed by the private sector and non-governmental agencies.

With the purpose of restoring the inclusiveness and effectiveness of the multilateral trade system as well as its legitimacy, G20 members could take active measures to enhance the WTO's monitoring, facilitation, and cooperation functions, in particular activating the regular work of committees, as well as leading or participating in informal, interdisciplinary initiatives. G20 members could also encourage new innovative approaches in formal rule-making negotiations, and provide alternative avenues for promoting regulatory coherence. Harnessing WTO rules to better address subsidies that have the potential to harm global welfare, such as fossil fuel subsidies, would be a useful contribution to global efforts to tackle climate change.

With respect to boosting global trade growth, the G20 members should explore practical ways to utilise the potential of the digital economy for global trade growth and jobs, including through the launch of a feasibility study towards Digital Trade Agreement negotiations. G20 members could also develop a comprehensive framework for services trade facilitation to maximise the contribution of growing service sectors to global trade growth.

GVCs have been among the key issues at G20 gatherings since 2012. The G20 could initiate a road map towards a clearer rules-based trade and investment system for those operating across GVCs to achieve greater inclusiveness, interconnectivity, and sustainability. Efforts envisaged as part of the road map would provide transparency on, as well as encourage convergence and harmonisation of, disparate trade and investment rules found across the wider ecosystem in key areas.

There is a pressing need to enhance investment policy cooperation. Future G20 work could consider further building on the new G20 Principles for Global Investment Policymaking, which can be non-binding, include the use of the updated IIA template, enhance the "Aid for Trade and Investment" initiative, and initiate a feasibility study of a G20 plurilateral investment promotion agreement. The G20 can also suggest better ways to manage and settle international investment disputes.



# The G20 and Global Trade and Investment Governance

**Sun Zhenyu**

Former Vice Minister of the Chinese Ministry of Foreign Trade and Economic Cooperation; Former Chinese Ambassador to the World Trade Organization



## The Role of the G20 in Global Economic Governance

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Established in the aftermath of the 2008 global financial crisis, the G20 Leaders' Summit has played an important role in global economic governance. Its development can be divided into two phases.

The first phase includes the first three summits: the Washington Summit (November 2008), the London Summit (April 2009) and the Pittsburgh Summit (September 2009). Significant achievements were realised in this period, with G20 leaders devoting themselves to combating the global financial crisis. Priority was given to joint efforts to stimulate growth, enhance financial regulation, increase bailout money and fight trade protectionism. At the London Summit, G20 leaders agreed to double the funds available to the IMF to US\$750 billion. At the Pittsburgh Summit, G20 leaders developed a "Framework for Strong, Sustainable and Balanced Growth" and set up clear targets for structural reform in the international financial institutions—namely, a gradual shift of quota share and voting power towards developing countries in the IMF and the World Bank.

These initial summits have served to enhance the coordination of international macroeconomic policy and fiscal and monetary policies. By including more countries in this coordination, the G20 played a crucial role in restoring stability and stimulating the world economy.

The second phase spans from the Toronto Summit (2010) to the present. During this period, G20 leaders extended the scope of issues on the agenda to include finance, trade, structural reform, corruption, development, energy security, green growth and many other topics. The summits proceeded in a comparatively smooth manner. Yet, as G20 member states started to implement individual economic reforms and restructuring, differences emerged and breakthroughs on major issues became more difficult.

Some progress has been achieved however. At the 2010 Toronto Summit, developed members of the G20 pledged to cut fiscal deficits in half by 2013 in response to the European debt crisis. In the same year, at the Seoul Summit held in November, development was named for the first time as a major topic of a G20 summit. A multiyear action plan was produced covering nine sectors, including infrastructure and human resource development. At the Brisbane Summit (2014), G20 leaders pledged to add an extra 2 percentage points to global GDP growth by 2018.

Each of these summits has seen heads of states call for the completion of the Doha Round, which would promote trade liberalisation and boost global growth and employment. In particular, at the 2013 Saint Petersburg Summit and the 2015 Antalya Summit, the G20 leaders provided guidance on facilitating the conclusion of "early harvest" agreements at the ninth and tenth WTO ministerial conferences in Bali (2013) and Nairobi (2015).

## Challenges and Opportunities for the G20

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Since international organisations have served as places to balance national interests among members ever since World War II, much boils down to how responsibilities and rights are distributed in terms of global public goods. As member states are at various stages of development, their challenges vary greatly and hence carry different appeal in international organisations.

The G20 summit is unique in that it has no conventions, no charter, no permanent secretariat and no international legal status. It is a summit meeting attended by heads of states where the host country holds the greatest sway over the agenda and its setting. A major challenge now facing the G20 is that not all resolutions passed at previous summits are fully implemented. This is partly due to under-representation: only a tenth of countries worldwide are included in G20 decision-making, thereby denting the organisation's authority. The authority of the G20 is also weakened since some major members have failed to fulfil some of their commitments—e.g. the delay in implementing IMF reforms due to resistance from the US Congress.

In spite of all of these limitations, the founding of the G20 itself and establishment of the summit signify an end to the era when developed countries dominated global economic governance. By raising their voices and building on their influence, emerging economies, the BRICS in particular, may be able to help steer the world economy towards a more just and balanced future.

## How can the 2016 Hangzhou Summit Contribute?

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The 2016 G20 Summit is set to be held in Hangzhou, China in September. It is the first time that China will host the summit, an occasion that will provide a great opportunity for China to "offer more Chinese solutions, contribute Chinese wisdom and provide the international community with more public goods," as stated by President Xi Jinping in a joint written interview in 2014. At the Hangzhou Summit, state leaders will continue to coordinate financial and macroeconomic policies so as to build on common ground in financial regulation. Meanwhile, the summit will shed light on how the G20 can be further institutionalised and how its execution of the agreements reached can be better enforced. In the field of trade and economic cooperation, priority should be given to the three areas identified below.

### **Efforts should be made to conclude the Doha Round before starting to negotiate "new issues."**

As the largest trading nation worldwide, China will engage G20 leaders to work on important issues such as the Doha Round negotiations so as to send out a clear political message. The ministerial conference in Nairobi in December 2015 succeeded in dealing with agricultural export competition, agricultural stockpiling in developing countries and matters related to least developed countries. But many outstanding issues are yet to be resolved. The majority of WTO members are against the idea of abandoning the Doha Round to deal with "new issues." The credibility of the WTO as an international organisation is at stake if the Doha mandate to give priority to addressing developing country concerns is compromised. Therefore, G20 leaders should give clear signals that the promise made to developing countries at Doha in 2001 on behalf of ministers should be kept.

The G20 leaders should encourage WTO members to refocus on the multilateral process and work out a programme for the next stage. As a first step, members could identify the "low hanging fruit" such as environmental goods and the Dispute Settlement Understanding (DSU), as well as other issues of importance such as non-agricultural market access (NAMA) and services. The NAMA and services negotiations should take into account the progress made in plurilateral negotiations on the Environmental Goods Agreement and Trade in Services Agreement. The negotiations covering agricultural domestic support and market access are more sensitive and complex, and will have to be dealt with in a balanced manner with special and differential treatment and special safeguard mechanisms for developing countries.

As for the new issues such as investment, e-commerce and SMEs, the G20 leaders may prefer to put forward proposals for WTO members to initiate some kind of discussion, while the formal negotiations might best be commenced immediately after the conclusion of the Doha Round.

**Under the grand vision of “One Belt, One Road,” efforts should be made to facilitate investment as well as cooperation in infrastructure and the real economy.**

Investment was first included in the G20 agenda at the 2014 Brisbane Summit. Boosting growth through expanded investment was particularly underlined at the Antalya Summit in 2015. More investment from member states seems imperative for an extra two percentage points of global GDP growth to be aggregated by 2018. The current challenge for investment is a lack of appropriate projects. There are acute infrastructure shortages in Africa, the Middle East, South Asia, Latin America and even North America. However, infrastructure projects rarely yield quick economic returns, making them unlikely to attract investment without support from governments and international financial institutions. The G20 Hangzhou Summit should encourage international and regional financial institutions to join together with local governments and local banks to finance infrastructure projects. At the same time, governments of both developed and developing countries should provide necessary services and encourage their construction companies to explore opportunities for closer cooperation in this area.

**Collective efforts should be made to promote development.**

At the United Nations summit held in September 2015, the Sustainable Development Goals were adopted by world leaders to combat poverty, hunger, disease, illiteracy, environment deterioration and gender inequality. The potential fulfilment of this 2030 Agenda for Sustainable Development is conditional on the facilitation of stable, equitable and inclusive growth.

A major challenge for meeting the 2030 Agenda lies in the huge gap between development assistance funds available and those promised. In addition, global downward pressure and trade protectionism are both obstacles for the realisation of the SDGs.

Relative to other economic and financial issues, sustainable development is of far-reaching significance and concerns the majority of countries. The G20 should strengthen its ties with the UN to give the organisation and its relevant institutions full agency in promoting development. In addition, the G20 needs to enhance the role of international financial institutions towards the end of fuelling growth and reducing poverty. The leaders of the G20 should urge developed countries to meet their international obligation to donate 0.7 percent of GDP as aid. Also, duty-free and quota-free treatment should be granted to LDCs, and issues related to rules of origin should be properly addressed as soon as possible. Redoubled efforts are also needed in fields like infrastructure and food security so as to address the North-South imbalance.



# The G20 and the Global Trading System

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Since the first meeting of the G20 at the leaders' level in Washington in November 2008, trade has been an integral part of their agenda. This first meeting took place at the peak of the global financial and economic crisis, which led to a strong contraction of world trade. Remembering the global economic crisis after 1929 and the following wave of protectionist measures, the G20 countries made the commitment not to erect new trade and investment barriers. In addition, the verbal commitment to the conclusion of the Doha Development Agenda—the current round of multilateral negotiations under the auspices of the World Trade Organization—has been part of the standard repertoire of G20 summit declarations. Until now, reforms of the world trading system have only played a subordinate role at the G20 summits. The summit declarations contain only vaguely drafted commitments to strengthen the multilateral trading system, or commitments that bilateral, regional and plurilateral trade agreements should be complementary and in conformity with the rules of the WTO.<sup>1</sup>

We argue in this article that the G20 should assume a more proactive role with regard to the future of the WTO and the reform of the world trading system. Such a reform is needed in light of the growing fragmentation of the system. At the same time, the 2030 Agenda for Sustainable Development of the United Nations calls for sustainability to be the core principle of global cooperation, including in the context of international trade. Among other things, the 2030 Agenda calls for “a universal, rules-based, open, non-discriminatory and equitable multilateral trading system under the World Trade Organization.” Bridging the gap between the realities of the international trading system and the aspirations of the 2030 Agenda is a formidable challenge that cannot be tackled effectively either in the context of the WTO or the UN and the 2030 Agenda alone. The G20 is a suitable forum to bridge that gap.

## Challenges for the Global Trading System

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The world trading system is in a phase of deep structural change, leading to increased fragmentation. The contours of a new three-pronged world trading system, which consists of multilateral, plurilateral as well as bilateral and regional agreements, are becoming apparent. Since the last ministerial meeting of the WTO in Nairobi in December 2015, the future of the Doha Round is more uncertain than ever before. Important member states, notably the United States, declared themselves in favour of terminating the Doha Round, whereas many emerging and developing countries insist on its continuation. Dissatisfied with the slow progress of the Doha Round, the major trading powers—first of all the United States and the European Union—are increasingly focusing on negotiating bilateral or regional trade agreements. Agreements such as the Trans-Pacific Partnership, which was signed on 4 February 2016 by the United States, Japan and 10 other Pacific countries, and the Transatlantic Trade and Investment Partnership (TTIP), which is currently under negotiation between the United States and the EU, cover large shares of global trade and investment flows and aim at regulating issues that go beyond the elimination of tariffs, such as investment, standards and environment. At the same time, the main trading powers are promoting so-called plurilateral agreements that focus on specific topics (Brandt 2016). The most prominent example is the Trade in Services Agreement (TiSA), which is negotiated outside the WTO. The WTO as the central organisation for the governance of world trade is weakened by this wave of mega-regional and plurilateral trade deals.

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1 This paper is based on: Axel Berger and Clara Brandt. 2016. “The G20 and the Future of the Global Trading System.” *Briefing Paper* 10/2016. Bonn: German Development Institute/Deutsches Institut für Entwicklungspolitik (DIE).

The crucial role of multilateral trade rules is emphasised in the 2030 Agenda for Sustainable Development, which was adopted by the United Nations in 2015. The 2030 Agenda provides the opportunity to advance the position that bilateral and regional agreements have to be coherent with the goals of sustainable development and the multilateral trading system. The 2030 Agenda does not adequately discuss this issue (Berensmann, Berger, and Brandi 2015). However, the Agenda emphasises the crucial role of international trade for sustainable development, and thereby highlights the importance of the development of coherent new trade rules that contribute towards fostering sustainability.

To secure the future of the WTO as a forum for negotiations, a discussion about the reform options is necessary. Such a debate has become more pressing—above all from the perspective of developing countries, which suffer particularly from the weakening of the multilateral forum of the WTO.

## Plurilaterals and the Future of the WTO

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In the future, the WTO should continue to be used as the central negotiation forum, not least because it is more inclusive than bilateral and regional negotiations, which are currently growing in importance. The WTO will also continue to retain its central role as a successful arbitrator in trade conflicts through its effective dispute settlement system. In consequence, the G20 members would be well advised to continue championing the WTO, seeking to ensure that it remains an important pillar of global economic order. Strong political endorsement of the WTO in the Communiqué of the Hangzhou Summit by its core members would underline the importance of the WTO as a negotiation forum. Such an endorsement would be more credible if supported by initiatives supporting the reform of the WTO.

The future of the WTO as a negotiation forum requires reconsideration. A currently much-discussed and increasingly-practised approach is the negotiation of plurilateral agreements, in which a “group of the willing” proceeds in specific subject areas more quickly.

If plurilateral agreements of this nature continue to grow in importance, it should—from a development policy perspective—be ensured that they satisfy certain minimum requirements. For instance, the states that are not participating should be able to accede to the agreement at all times, and the WTO’s most favoured nation clause should apply, so that all WTO members can benefit from the plurilateral dismantling of barriers to trade. These key aspects apply, for example, to the recently adopted plurilateral Information Technology Agreement, as well as to the Environmental Goods Agreement, which is currently under negotiation among like-minded countries that seek to dismantle tariffs on environmental goods. In addition, the procedures to initiate a new plurilateral agreement within the WTO need to be simplified.

However, for those countries not involved in plurilateral negotiations, one may well wonder whether the inroads made by several others are paving the way for future trade regulations that are not in their best interests. One thing is certain: for these countries, plurilateralism under the aegis of the WTO may not be ideal, but it is nevertheless preferable to a continuously increasing number of mega-regional agreements such as the TTIP and TPP, which offer them fewer accession opportunities and trade benefits.

## The Future of (Mega-) Regional Trade Agreements

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The negotiation of mega-regional trade agreements such as TTIP and TPP represent a trend towards an increasing regionalisation of trade policy via comprehensive free trade agreements and a progressive market opening outside the confines of the WTO. The impact of mega-regional trade agreements on the global trading system and on developing countries depends on the manner in which these agreements are drafted. Above all, the following aspects should be considered (Berger and Brandi 2015): mutual recognition of standards and procedures should be non-discriminatory and be extended to include third countries; EU and US rules of origin should be simplified and harmonised and they should be generous; there should be increased transparency towards third countries and options for the asymmetric opening of mega-regionals for poorer developing countries with conditions of accession varying according to level of development. Moreover, a debate is needed about how the rules of mega-regional trade agreements can be multilateralised in the future.

## The Role of the G20

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The G20 could play an important role as a forum to discuss and initiate reforms of the world trading system along the conceptual lines described above. The G20 brings together most of the important trading nations and has an institutional structure—including a newly founded Trade and Investment Working Group—that can facilitate discussions about reform needs and options for the international trading system. In contrast to the traditional fora, such as the UN and the WTO, where a North–South mindset often prevails, discussions in the G20 are conducted on a more level playing field. The increasing significance that the G20 attaches to the implementation of the 2030 Agenda could ensure that the deliberations of the reform of the world trading system also take social and environmental challenges into account. This is all the more compelling as the G20 is being chaired by two countries—China in 2016 and Germany in 2017—that have been strong proponents not only of the multilateral trading system but also of the 2030 Agenda.

- The G20 should continue to underline the centrality of the WTO for global trade governance. Whereas previous G20 summits issued rather vague statements, the signing of the TPP and the ongoing TTIP negotiations require a stronger signal in this regard. In its “Leaders’ Declaration” at the next summit in Hangzhou, the G20 should speak out strongly in favour of strengthening the WTO’s routine functions, for example by calling upon the WTO’s member states to increase the budget for the dispute settlement mechanism and also for legal support for developing countries.
- The G20 should further speak out in favour of clarifying the principles and procedures for plurilateral negotiations in the context of the WTO and should task the Trade and Investment Working Group with engaging in discussions about concrete reform proposals.
- The G20 should also address the relationship between bilateral, regional and plurilateral trade negotiations and reflect on guiding principles to coordinate negotiations at these different levels. The G20 should propose to mandate the WTO Secretariat to track bilateral, regional and plurilateral negotiations, thereby fostering transparency.

The 2030 Agenda and the Sustainable Development Goals outlined therein—adopted by world leaders in 2015—ascibe an enabling framework to the international trading system. This raises the

question of how the global trading system should be guided by the principles of global sustainable development and what role the G20 can play in this process.

- The G20 members should signal their commitment to sustainable development as the cornerstone of global economic governance and the trading system. The G20 should emphasise—as part of the upcoming Action Plan for the 2030 Agenda—that global economic governance should be in line with and conducive to fostering the implementation of the 2030 Agenda for Sustainable Development and the 2015 Paris Agreement on climate change.
- Moreover, the G20 should propose that the multilateral trade regime should underline the significance of sustainable development as a core frame of reference for the world trading system, for example through a WTO General Council interpretive statement that calls on WTO practice—including dispute settlement panels—to interpret and promote trade rules, such that they are in line with the 2030 Agenda and the Paris Agreement. The G20 could also call for a clarification of the exemptions that are part of Article XX of GATT to permit states to implement climate change and sustainability measures with less concern that these measures might be in conflict with the multilateral trade regime. The G20 members should also call for “global sustainable development impact analyses” that are conducted by the negotiating parties whenever new bilateral and regional trade agreements are being discussed (Esty 2016).
- In addition, the G20 summit participants should agree to promote trade negotiations and trade rules that contribute towards supporting the implementation of the 2030 Agenda and the Paris Agreement in all countries—richer and poorer alike—for example by joining the Environmental Goods Agreement as well as by fostering duty-free and quota-free market access for least developed countries.

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# Running Out of Tools: The G20 and the Global Trade Plateau

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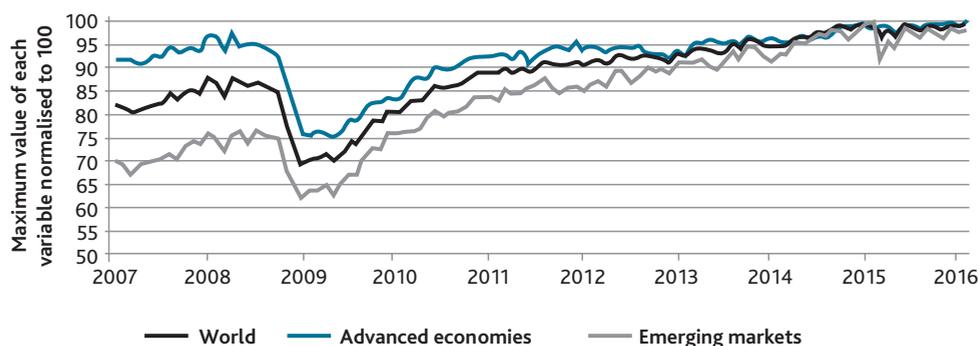


Restoring economic growth is the primary mission of the G20. International commerce—exports, imports, foreign direct investment (FDI), international licensing, technology transfer, and cross-border movement of expertise—can boost national economies, improving performance in the short and longer run. For this reason, at the beginning of the global financial crisis G20 leaders sensibly committed to keep the world economy as open as possible. One tangible manifestation of that commitment was the pledge to refrain from protectionism.<sup>1</sup>

## Global Trade Plateaus

Trade and FDI bounced back after the nadir of 2009. However, their recoveries have run out of steam (see Figure 1 for the data on world export volumes). It has been fashionable among certain international organisations and analysts to talk of a global trade slowdown. This is wrong—world export volumes have been flat for two years now. If the UN data on the total value of world trade is to be believed, global trade has not grown in five years. What we are experiencing is a plateau in global trade, which calls into question the assumption that globalisation is a process that automatically expands over time.

**Figure 1. World Export Volumes have Stagnated Since January 2015**



Source: CPB Netherlands Bureau for Economic Policy Analysis World Trade Monitor (February 2016).

The CPB's data on export volumes for 2015 paint a grim picture. Export volumes actually fell in Emerging Asia, Japan, and the US. Similarly, as far as FDI flows are concerned, the May 2016 edition of UNCTAD's *Global Investment Trend Monitor* concluded: "Barring another wave of M&A deals and corporate reconfigurations, FDI flows are expected to decline in 2016." In sum, the external factors are contributing little to growth.

## Failure to Identify Root Causes

While the "global trade slowdown" has attracted the attention of several analysts, unfortunately, they have failed to identify its root causes. Instead, only proximate causes—slowing parts and components trade, retrenchment of supply chains, and falling shipments of capital goods—have

<sup>1</sup> This paper was presented at an ICTSD workshop on "Key policy options for the G20 to support robust international trade and investment," held back to back with the G20 Trade and Investment Working Group Meeting in Nanjing, April 2016.

been identified. What decision-makers really need to know are the policy steps that have influenced these private sector decisions.

Here, the news may be mixed. For example, the March 2016 accord between G20 Finance Ministers to limit currency fluctuations is likely to have diminished one form of uncertainty that is well known to reduce trade. Looking forward, what matters is whether this accord will last. There are, however, less positive possibilities. Could the retrenchment in supply chains have anything to do with the growing resort to local sourcing rules on foreign investors and associated with government purchases or with the decision by some G20 members to revoke bilateral investment treaties? On this crucial matter, the international organisations and many analysts have not served G20 policymakers and officials well.

## Reduced Faith in Macro Stimulus Results in Diminished Policy Options

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All of this matters because policymakers are running out of tools to restore economic growth. For many, expansive fiscal policy is off the table. Aggressive monetary policies are said to be reaching the limits of their effectiveness. That leaves structural reform (which few policymakers seem keen on embracing) as well as its opposite—domestic re-regulation and protectionism—and currency manipulation. In an era of zero global trade growth, national export expansion comes at the expense of other nations, and the temptation to engage in beggar-thy-neighbour activity grows. Arguably, the world economy is at a crossroads as far as growth responses are concerned.

A depleted toolbox for policymakers coincides with a world economy where many important sectors face excess capacity. The consequences of too much supply chasing limited demand are all too clear in the steel sector—sharp trade tensions and resort to import restrictions have made headlines this year and last. But excess capacity can be found in other sensitive sectors too, such as the chemical sector and automobiles. In these circumstances, the temptation to shift the burden of adjustment on to trading partners is all the greater.

New forms of competition, often associated with the rise of the digital economy, are shaking up sectors unused to foreign rivals. The backlash that companies such as Uber and Airbnb are facing, as well as the investigations into the potential abuse of monopoly power by internet behemoths, increasingly has a nationalistic edge to it. The departure from the liberal attitudes towards cross-border commerce witnessed in the years after the fall of the Berlin Wall becomes clearer over time.

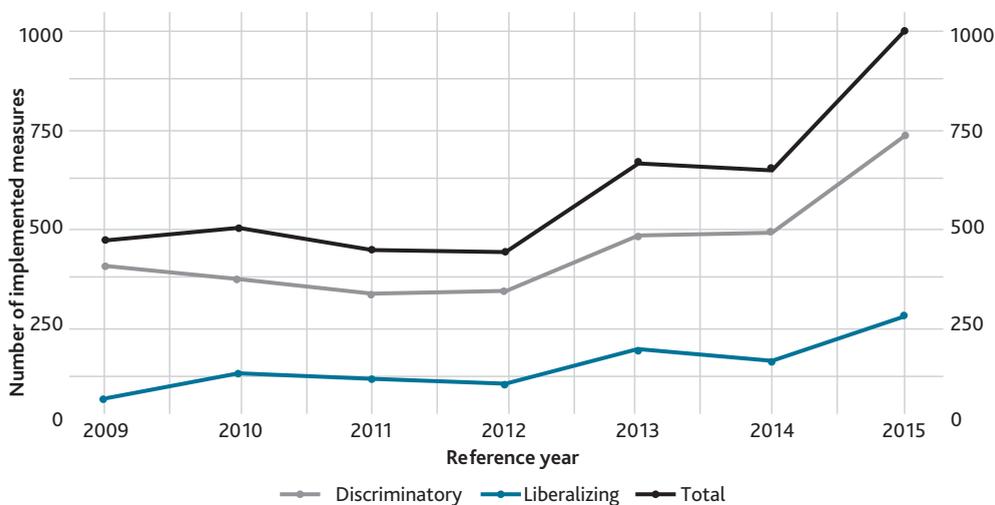
## Succumbing to the Protectionist Temptation

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In this climate it should come as no surprise that governments have been resorting to measures that tilt the commercial playing field in favour of domestic enterprises at an increasing rate. The Global Trade Alert (GTA) team, which I coordinate, keeps an eye on government steps to open and close domestic markets to international competition and tracks many more policy interventions than the international organisations do. Even more importantly, the GTA keeps looking for evidence of government action from earlier months and years and updates its statistics accordingly, so its totals tend to be much higher than those found in the reports of international organisations.

As a result of reporting lags, there is some tendency for the GTA to find that resort to protectionism tends to be higher in earlier years (such as 2009). This might give the incorrect impression that protectionism in more recent years is less of a problem. To sidestep this problem, in Figure 2 data are reported on the total number of government measures that benefit and harm foreign commercial interests implemented in a given year that were reported by 15 April of the following year.

**Figure 2. Since Global Growth Slowed in 2011–12, Protectionism has Got Much Worse**



Source: *Global Trade Alert* (May 2016).

Totals found by 15 April of the following year—which helps correct for reporting lags

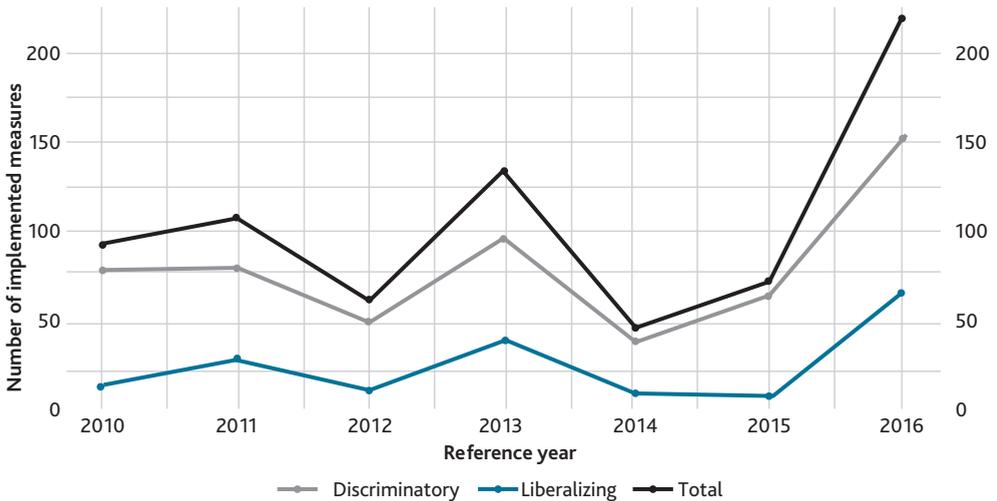
Three findings stand out. First, that in each year the number of harmful (discriminatory) measures always exceeds the number of liberalising measures implemented. Secondly, that there has been a doubling of the number of harmful measures implemented from 2012 to 2015, coinciding with the global economic growth slowdown. Thirdly, that the gap between the liberalising and harmful measure totals is widening over time. While much has been made in 2016 of a populist backlash against free trade and the potential threat of a return of protectionism—especially in certain G-20 nations—in fact, governments worldwide have been making life more difficult for foreign firms and investors for some time.

Worse, the number of beggar-thy-neighbour steps implemented by governments between 1 January and 15 April 2016 has broken the records for previous years (see Figure 3). For sure, the number of liberalising measures is up a lot too, but again the former far exceeds the latter. The governments of the G20 nations are responsible for 125 of the 149 trade distortions implemented so far this year. Of the 125 trade distortions imposed by the G20, 40 were subsidies to firms facing international rivals and 41 were tariffs imposed on dumped or subsidised imports or on import surges.

Having lost faith in macro stimulus policies, perhaps many G20 governments are already turning to policies that distort markets rather than boost growth? These data are a major source of concern

and, while it may be tempting to look for fresh topics to discuss, there is still plenty that the G20 can do with its long-standing agenda on protectionism.

**Figure 3. Initial Reporting for 2016 Suggests Even Worse News on Protectionism**



Source: *Global Trade Alert (May 2016)*.

## Use the Global Trade Plateau to Revive the G20's Interest in Trade

The redistributive nature of much trade policy, plus the natural diplomatic desire to avoid confrontation, no doubt account for the limited attention that G20 policymakers give to protectionism. Now that global trade is contributing little, if anything, to growth, governments are finding it harder to resist the temptation to steal global market share for their firms. This temptation is all the greater at a time when monetary and fiscal policy tools have lost their shine. Further action should be taken to revive the G20's collective interest in an open, transparent world trading system.

The G20 pledge on protectionism should not just be reaffirmed, but active steps must be taken to unwind the backlog of trade distortions implemented in the crisis years. Moreover, the international organisations should examine, with input from others, how existing international trade rules could be strengthened to reduce resorting to beggar-thy-neighbour activity. The impact of these trade distortions on international trading costs should be estimated. Furthermore, the merits of eliminating nuisance tariffs (tariffs of less than three percent) should be examined by experts, international organisations, and governments in advance of the 2017 G20 Leaders' Summit.





# Reflections on How the G20 Could Enhance the Multilateral Trading System

**Zhao Hong**

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## Background

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To date, WTO members have not reached a consensus on how post-Nairobi work should be carried out. Roberto Azevêdo, WTO Director-General, has called on all parties to move from reflection to action as soon as possible. Negotiating committees, on agricultural issues in particular, have recently begun to accelerate their work. There have also been expectations for disciplines to be set up on fisheries subsidies. In spite of little real progress made in the Paris OECD Ministerial Meeting on 2 June 2016, the parties showed a strong will to push negotiations forward. Thus, the best way to promote the remaining issues in the Doha Round negotiations and strengthen the multilateral trading system as a main channel for global trade liberalisation has become the focus of public attention once again.

Meanwhile, intensive negotiations on certain regional trade agreements among members continue. For instance, negotiations on the Trans-Pacific Partnership Agreement and the EU-Canada Comprehensive Economic and Trade Agreement have been completed, with review and ratification by members ongoing and expected, and negotiations on the Transatlantic Trade and Investment Partnership and the Regional Comprehensive Economic Partnership are in progress. The TTP and TTIP, as the two major mega-regionals, have attracted worldwide attention due to their high level of liberalisation and broad coverage of new issues arising in the 21<sup>st</sup> century, as well as their potential influence on global trade rules. At the same time, close attention is also given to the RCEP because of the diversity of the levels of economic development of the participating parties, and the huge size of the potential markets.

Against a backdrop of slow global economic recovery and indecision in the multilateral trading system, all sides expect the G20, a vital mechanism for global governance, to play a leading role in the international trade agenda. China, the host country for the G20 summit in 2016, is also expected to play a commensurate role in promoting a consensus among G20 members in the field of multilateral trade, rendering further assistance to the resumption of multilateral talks.

At the G7 summit in Japan on 27 May 2016, a statement was made on multilateral trade issues. It stresses the importance of the rules-based multilateral trading system; calls on WTO members to make every effort to bring the Trade Facilitation Agreement into force by the end of the year; demands early implementation of the outcome of negotiation on product expansion of the Information Technology Agreement; and aims at concluding the negotiations on the Environmental Goods Agreement before the G20 summit in Hangzhou, and accomplishing the negotiations on the Trade in Services Agreement by the end of 2016. In addition, WTO members are urged to take advantage of various fora to discuss the post-Nairobi agenda, including both outstanding and new issues, and explore new approaches to negotiation. The statement emphasises the duty of WTO members to be constructive and act with a sense of urgency to pursue and resume the negotiations in Geneva as soon as possible. In this way, the WTO can respond to the needs of the private sector, such as small and medium-sized enterprises, and the demands of digital technologies and global value chains.

Under these circumstances, all sides show considerable expectations of what can be achieved in the upcoming G20 summit in China with regard to supporting the multilateral trade agenda.

## What is Needed?

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### Enhance Understanding and Trust, Strengthen Solidarity and Cooperation

Over the past 60 years, the multilateral trading system has developed a comprehensive set of international rules. The WTO includes 162 members and covers 98 percent of global trade. It has become an institutional platform for global economic governance and the major channel for trade liberalisation. This helps to lower trade costs and provides rules and regulations for fair competition. The multilateral trading system, however, does not evolve and develop in a self-sustained manner. It consolidates and expands through the multilateral trade negotiations that are its vital function. Given the current economic recession and the unprecedented difficulties confronting the multilateral trading system, key members are obliged to work towards improving mutual understanding and trust, identify win-win situations, abandon the outdated concept of rivalry between large nations and abandon a zero-sum mentality. Common interests should be pursued positively, a common configuration should be jointly found to achieve consistency of trade liberalisation and rules, and negotiations should benefit from firm political will and follow the guiding principles of mutual ownership, mutual sharing, mutual promotion and mutual protection.

As a common feature and prerequisite, political will comes first in all successful trade negotiations. The G20 members, accounting for 85 percent of global GDP and 80 percent of global trade, clearly have a strong impact on world development and they need to stand together to overcome difficulties. To rise to its task, the G20 must act as a point of conjunction for intensifying coordination and cooperation among the core members, presenting firm political will through a consensus on the direction of negotiations, and proposing feasible ideas for the multilateral trade negotiations to reap the benefits from the trade and investment. At present, this is the most challenging task that the multilateral trading system encounters.

### Step by Step, Reinvigorate the WTO's Negotiating Function

The key to strengthening the multilateral trading system is to reinvigorate its negotiating function. This can be handled at two levels. The first is multilateral trade negotiations, the second is plurilateral trade negotiations. Geneva is currently still in a period of reflection on how to move forward. Because of the domestic political impact on trade policy in some core nations, it seems unrealistic to expect a major breakthrough in multilateral trade negotiations in 2016. But positive outcomes are always attainable if they build from the simple to complex and from penny to many.

First, the G20 should call upon its members to take the lead in the implementation of completed agreements, such as a smooth enforcement of the Information Technology Agreement expansion, and broader acceptance of the Trade Facilitation Agreement and of the Protocol Amending the Agreement on Trade-Related Aspects of Intellectual Property Rights in relation to Public Health. Implementation of the Nairobi Package is also imperative for all WTO members. As negotiating outcomes were achieved at the last moment during the ministerial conference in Nairobi in December 2015, there was a missing step before the Nairobi Package could be successfully integrated into the WTO legal complex. It is thus suggested that a proper legal instrument be developed, for example a protocol amending the Agreement on Agriculture that reflects the rights and obligations of members as agreed in Nairobi in respect to export competition. Such a protocol should then be agreed by WTO members, adopted by the General Council, and subsequently subjected to ratification by

members. Secondly, it is advisable to seek progress by promoting existing and easier issues, such as improvements in transparency and procedural rules concerning regional trade agreements. Thirdly, the G20 should encourage plurilateral negotiations on the Environmental Goods Agreement and strive to achieve results in 2016.

At the level of multilateral trade negotiations, WTO members have no objection to pursuing the negotiations on the outstanding Doha Round issues. A bone of contention among members is whether future negotiations will use as a basis existing results. All parties should be encouraged to present their views, listen to others in order to reach a reasonable conclusion, and lay the foundations for the WTO Eleventh Ministerial Conference to be held in 2017. Engagement and discussion are certainly the only means through which the negotiations can be revitalised. Therefore, communication and exchange among G20 members must necessarily be intensified and, on this basis, the G20 can help build a consensus on the future direction of multilateral trade negotiations.

China, in fact, provides a platform for this work. The role of China is to motivate the G20 members to foster mutual trust and cooperation and establish a consensus so as to strive towards resuming the multilateral trade negotiations.

### **Explore New Issues and Initiatives for Plurilateral Negotiations**

Currently, members of the G20 and WTO hold various attitudes regarding the discussion of new issues that lie outside of the Doha Development Agenda. Nevertheless, the members basically remain open to exploratory discussions. But there are different views among the parties on how to move forward and on which topics.

The WTO held a consultation with the business community on 30 May 2016. Representatives from the private sector raised both traditional issues which are the subject of multilateral negotiations and new issues such as e-commerce, services facilitation, investment, SMEs, and trade finance, hoping that WTO members will discuss and formulate rules. G20 members can pay attention to these issues and foster an initial consensus among G20 members so as to provide guidance to the multilateral trade negotiations, for instance on e-commerce and supporting SMEs. With regard to certain topics such as investment policies, where some are in favour and others object, it is suggested that discussions be started under the G20 Trade and Investment Work Group.

While multilateral trade negotiations have been stagnating, plurilateral negotiations can offer an approach to promoting the multilateral solutions. Starting with plurilateral rules and then multilateralising them could be an avenue to be pursued with a view to advancing the development of new trade rules.

Which WTO plurilateral negotiations will come next after the Environmental Goods Agreement? As the liberalisation of trade in environmental goods was proposed as a target by the Asia-Pacific Economic Cooperation, is it possible for the G20 to put forward some constructive topics for negotiation? Global value chains will possibly become a topic for plurilateral negotiations because they reflect a new framework and a developing trend for international industrial cooperation and competition in the context of globalisation. Regarding this topic, the G20, APEC, and OECD have conducted a number of studies and produced a solid economic impact analysis and a statistical basis for the measurement of data. An initiative to facilitate goods and services trade under GVCs could

be considered, and the possibility of launching negotiations on this topic could be explored. It is suggested that the T20—an informal consortium of think tanks working on G20-related issues—and the B20 start to do some research on this topic, and that the G20 trade ministers report to summit leaders, who could give new political impetus to plurilateral negotiations. Interested WTO members would then develop new plurilateral negotiations to revive the WTO negotiating function with a view towards advancing multilateral trade liberalisation.

### **Intensify the Trade and Investment Mechanism within the G20 to Benefit the Multilateral Trading System**

After the 2008 financial crisis, the main function of the G20 was to deal with the global crisis, relying on monetary and fiscal policy coordination. Working mechanisms for such coordination have been established between central bankers and finance ministers. The trade ministers of the G20 meet occasionally. But trade has not yet joined the currency and finance as a third formal mechanism for policy coordination.

The G20 has now gradually shifted its function from that of crisis response to that of a forum geared towards promoting sustainable post-crisis economic growth. Thus far, the G20 has developed the practice of convening trade minister meetings, with Australia, Mexico, Turkey, and other organisers hosting such ministerial level meetings. But this practice has yet to be institutionalised. China, as a contributor to and beneficiary of the multilateral trading system, can utilise the global economic governance platform to promote a consensus for regular meetings of G20 trade ministers, put forward trade-related recommendations or programmes, and capitalise on this formal mechanism to support the multilateral trading system.

### **Utilise Other Governance Mechanisms to Strengthen the Multilateral Trading System**

In summary, it is suggested that good use should be made of the G20 as a governance platform to give a strong and positive signal in support of the multilateral trading system while providing political guidance to WTO negotiations in Geneva. In the meantime, the G20 can strengthen its cooperation with APEC, OECD, BRICS, the Shanghai Cooperation Organisation, the Eurasian Economic Union, and other regional and international governance mechanisms to support initiatives in favour of the multilateral trading system. Furthermore, the G20 can explore the feasibility of bringing regional and bilateral trade liberalisation and domestic regulatory measures into the multilateral framework as soon as conditions permit.





# Trade Challenges for the G20

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## Unrealised Commitments

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At its next meeting in Hangzhou the G20 needs to revitalise the WTO so that it can play a central role in an open trading system that accommodates the diverse needs of its membership. In addition, it should ensure that the ultimate impact of the mega-regional agreements is to provide building blocks and create more contestable and open markets rather than present stumbling blocks and establish more exclusionist arrangements.

Thus far, the G20 actions on both fronts have been disappointing. In the official communiqué issued in Turkey in November 2015 they emphasized their commitment "to work together for a successful Nairobi Ministerial Meeting that has a balanced set of outcomes, including on the Doha Development Agenda, and provides clear guidance to post-Nairobi work." They also promised to ensure that their "bilateral, regional and plurilateral trade agreements complement one another, are transparent and inclusive, are consistent with and contribute to a stronger multilateral trade system under WTO rules."

Yet barely one month later, at the WTO Ministerial in Nairobi in December 2015, it had become clear that these commitments on the Doha Round and "post Nairobi work" could not be realised. Reflecting differences that exist not only among G20 members but the broader WTO membership, the trade ministers could not agree on how to tackle the unresolved core issues of the Doha Round that relate to agriculture (particularly domestic subsidies), market access for industrial goods, and services. In addition, while some members wanted the WTO to start discussing new issues that are not on the Doha agenda, they could not achieve the necessary consensus to do so.

## Why is This Happening?

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An understanding of how to achieve a "robust and effective" WTO must begin with an analysis of why bilateral, regional, and plurilateral agreements have proliferated at the same time as the Doha Round has been stymied. The lack of progress in the Doha Round has exposed the weaknesses in the WTO. Unlike other multilateral institutions, the consensus rule of the WTO ensures that the views of both developed and developing countries are given due weight, but it has also led to impasse when members have fundamental disagreements. This is especially the case when what is being sought is an agreement that is a single undertaking in which all members accept all obligations.

Prior to the Doha Round, it was possible to achieve consensus by exempting the least developed countries from most obligations, and by granting other developing countries generous special and differential treatment. However, the emerging economies have become too large and significant to be treated in this manner. On the one hand, for the advanced economies, concessions from large emerging economies are viewed as necessary for an agreement. On the other hand, several emerging economies avoid making concessions on their maximum allowed tariff rates by claiming treatment as developing countries.

Efforts have been made to use formula approaches to ensure meaningful liberalisation by all members. However, these efforts have been nullified when it comes to developing countries by their insistence on being allowed exclusions, such as those for special and sensitive products in agriculture. The result is that even if the modalities agreed upon in 2008 were to be implemented, the changes in most emerging market trade barriers would be minimal.

At the same time, again because of the need for consensus, the WTO has not been able to accommodate the demands of those of its members who seek deeper international integration. These demands are partly driven by the changing nature of international trade from a system in which products were entirely made in one country and exported to others, to a system in which products are “made in the world” in global value chains. This new form of trade has generated the need for new forms of governance in order to reduce transactions costs and inefficiencies and make markets more contestable. There is a new emphasis on eliminating regulations, harmonizing standards, technical requirements and product certification, and improving infrastructure and customs procedures and opening government procurement to foreign products and firms. These firms also wish to fully exploit the use of the internet for the transfer of data and provision of services without excessive restrictions on the grounds of national security and data privacy. There are also demands for deeper integration that are generated by more political concerns. Some seek the inclusion of labour and environmental standards in trade agreements.

There are conflicting responses to these demands. On the one hand, there are developing countries that are willing to sign deeper agreements in order to capture more of the value produced through GVCs. They are also interested in intellectual property protection that can enhance innovation and encourage technological diffusion. The result has been that these countries have been able to conclude deep-integration agreements such as the Trans Pacific Partnership.

On the other hand, there are other countries that are sceptical of deeper integration. Some of these countries seek to preserve their domestic policy space by promoting domestic industrial policies, maintaining state-owned enterprises, protecting domestic producers and limiting ownership by foreign investors and using government procurement to nurture domestic firms and indigenous technological development. Others also deem the demands for deeper integration on issues such as labour and environment as inappropriate for their level of development or beyond their implementation capabilities.

The WTO has thus far not been able to respond to these tensions by accommodating the diversity of its membership by adopting a more variable geometry in which all members would adhere to a core set of agreements but only some subscribe to plurilateral and sectoral agreements. Investment might be an ideal candidate for such an agreement.

## Proposals for the G20

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### Revitalizing the WTO

The G20 should now take a leadership position by proposing a new approach to WTO negotiations by learning a lesson from the UNFCCC climate negotiations, which have managed to reach beyond sharp divisions between developed and developing countries.

For years, global climate change policy was hobbled by the division between developing and developed countries. The stark demarcation made meaningful progress impossible because the growth in emissions since the Kyoto Protocol came into force in 2005 is entirely in large developing countries. In the climate arena, the big break came in Durban, South Africa in 2011, where member countries agreed to achieve an outcome with legal force that is *applicable to all Parties*.

In the Paris Agreement reached in December 2015, countries adopted a new hybrid international climate policy architecture that includes: bottom-up elements in the form of “nationally determined contributions” and top-down elements for oversight, guidance, and coordination. A similar approach with “differentiated responsibilities that reflect different capabilities” should be adopted by the WTO. New negotiations should be launched. Instead of negotiating over formulas to reduce fictitious maximum rates, some members might offer to adopt the tariffs they actually apply or make small reductions to these. There would then be a process of request and offer in markets of particular interest.

### **Measures to ensure open regionalism**

The G20 should also agree on measures on preferential trade agreements. First, the G20 should actually promote transparency with an institution that would serve as a central repository for information, analysis, and collective international knowledge on regional trade agreements (RTAs). This institution would allow a broad set of stakeholders to participate in the information exchange. G20 countries should also pledge that any new agreements and once implemented the introduction of new regulations would allow for a certain time period in which comments could be submitted through a dedicated platform.

Second, the G20 could also establish a body with a distinguished panel of trade authorities that would subject drafts of all agreements to a multilateral impact statement to encourage agreements that create internationally contestable markets. Experts should be encouraged to work out suitable methodologies and criteria and then to issue reports that could provide guidance and help encourage more open and modular agreements.

Third, RTAs should allow for mutual recognition of certification and standards in a manner akin to how the EU Common Market allows for the mutual recognition of product standards. A major goal of several free trade agreements entails establishing common standards, or equivalence of standards and/or mutual recognition. The G20 would pledge, in such cases, to extend the benefits from such standards to goods and services originating in other WTO members. For example, any such standards established in the Transatlantic Trade and Investment Partnership would be available to producers from outside the EU and the US.

Finally the achievements of mega-regional agreements could be used as a basis for zero-for-zero critical mass liberalisation agreements under the auspices of the WTO. Taken together, the G20 countries that are participating in the three large mega-regional arrangements (Trans-Pacific Partnership, Transatlantic trade and Investment Partnership, Regional Comprehensive Economic Partnership) will comprise almost 80 percent of world GDP. Once a critical mass of participation is achieved, these would be introduced into the WTO on a most favoured nation basis.



# China's G20 Agenda: Call for a Multilateral Investment Framework for Development

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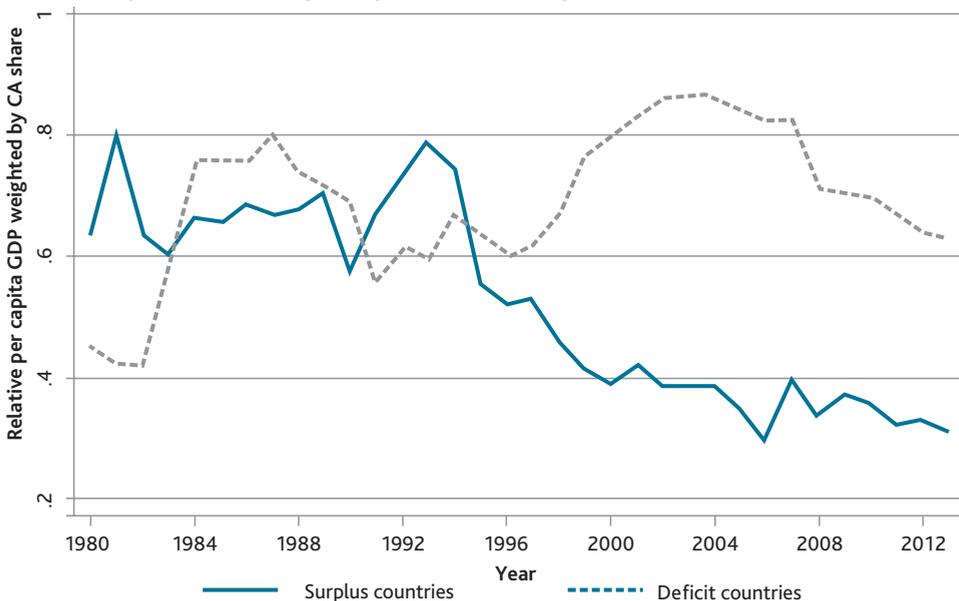
China has taken over leadership of the G20 meeting in 2016, providing a timely and opportune moment to move its development agenda forward at the global level. One important contribution that China could make would be to launch discussions on a multilateral investment agreement to be developed next year. One achievable goal could be for G20 members to agree on a working framework setting out the principles and timeline for concluding this multilateral agreement.

## Why is a Multilateral Investment Agreement Critical for Development?

If we investigate the development process, we find that constant technological improvement is a critical ingredient for continual growth and job creation. This process of improvement requires not just innovation, but sufficient injections of human and physical capital. In addition, infrastructure investment is needed in many developing countries in order to reduce transaction costs within the economy and increase efficiency. Developing countries are precisely constrained by low supplies of human and financial capital. Moreover, they are typically constrained by a lack of foreign exchange, which limits their ability to import raw materials and equipment, embedded new technology, needed in the upgrading process.

The natural solution to these development gaps—of human capital, financial capital, and foreign exchange—is to attract FDI. As returns to capital should be higher in developing countries where capital is scarce relative to labour, the flow of capital from high- to low-income countries should create gains on both sides. However, as pointed out in Alfaro et al. (2003), capital has been flowing in the “wrong” direction, from low- to high-income countries (see Figure 1, constructed using the same methodology employed in Prasad et al. (2006)), further depleting the available capital in developing countries, constraining development prospects, and contributing to the widening global income gap.

**Figure 1. Relative per capita GDP for Surplus and Deficit Countries**



Source: World Bank Development Indicators

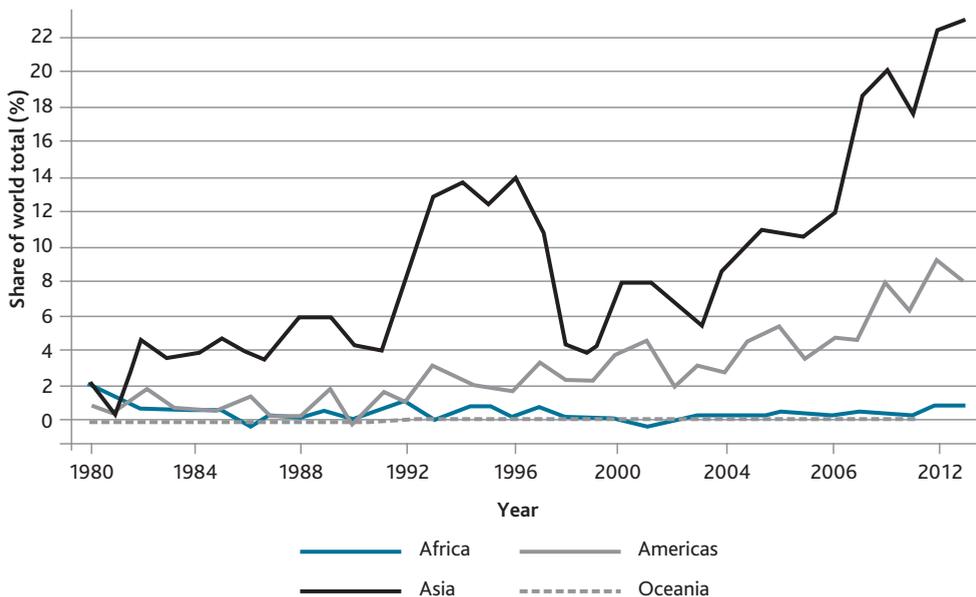
One reason for this reverse flow of capital is a lack of investment facilitation in developing countries. This investment gap underlines the global need for some kind of multilateral investment agreement, which would not only facilitate the flow of capital in the 'right' direction, but also fundamentally strengthen the foundations of growth for developing countries. Some of the issues that this agreement would deal with include: investment protection and incentives, dispute resolution, corporate social responsibility, and regulation related to investment by state-owned enterprises and sovereign entities.

## Why Now, and What is the Best Platform?

The World Trade Organization is the natural platform for negotiating this multilateral investment agreement, particularly given the strong links between trade and investment. However, past efforts to conclude such an agreement stalled and were eventually abandoned, in part due to perceptions that the agreement was weighted too heavily in favour of the interests of developed country and failed to take into account the needs of developing countries

The global investment environment has changed dramatically in the past decade, and conditions are now much more favourable for the creation of a multilateral investment agreement that will bring substantial benefits to developing countries. Notably, developing economies now account for an increasing share of outward direct investment (ODI) (see Figure 2). It is therefore the right time to restart discussions about the creation of a multilateral investment framework. Given the growing participation of emerging market economies in FDI, the G20 meeting in 2016 will be a good platform for establishing such a framework. Indeed, the G20 proved its usefulness in coordinating multilateral efforts to respond to the 2008 global financial crisis and continues to play a constructive role in global economic governance.

**Figure 2. Outward Direct Investment from Developing Economies**

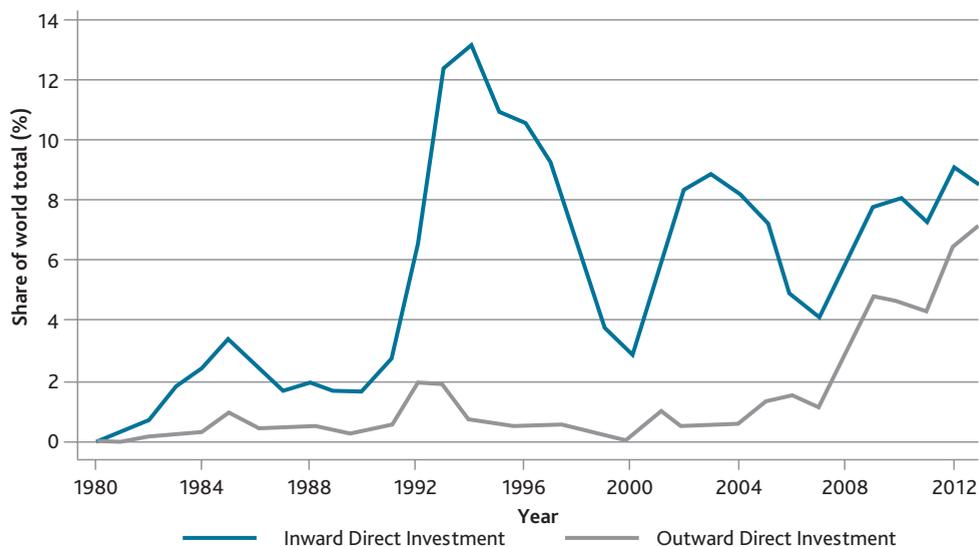


Source: UNCTADSTAT

## The Role of China

China has benefited tremendously from FDI in its own development process, and over the past decade, its own ODI has increased significantly (see Figure 3).

**Figure 3. Outward and Inward Direct Investment from China**



Source: UNCTADSTAT

According to UNCTAD, in 2013 China became the third largest source of FDI to other countries and is expected to become a net capital exporter for the first time in 2016. This trend of rising Chinese FDI is likely to strengthen in the future, when one considers the combined impact of China's Going Out and OBOR strategies. In time, China is likely to become the world's largest source of FDI. Having been a major recipient of FDI, and now a growing contributor of FDI, it is both timely and appropriate for China to lead discussions at the G20 in 2016 on how to harness investment for global development.

## An Inclusive but Non-Binding Investment Facilitation Framework

In conclusion, a concrete goal for the 2016 G20 meeting should be for members to agree on a working framework for achieving this multilateral investment agreement for development. This framework could lay out a concrete timeline for achieving specific milestones. For example, one milestone could be the achievement of a non-binding investment facilitation framework. Most importantly, the core of the agreement should include a non-binding principle while highlighting inclusiveness and emphasise an overarching commitment to fostering economic growth for developing countries.

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# **A Multilateral Investment Agreement: A Road to Nowhere?**

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## Introduction

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One of the recurrent debates on international investment rule-making, often with a reference to the G20, relates to the question of whether it is possible and desirable to establish a multilateral investment agreement (MIA).<sup>1</sup> We currently observe a renaissance of the debate about an MIA after past attempts to establish a Multilateral Agreement on Investment failed in 1998 at the OECD and in 2003 as part of the Doha Development Agenda of the World Trade Organization. The proponents point to recent fundamental changes in the international investment regime that speak in favour of a resumption of negotiations about an MIA (Åslund 2013; WEF 2013; Lin 2015; Hufbauer and Schott 2015).

First, we can now observe a fundamental shift in global investment flows. Companies from emerging countries are increasingly investing abroad and aim at better protection of their companies' foreign direct investment in developing and industrialised countries. The traditional criticism put forward by influential, emerging countries against an MIA appears to be weakening as a result of a growing convergence of interests. China's decision to discuss multilateral investment rules in a dedicated working group under its G20 presidency is a case in point.

Secondly, among industrialised countries themselves there is a growing consensus regarding international investment rules. Controversies among the members of the OECD were one of the main reasons for failure of the negotiations towards a Multilateral Agreement on Investment. One sign of a convergence of approaches are the Shared Principles for International Investment, adopted in 2012 by the European Union and the United States, whose purpose is to smooth the way for a Transatlantic Trade and Investment Partnership, and recently concluded treaties such as the Comprehensive Economic and Trade Agreement between the EU and Canada. With this gradual convergence, in particular regarding the inclusion of market access provisions, a further stumbling block along the way to an MIA appears to have been done away with.

Thirdly, the increasing regionalisation of investment rule-making is advanced as an argument which can facilitate the leap to the next-higher, multilateral level. As a result of so-called "mega-regionals"—like the Trans-Pacific Partnership between the US and 10 other countries in the Pacific region, the Regional Comprehensive Economic Partnership between the Association of Southeast Asian Nations and six other countries, including China, or the planned Transatlantic Trade and Investment Partnership—it is possible that a consolidation of investment rules will arise which would simplify the negotiations about an MIA.

Although these developments are far from linear and there are prevailing differences in the international investment policies of industrialised and emerging countries, current trends can indeed help to smooth the path to a global accord. However, the main question driving the international debate should not be whether it is possible to establish an MIA (*function follows form*). What is more important is the question of whether the institutional form of an MIA is suitable for effectively solving the most pressing challenges in the current investment regime (*form follows form*). It is not very likely that an MIA would pass the latter test, as I argue in this article, since an MIA would not lead to significantly more FDI flows or give stronger consideration to the interests of the developing

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1 This paper is an adapted and rewritten version of Berger (2013).

countries. An MIA will most likely also not lead to greater coherency between the investment rules and other policy areas.

Given the existing complex structure of the international investment regime, it is inevitable that these challenges will be tackled at various levels (national, bilateral, and regional). Negotiations at the various levels should be supplemented by coordination efforts on the global level. The G20 is the appropriate orchestrator for talks about these overarching questions, talks which in turn should be carried on with the inclusion of the OECD, WTO, and the United Nations Conference for Trade and Development (UNCTAD), and other stakeholders.

## Deficits of the Current Investment Regime

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In contrast to world trade, no comprehensive multilateral accord exists for investments. Global investment flows are protected by a fragmented system of almost 3,000 bilateral investment agreements and more than 350 free trade agreements with investment chapters (UNCTAD 2016). Most of these agreements establish far-reaching and binding standards of protection for international investors, such as national treatment, fair and equitable treatment, and liberal financial transfer clauses. Among the essential features of international investment agreements (IIAs) is that investors can assert their rights against host countries directly before transnational arbitration tribunals.

In recent years, a lively debate has developed about the economic and social effects of IIAs and about the limits imposed on host countries' policy space by IIAs, a debate in which the following critical arguments are advanced.

First, the effectiveness of IIAs as an instrument for promoting investment flows is called into question, even though some econometric studies show a generally positive influence of IIAs on FDI flows (Berger 2015b). However, IIAs which provide greater legal protection to international investors do not have a significantly greater impact on the volume of FDI flows than that of "weaker" agreements. In addition, company surveys have shown that IIAs play only a minor role in the investment decisions of many investors. Only free trade agreements with investment chapters which simultaneously liberalise market access for investors can significantly increase FDI inflows. Finally, IIAs are only one determinant among many which affect the volume of FDI inflows.

Secondly, the critics advance the argument that IIAs greatly limit host countries' policy space for regulating FDI. On the one hand, this effect is intended as a means of attracting FDI. Host countries hope to signal international investors via IIAs that their respective national investment regimes are open and reliable. On the other hand, the very rapidly rising number of investor–state dispute settlement procedures is a sign of the restrictive influence of IIAs, which in turn was never intended by the parties to such agreements. In particular, clauses specific to IIAs like the sweeping requirement of fair and equitable treatment make it possible for investors to go to court against a broad range of host country measures. It is not least due to the legal actions taken by international investors against the health- and environment-related measures of governments that the restrictive influence of IIAs is criticised.

A third point of criticism against the current investment regime and in particular the system of arbitration is the inconsistency of arbitration awards and the inconsistent interpretation of the protection standards contained in IIAs. As a reaction to these shortcomings, the countries of the

North American Free Trade Agreement have begun to formulate protection standards in their IIAs in greater detail and to increase their regulatory latitude by specifying exceptions. These reforms are being taken up by more and more countries.

Finally, IIAs are also the target of criticism due to their impact on other policy areas. Traditionally, IIAs were entered into above all as instruments for promoting FDI, and were oriented correspondingly in a one-sided fashion to the protection of investors. This one-sided orientation is no longer suitable in view of a growing interconnectedness of different policy areas. The protection standards contained in IIAs intervene deeply in the national regulatory system of any host state, affecting not only investment-specific policies but also, as already mentioned above, a multitude of other areas subject to public regulations. IIAs which are all too one-sided in their orientation towards the protection of investors can have an unduly restrictive effect on the ability of the host countries to act in other political arenas.

Against this background, the effectiveness and legitimacy of the current investment regime is being called into question. One sign of this is not only the criticism of many non-governmental organisations and such international organisations as UNCTAD, but also the recent policy responses of many countries (Berger 2015a). Latin American countries like Bolivia, Ecuador, and Venezuela have already cancelled their membership in the International Centre for the Settlement of Investment Disputes, which is affiliated with the World Bank, and South Africa and Indonesia intend to cancel their IIAs. Other countries have reformed the model treaties which they use to negotiate new treaties. These developments are signs of an erosion of the current investment regime.

## What Can a Multilateral Investment Agreement Achieve?

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In analogy to the world trading system, argue the proponents of an MIA, universal rules would be preferable in the area of investments too, due to the fragmentation of the system of more than 3,000 bilateral accords (Åslund 2013).

However, it appears doubtful whether the integration of trade and investment policies will have comparable economic effects. Irrespective of its normative permeating force, the multilateral logic does not apply automatically to the dismantling of non-tariff barriers. The WTO World Trade Report 2011 shows that "deep integration" within the framework of bilateral or regional accords – for example, regarding the dismantling of technical trade barriers or the liberalisation of services – often has no discriminating effect on third parties (WTO 2011). Non-members cannot easily be excluded from the benefits of this integration.

The same holds true for investment policies as well. For the benefits of bilateral IIAs are not necessarily concomitant with negative effects on non-members. Among the special features of IIAs are, for example, most favoured nation clauses, which explicitly extend the benefits of bilateral integration steps to non-members as well. In view of the wide-ranging overlaps and structural connections, we indeed already have a multilateral investment system, but one which is constituted above all by a fragmented and complex network of bilateral accords (Schill 2009). This cooperative fragmentation does not necessarily have to involve negative consequences for the system as a whole.

In view of the non-discriminatory nature of the current investment regime, it is to be doubted that an MIA can help meet the challenges described above.

### **Would an MIA Lead to an Increase in FDI Inflows?**

The proponents of an MIA argue correctly that the bilateralisation of rules of investment only promotes lack of transparency and higher complexity, thus leading to elevated transaction costs for international investors. Regardless of the systemic overlaps of bilateral IIAs already described, these accords differ from one another in detail and make it difficult for international investors to evaluate the existing legal framework for investment. An MIA could therefore result in more investment flows, especially since the signal effect of a multilateral accord would be greater than the multitude of individual accords. However, the positive effect of an MIA due to the dismantling of transaction costs depends on whether a multilateral accord would supplant the bilateral IIAs among the members. An MIA would otherwise merely add another level of regulation, and opacity and complexity would only be increased even further.

### **Would an MIA Bolster the Bargaining Power of Developing Countries?**

As described at the beginning, existing IIAs are for the most part one-sided in their orientation to the protection of international investors. One argument that could be advanced for an MIA is that of the dismantling of power asymmetries between industrialised and developing countries. A comparison with negotiations in the WTO or the United Nations Framework Convention on Climate Change shows that by forming coalitions developing countries are quite capable of having a decisive impact on the course of multilateral negotiations. However, should the developing countries prevail and succeed in anchoring exceptions to the regulation of FDI and the accountability of investors in an MIA, it would be equivalent to a Pyrrhic victory: capital-exporting industrialised countries (and emerging countries) could pull back from the multilateral negotiations and would again concentrate on negotiating bilateral or regional accords.

### **Could the Coherency of Rules of Investment Be Improved in the Context of MIA Negotiations?**

On the one hand, the issue here is to take into account previously neglected issues such as public policy interests, negative effects of host countries' investment incentives, or investments of state-owned companies. On the other, the aim would be to reduce the potentially negative impact of investment rules on other policy areas such as international financial and trade policies, or health and environmental policies. It appears doubtful that a stand-alone MIA, due to its focus on the liberalisation and protection of investments, would improve the coherency of the current investment regime.

Finally, one fundamental question also remains open: in what forum could an MIA be successfully negotiated? The WTO is advanced by proponents of an MIA as an appropriate platform for negotiating rules of investment. However, the WTO currently finds itself in a deep crisis which makes it impossible for it, in the short or medium term, to assume responsibility for new policy areas such as investment. In addition, other fora for negotiation such as the OECD or UNCTAD are allied too closely with the interests of industrialised or emerging countries and developing countries respectively.

## Global Coordination Needed

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The shortcomings of the current investment regime can't be cured by the negotiation of one single multilateral treaty – unless this treaty replaces the existing bilateral treaties. While the EU has used this “replacement logic” to negotiate European IIAs to supersede the bilateral investment treaties of its member states with their respective treaty partners, there are no signs that this model is being pursued by other countries. Given the existing architecture of the international investment regime, reform efforts within it will take place on the level of the individual country with regard to the reformulation of model treaties, in bilateral or regional negotiations and with regard to different sets of rules such as investor–state dispute settlement mechanisms (UNCTAD 2015).

Given the complexity of ongoing reform efforts there is a need for an accompanying process of coordination on the global level (Sauvant and Ortino 2013). This should lead to a better understanding of the reform option available between the traditional, capital-exporting, industrialised countries, the emerging countries, whose companies are increasingly investing abroad, and the developing countries, which often continue to be cut off from global investment flows. In analogy to initiatives to build trade capacity in the global trade system, similar initiatives should be intensified in the investment sphere in order to help developing countries to better navigate the increasingly complex international investment regime.

The G20 is the natural candidate to be the initiator of a concomitant process of coordination. The G20 comprises not only the industrialised countries but also the most important of the emerging countries and takes into account—even though inadequately up to now—the interests of the developing countries via the participation of regional organisations such as the African Union. Orchestrated by the G20, these discussions should be conducted with the inclusion of international organisations like the OECD, the WTO, and UNCTAD, along with representatives of business, civil society, and academia.

The discussions should include new topics that have not been dealt with in IIAs. In particular, the discussions should include the balance between liberalisation and regulation of investment policies, the financial incentives of host countries, investment facilitation, the investments of state-owned companies, the integration of voluntary sustainability standards, and the consolidation of the existing system of bilateral IIAs.

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# The 2016 G20 Trade Agenda: Focus on Global Value Chains

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## Introduction

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The single most significant unifying theme in all G20 deliberations since the Los Cabos Summit in 2012, when GVCs were first singled out for attention, is the need for GVCs to foster inclusiveness and contribute to a viable development path. All subsequent G20 summits, along with supporting prior meetings covering this topic, have called for—with more or less specificity—development-oriented policy approaches. The Turkish presidency in 2015 added considerable emphasis on supporting SME participation in GVCs.

If GVCs are to fulfil their promise as a development vehicle, they must contribute to economic diversification, jobs, and upgrading beyond simple low value-added tasks. The ways in which this may be assured involve national governments, business, and international agreements that stabilise equitable and opportunity-creating trade and investment relationships.

Outsourcing by lead firms in GVCs is an important mechanism for fostering inclusion, providing opportunities for SMEs, building up local specialisation and creating production clusters. Governments can do much to encourage lead firms to source locally by creating an enabling environment and assisting potential domestic suppliers to prepare themselves for GVC participation. Over time, outsourced suppliers can build up expertise, find ways of upgrading, and become lead firms themselves.

Increasing attention is being paid to the role of SMEs in development processes, and the need to create favourable conditions for their participation in production and trade. SMEs account for large shares of output and jobs in virtually all economies. Oftentimes, their participation in trade is more far-reaching than generally appreciated. Much of this participation is indirect, supplying inputs to firms that export.

In the early stages of involvement in GVCs, SMEs will often be service suppliers. This is partly why the services economy deserves to receive closer attention than it has in the past. One reason for SMEs' relatively heavy reliance on services is that barriers to entry are low in terms of start-up capital. High fixed costs associated with economies of scale are not as likely to play a role as in the case of goods production. A good part of the capital requirement for higher-return services operations is human capital. The degree of sophistication in the offerings of service-oriented SMEs varies from low-end unskilled work to high-end value-added.

A flourishing part of higher added value, SME activities is found in the digital economy. Opportunities are considerable for direct involvement in international trade via Internet-based platforms. Very small firms can have large, multi-customer and multi-destination clienteles, offering a range of services requiring differing skill attributes. The fuller and more effective participation of SMEs in GVCs requires a multifaceted approach. Partly it is about supporting SMEs in skill acquisition in various areas and in exploring opportunities for innovation and productivity growth. It is also about governments creating an enabling environment through developing adequate infrastructure. Possibly an even more important focus for enablement in many economies is improving the policy environment.

Cumbersome and cost-augmenting regulations, poor administration, and various obstacles to doing business fall disproportionately on SMEs. Large firms are better able to deal with, or work around,

such obstacles. Finally, with some encouragement from governments, large lead firms are likely to find it in their interests to anchor more solidly in the domestic economy and build long-term supplier relationships with SMEs.

Trade and investment decisions are crucial in shaping the location, configuration, and operation of GVCs. A range of underlying conditions—not least the policy environment—determine those trade and investment decisions. The GVC lens provides a useful context for understanding and promoting desirable economic and developmental outcomes in terms of international economic engagement. The GVC-related framework for policy analysis is necessarily joined-up and holistic. Proposed courses of action will complement, dovetail, and—in some instances—repeat various recommendations for policy action identified in the broader G20 context.

This overlap is to be expected within the G20's overarching thematic positioning, whose focus in 2016 is to promote an "innovative, invigorated, interconnected and inclusive world economy." The challenge is to ensure coherence among the various analytical entry points giving rise to recommendations for policy action. The starting points and specific conditions facing each economy differ and will determine the emphasis and sequencing decisions of individual governments.

As governments seek to benefit from participation in GVCs to the greatest extent possible, the following policy areas and actions suggest themselves for consideration. For convenience, the policy areas identified are divided between domestically-oriented policies and international policy cooperation, but in reality the two overlap in various ways.

## Establishing a Conducive Domestic Policy Environment

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- Strengthen actions to nurture a supportive environment for GVC participation, especially for SMEs: areas for action include infrastructure development (physical, virtual, and human), and coordination and support for R&D and innovation "laboratories" to enhance domestic productivity growth and competitiveness. Support should also be extended to enable SMEs to navigate and manage regulatory requirements more effectively, especially in the field of standards. All this support is fundamental to creating opportunities for upgrading on value chains;
- Review and, as necessary, reform policies affecting factor markets: this includes regimes for FDI and for foreign labour (visas, work permits, etc.). Policies should favour openness in order to benefit from foreign resources, technology, and expertise, but be tempered by appropriate actions, conditions, and constraints to foster domestic developmental objectives. High standards of analysis and implementation, based on good governance practices, are essential to ensure balance;
- Review and, as necessary, reform policies affecting production: streamlining regulation, both in terms of design and administration, is at the core of actions here, aimed at lowering trade costs and promoting competitiveness. Regulations are designed to pursue legitimate public policy objectives poorly attended to by markets or functionally necessary for government. However, they should not serve a dual protectionist purpose (especially not for private gain), nor impose unnecessary costs. Policy failure here particularly penalises SMEs;

- Establish mechanisms for analysing the role of services in GVCs, including at the production stage and in relation to upstream and downstream sources of added value. Value chains for both goods and services require analysis in order to acquire a better understanding of the multifaceted contributions of services to the economy. This is important in light of the prevailing knowledge deficit, the often predominant role of services as a source of value, jobs, and innovation, and of the scope that services offer for SME participation in GVCs.

## Areas for International Cooperation

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- Urge and support actions by governments and international organisations to improve data collection and techniques for analysis—the paucity of data prevailing today inhibits sound and well-informed policymaking;
- Build on the Antalya initiatives to support and nurture SME participation in GVCs and the international economy; support and strengthen the World SME Forum as an international focal point for actions to strengthen and empower SMEs in the marketplace;
- Support and strengthen existing work undertaken by international agencies to facilitate access to trade finance for firms, especially SMEs, in developing and emerging economies;
- Engage business, through the International Chamber of Commerce and the Business 20 (B20), in analysis and dialogue on ways of facilitating the participation of SMEs in GVCs; establish a mechanism and work programme for this purpose that will draw on business experience;
- Support the reinvigoration of the WTO as the primary forum for international trade cooperation and the integration of preferential trade agreements into the broader framework of inclusive, non-discriminatory trade cooperation;
- Promote work to build an IIA that would establish multilateral rules on investment and render coherent the current network of thousands of bilateral investment agreements;
- Launch a work programme aimed at fusing the currently disparate elements of international trade and investment rules into a more coherent and integrated system of rules; existing policy silos dealing with goods and services, trade and investment, competition policy, intellectual property rights, and multiple aspects of regulation should be brought together and rendered mutually consistent and supportive.

## Annex: Excerpts from Past G20 Declarations and Reports

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### **G20 Leaders' Communiqué (Los Cabos, Mexico 2012)**

We value the discussion held by our Trade Ministers in Puerto Vallarta on the relevance of regional and global value chains to world trade, recognizing their role in fostering economic growth, employment and development and emphasizing the need to enhance the participation of developing countries in such value chains. We encourage a deepening of these discussions in the WTO, UNCTAD and OECD within their respective mandates, and we call on them to accelerate their work on analyzing the functioning of global value chains and their relationship with trade and investment flows, development and jobs, as well as on how to measure trade flows, to better understand how our actions affect our countries and others, and to report on progress under Russia's Presidency.

### **G20 Leaders' Declaration (St. Petersburg, Russia 2013)**

We recognize the importance of better understanding the rapid expansion of global value chains (GVCs) and impacts of participation in GVCs for growth, industrial structure, development and job creation. In this regard, we welcome the work done by the OECD, the WTO and the UNCTAD and ask them to seek the views of governments and continue their research on the impact of GVCs, particularly in relation to the influence of GVCs on trade, economic growth, development, job creation and distribution of value-added along GVCs. Identifying the opportunities and challenges of participation in GVCs and making available value-added trade statistics may help countries in due course to decide upon appropriate policymaking options to benefit from GVCs. We call for the OECD in cooperation with the WTO and the UNCTAD to deliver a report in the first half of 2014.

### **G20 Leaders' Communiqué (Brisbane, Australia 2014)**

Trade and competition are powerful drivers of growth, increased living standards and job creation. In today's world we don't just trade final products. We work together to make things by importing and exporting components and services. We need policies that take full advantage of global value chains and encourage greater participation and value addition by developing countries.

### **Chairman's Summary of Meeting of G20 Trade Ministers (Sydney, Australia July 2014)**

We discussed global supply chain barriers and how domestic reform and liberalising services will generate particularly large economic gains because there is a compound effect on international competitiveness. We agreed that barriers to trade in services hamper economic growth and need to be addressed through both domestic reform and international cooperation.

### **G20 Leaders' Communiqué (Antalya, Turkey 2015)**

Inclusive Global Value Chains (GVCs) are important drivers of world trade. We support policies that allow firms of all sizes, particularly SMEs, in countries at all levels of economic development to participate in and take full advantage of GVCs and encourage greater participation and value addition by developing countries.

**Chairman's Summary Meeting of G20 Trade Ministers (Istanbul, October 2015)**

In order to achieve strong global trade growth, Global Value Chains (GVCs) should be more inclusive. Better integrating SMEs at the national and Low Income Developing Countries at the global level are key to achieve this goal. Recognizing that GVCs of the developed regions have matured, the income elasticity of trade started to diminish. Therefore, we stressed the importance of expanding them to regions and countries that have missed out these opportunities in the past. Accepting the crucial role of GVC participation for economic development and growth, we also noted the importance of identifying and implementing policies that allow firms of all sizes, especially SMEs, in countries at all levels of economic development, to take full advantage of GVCs.

We noted that costs imposed unnecessarily on firms place the heaviest burden on SMEs. We agreed that it is pivotal to provide a conducive environment for investment and trade. We also stressed the importance of infrastructural prerequisites, including policies addressing financial constraints faced by SMEs' in starting ups. We welcomed the launch of the World SME Forum in co-operation with the International Chamber of Commerce and B20 as a platform to provide advocacy to enable SMEs to better integrate GVCs and to improve their financing and investment.



# Re-Energizing Global Trade Growth: New Frontiers of Digital Trade

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Globalisation has entered a new phase, driven by the rise of digital (data and information) flows, raising new questions for the WTO, and global economic and trade governance. India and other emerging markets need to fully engage in developing universal standards conducive to innovation, productivity, and growth.<sup>1</sup>

Let's first look at the facts about recent developments in global trade, before turning to their implications for sectors and regions, and for global governance and growth:

- Since the global financial crisis, overall trade has clearly stalled—globally as well as for emerging markets. Before that, the long term average growth of global trade was about five percent a year, considerably higher than global growth.
- The slowdown in trade has taken place despite favourable factors, such as declining transport costs, and may reflect lingering cyclical conditions.
- While there have also been one-off disruptions to the trade slowdown, structural factors are clearly at play, such as falling trade elasticities to growth (Constantinescu et al. 2015). The structural factors clearly include China's falling demand for raw materials and capital goods, and stalled efforts at global trade liberalisation.
- While global goods trade as well as cross-border financial flows have fallen sharply since 2007, flows of digital information have surged.<sup>2</sup> Growing international evidence, recently from the McKinsey Global Institute (MGI), suggests that cross-border bandwidth use has grown 45-fold over the past decade, with about 12 percent of global goods trade already conducted in e-commerce channels (Manyika et al. 2016). These rising cross border flows of digital globalization are already circulating intellectual content and innovation around the world, with rising implications for productivity and growth.

## Implications of Digital Globalisation

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Let's consider now the implications of the rise in the new information-intensive goods and services for productivity and growth. Why is there not already greater empirical evidence of their impact on output? Certainly, the reality is that, since the global financial crisis, overall productivity growth has been very slow in absolute terms and relative to previous decades, in advanced and emerging market countries.

There are clearly wider forces at play, such as the hypothesis of "secular stagnation" as proposed by Larry Summers (2016), and history tells us that that lags are historically evident between innovation and productivity.

But, we are already seeing growth effects from the surge in digital information flows. Indeed, the cited research from MGI finds that "cross-border flows of goods, services, finance, and data during this period increased world GDP by roughly 10% – roughly an additional \$7.8 trillion in 2014 alone. Data flows exerted a larger impact on growth than global goods trade" (Tyson and Lund 2016).

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1 This paper is based on a presentation at the T20 Trade and Investment Conference, June 8 2016, Geneva, Switzerland.

2 These digital flows cover an expanding span of flows in cross-border electronic commerce issues, such as innovative technologies in information, manufacturing, biotech, energy, financial, and defence.

Let's now look at the broader potential implications of this surge in digital flows:

- Evidence is building through recent research that digital connections can directly promote productivity growth. Most importantly, barriers aside, the marginal costs of digital communications and transactions are potentially near zero, hence creating new scales for conducting cross-border business (ibid).
- This provides new and remarkable scope for companies to overcome local market constraints and connect globally with customers, suppliers, financing, and human resources.
- All of this offers new potential for developing economies to "move closer to the productivity frontier by exposing their business sectors to global and innovative technologies, investment, and best management practices" (ibid).
- Evidence also suggests that the potential could be higher in the tradeable services sector, such as trade in business services. This fits well with emerging markets' priorities, especially China which is rebalancing growth to focus on services, and India with its early emphasis on services, and India's creation of the world's first digital ID infrastructure that is transforming India's potential for online services.

But all this requires that countries build the necessary domestic digital infrastructure and provide access to global data flows. And we are not there yet:

- Much of the developing world still needs to bring their offline population online. Estimates are that more than half of the world's population, close to four billion people, are still offline.
- And, "in many developing countries, connectivity is too slow, unreliable, or expensive to allow entrepreneurs and individuals to take full advantage of these emerging new global business and educational opportunities" (ibid).
- This explains why digital globalization is already playing directly to the strengths of the United States and other advanced countries in technology and innovation—offsetting the disadvantages advanced countries faced during the period when low labour costs were paramount in global manufacturing value chains.
- McKinsey's research on the connectedness of countries linked to their participation in global flows (including of digital technology) finds that these flows are disproportionately concentrated among a small group of advanced countries. From emerging markets, China is the only country within the top ten of this Connectedness Index reflecting also its push to raise its innovation clusters.
- Certainly, developing countries will need to adjust their human capital by emphasizing education in technology and digital skills, to participate much more fully in digital globalisation. This is particularly important for the G20 to support, and ensure that countries with low cost labour do not lose out in jobs as digital technology and automation begin to take over.
- Thus, "lagging countries are closing their gaps with the leaders at a very slow pace, and their limited participation will have a real cost to the world economy" (Manyika et al. 2016). We

see this also in the indicators of declining productivity and growth, globally, and in emerging markets.

## Governance and Policy Challenges

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Let's now turn to the new policy challenges posed by the surge in digital trade flows and their governance implications. The reality is that globally there are high barriers to trade and investment in business and other services, and the challenge is how to promote an open and level multilateral playing field for trade in digital goods and online services. Regional trade and investment treaties, such as through the proposed Trans-Pacific Partnership and the Transatlantic Trade and Investment Partnership, are taking over from the WTO as the main forum for agreements, including for trade in services, although they are politically far from adoption (Schott 2016).

In its present form, it is important to note that the TPP seeks to promote a free and open market for digital goods and online services, prohibiting customs duties on digital goods. It also seeks to limit domestic restrictions on data flows, and encourages trade by SMEs, and introduces potentially binding dispute settlement procedures in all areas. Over time, these principles should lower costs and intensify the development of new digital goods and services.

The trade diversion risks for countries potentially excluded from such regional agreements, which are now also covering digital trade, are potentially more immense. These risks could constitute a new barrier to sustaining growth in areas that could be the forward anchor for boosting innovation, productivity, and growth, especially in services.

This is particularly important for India which needs to open new external markets for trade in services—that has been India's strength. Such external integration can also be a driver of needed domestic reforms for India's domestic economy.

At the same time, countries would create these risks by national efforts at "data localization"—which could limit cross-border data flows, servers, and storage with potentially high regulatory and compliance costs. Recent research clearly indicates that such regulatory barriers that impede adoption and diffusion of technology are already affecting investment and growth in a number of countries (Bauer et al. 2014).

This emphasises the need for universal standards and raises the stakes for the G20 to support the WTO's efforts to play this role and negotiate agreements for trade in services. An early test is the Trade in Services agreement, initiated by the United States and Australia, with at least 50 participants that represent 70 percent of the world's trade in services. The WTO established the last major services agreement, the General Agreement on Trade in Services in 1995 but, since then, as we have seen, the world has evolved dramatically from the result of technological advances, and deeper global digital flows and integration.

An agreed multilateral approach is needed to strike the right balance between assuring digital openness while mitigating the privacy and security risks inherent in a new stage of interconnectedness and globalisation. Otherwise, rising protectionist sentiments could especially affect investment and growth in developing countries who are still distant from the productivity frontier.

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# A Proposed G20 Sustainability Package

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Sustainability moved decisively towards being a core value of the global community in 2015.<sup>1</sup> In September, the United Nations General Assembly adopted a new 2030 Agenda for Sustainable Development including 17 Sustainable Development Goals (SDGs) that provide depth and clarity for the international community's ambitions for economic, environmental, and social progress over the next 15 years. In addition, 195 countries came together in Paris in December and concluded a new climate change accord that lifts the trajectory of the global response to the build-up of GHGs in the atmosphere and commits the nations of the world to significant actions to reduce the threat of climate change. The breadth and depth of these commitments to make sustainability a fundamental element of the global community's "collective journey" (United Nations 2015b, 1) creates both challenges and opportunities for the international trade and investment regimes.

As a critical forum for global economic governance, the G20 (with strong leadership from China as the host nation for the 2016 G20 Summit) could provide important direction to the WTO, countries engaged in regional and bilateral trade and investment agreements, and managers of banks and funds (both public and private) that seek to promote economic development on the importance of conducting their activities in a manner that reinforces the SDGs and the 2015 Paris Climate Change Agreement. This paper offers an array of ideas on how to weave the concept of sustainability into the fabric of international cooperation on trade, investment, and development—including the institutions of global economic governance.

In advancing this agenda, the G20 has an opportunity to address some of the tensions that are inherent in the concept of *sustainable development* and to provide a framework for operationalising the world community's commitment to a sustainable future. Absent such efforts, there exists a real risk that the trade and investment regimes will advance principles and practices that conflict with the SDGs and the actions required to fulfil the global community's goal of mitigating the risk of dangerous anthropogenic climate change as well as the "intended nationally determined contributions" (INDCs) to reducing GHGs submitted by 188 nations.

China is particularly well-positioned to play a leadership role in developing and promoting this proposed initiative as it has powerfully demonstrated in recent decades how economic success can advance the sustainability agenda—and has long been committed to a peaceful and mutually beneficial development agenda that pursues "win-win" solutions to advance a "harmonious world." In fact, a commitment to operationalise the concept of sustainability within economic development strategies and institutions would be a logical extension of former Chinese President Hu Jintao's vision of a "scientific outlook on development" (Xinhua 2012) which has been reaffirmed and extended by China's present leadership including President Xi Jinping.

## Sustainability as a Central Pillar of Global Cooperation in the 21st Century

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One reason for the success of the negotiations leading to the SDGs and the 2015 Paris Climate Change Agreement was a willingness to leave behind 20<sup>th</sup> century frameworks and assumptions. In both cases, the world community united around a concrete agenda for action that goes beyond past talk and targets—and moves towards a multidimensional "solutions" strategy for global cooperation. Both agreements draw all nations into the pursuit of ambitious global efforts with a clear emphasis

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<sup>1</sup> The author wishes to thank Yume Hoshijima for research assistance for this paper.

on every country playing a role on the basis of “common but differentiated responsibility” and “respective capabilities.” And both offer an integrated vision of how international cooperation should proceed with a clear recognition that economic, environmental, and social priorities must be pursued in parallel.

Both the SDGs and the new Climate Agreement recognise, furthermore, that real progress on these challenging agendas of sweeping scope will require more than the signatures of presidents and prime ministers on a UN declaration. Success depends on building a “bottom-up” implementation strategy of much broader engagement than has been emphasised in the past—drawing mayors, governors, premiers, CEOs, and civil society leaders into the conversation and ensuring that cities, states, and provinces as well as the business community and the whole world of non-governmental organisations to play a role in delivering the results that have been called for. The same spirit of broader engagement and emphasis on a solutions orientation that meets the on-the-ground needs of people everywhere would be useful in energising global economic governance and integrating sustainability into the trade and investment regimes as a core principle and guide to action.

## Sustainability in the International Trading System

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While global governance related to sustainability reached a high water mark in 2015, the WTO continues to struggle. In a number of nations across the world, critics of freer trade have cast doubt on the value of recent trade agreements and have celebrated the demise of the Doha Round of negotiations. These critics suggest that trade liberalisation tends to diminish economic prospects in some countries and for some workers and that the economic growth that trade produces often comes at the price of environmental degradation. There is a long literature that evaluates such claims both in theory and practice (e.g. Esty 1994; Frankel and Rose 2005; Howse 2008). And while the depth and substance of these claims can be debated, what is beyond doubt is that many people, organisations, and political leaders around the world have come to believe the trading system diminishes rather than enhances prospects for sustainable development.

If a global commitment to international economic integration is to be revitalised and trade liberalisation and free flowing foreign investment are again to be seen as critical engines of economic growth—and thus potentially important drivers of sustainable development—the arguments of the critics must be addressed. In particular, the G20 should confront the fear that the trading system and the institutions of international economic governance, including the WTO, will undermine rather than reinforce the recently sharpened focus on sustainability as a core concern of the global community. To put a finer point on this observation: a G20 initiative to demonstrate that the trading system will be managed in a manner that takes sustainability seriously could enhance the system’s legitimacy in a very important way.

The foundations for such an initiative are already in place. The 1994 Agreement that created the WTO makes clear in its Preamble that sustainable development is to be a core principle of the organisation (United Nations 1994). And the Marrakesh package of agreements contains numerous other references to various dimensions of sustainability as well as the need to protect the environment (see e.g. United Nations 1994a, 1994c, 1994d). But the critics remain worried that the trading system’s vision of sustainable development is more focused on development than sustainability—and more concerned about economic growth than environmental progress. More broadly, they doubt that

global economic governance will be managed in a way that advances the SDGs and the commitments of 188 nations to control their GHGs and reduce the threat of climate change.

The G20 could confront these fears head-on with an initiative to embed the concept of sustainability more deeply into the principles and practices of the WTO and all future trade agreements, whether bilateral, regional, or multilateral. Such a "Sustainability Initiative" might include a number of elements.

### **Sustainability Endorsement**

As a clear signal of the G20 nations' commitment to sustainability as a core principle of international cooperation, the September Summit could adopt a resolution declaring that the institutions of international economic governance should be guided in all of their work by the SDGs and the 2015 Paris Climate Change Agreement.

### **WTO Sustainability Commitment**

The G20 might further suggest that the trade regime formalise this commitment through a WTO General Council interpretive statement reiterating the importance of sustainable development as a goal, acknowledging the 2015 international agreements that heighten the global community's focus on sustainability as a core principle, and indicating (perhaps using section 104 of the North American Free Trade Agreement as a rough guide<sup>2</sup>) that WTO practice, including dispute settlement panels, will seek to interpret and advance trade principles in a manner that is consistent with the SDGs and climate change commitments. This statement could include an express acknowledgment that in the event of a perceived inconsistency between a country's obligations under WTO rules and its obligations under the Paris Climate Change Agreement or the 2015 Agenda for Sustainable Development, the WTO will interpret the GATT rules (notably Article XX) and any other trade or investment obligations in a manner that permits the SDG initiatives or GHG controls to go forward, so long as the country has chosen policy options that treat international and domestic interests similarly and has not overlooked obvious ways to reduce inconsistencies with its WTO obligations.

Secondly, the G20 might suggest a WTO General Council interpretive statement that explicitly places the SDGs and Paris Climate Change Agreement within the exemptions listed in Article XX of the GATT. Given the multilateral consensus behind both of the 2015 agreements, activities undertaken in implementing these agreements might be presumptively covered by Article XX(b) (measures "necessary to protect human, animal or plant life, or health") or XX(g) (measures "relating to the conservation of exhaustible natural resources"). Such a clarification would allow nations to pursue climate change actions and sustainability projects with less fear of interference from the international trade system. But the language would need to be carefully crafted to avoid creating a new structure that protects hidden trade barriers in the guise of sustainability.

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2 The North American Free Trade Agreement (1992, § 104) states that in the case of "any inconsistency" between the agreement and "specific trade obligations" contained in several explicitly named multilateral environmental agreements, the trade obligations in the environmental agreement "shall prevail to the extent of the inconsistency, provided that where a Party has a choice among equally effective and reasonably available means of complying with such obligations, the Party chooses the alternative that is the least inconsistent with the other provisions of this Agreement."

## **Sustainability Impact Assessments**

The 2016 G20 Summit could break new ground with a call for the undertaking of “sustainability impact analyses” (SIAs) as an analytic underpinning for all new trade agreements. Such SIAs might require governments at the launch of negotiations to identify: (a) opportunities to enhance efforts to make progress on the SDGs or to implement the 2015 Climate Change Agreement, (b) tensions or risks that might arise from expanded trade or investment under the proposed topics for negotiation, and (c) a game plan for fulfilling the opportunities and mitigating the risks that have been highlighted. Such a requirement, modelled on the EIAs required by many nations (see Wood 2002), would further ensure the alignment of trade practice and future trade liberalisation efforts with the logic of sustainability as a defining feature of international cooperation.

## **Support For Sustainability-Enhancing Market Access**

The 2016 G20 Summit might further agree to participate in and expedite trade negotiations that would expand the flow of goods, services, and capital that support the implementation of the climate change and SDG agendas. For example, the EGA, which would reduce tariffs for environmental and energy technologies that support implementation of climate change commitments and the SDGs, does not enjoy universal participation among G20 members. Participation by the entire G20 could promote broader support for trade liberalisation in this critical sector. Such an initiative would fit nicely in the post-Doha world of trade liberalisation through sectoral agreements that can garner broad support.

The G20 could also provide new momentum for the various WTO programmes that promote export sectors in developing countries (and thus the prospect of sustainable development), including: DFQF market access, AfT, and the Enhanced Integrated Framework for Least Developed Countries. Although the WTO Ministerial Conferences at Bali (2013) and Nairobi (2015) made substantial progress on these fronts, further work is needed to expand sustainable development opportunities for the world's poorest countries.

## **Prohibition on Sustainability-Threatening Policies**

The G20 could also push for an agreement on “pollution haven” provisions in future regional trade agreements that would prohibit countries from relaxing environmental standards to attract investment (similar to Section 114 of the North American Free Trade Agreement 1992). Such provisions would strengthen efforts to advance the SDGs and the INDCs that stand at the heart of the 2015 Paris Climate Change Agreement. By reducing the incentive to attract FDI by defecting from the recently-made sustainability commitments, the trading system would be seen as explicitly reinforcing the new climate accord, the SDGs, and other multilateral environmental agreements.

## **Sustainability-Enhancing Rules**

The 2016 G20 Summit might also take up the call for a broader agenda of “sustainability-enhancing rules interpretations” at the WTO and in other trade and investment agreements. Such an initiative—designed to ensure that trade regime practices do not inhibit global, regional, national, or local efforts to reduce GHGs or advance programs to meet the SDGs—might advance reinterpretations of both core WTO principles and those in related agreements. With respect to core principles, a rules interpretation that moves away from the problematic product/process distinction and acknowledges

that in a world concerned about climate change how goods get produced can be as important as *what* gets made, would be seen as important step towards reconciling long-standing trade and environment tensions.

In this spirit, the G20 nations might invite the WTO (perhaps through the Committee on Trade and Environment) to produce a study that analyses the rules and procedures of the international trading system and identifies those that might negatively impact the global climate and sustainable development regimes. Such a "consistency" review would help the global community limit transboundary pollution spillovers and potential races towards the bottom.

With respect to specific agreements concluded under the WTO, the G20 could push for interpretations of the SCM Agreement and the Agreement on Technical Barriers to Trade (TBT) that advance sustainable development and climate change objectives. For example, the SCM Agreement might be interpreted to require the phase-out of fossil fuel subsidies—widespread market distortions estimated to total about US\$500 billion/year (Coady et al. 2015, 31)<sup>3</sup>—that the G20 has previously condemned as leading to "wasteful consumption," and to outcomes that "distort markets, impede investment in clean energy sources and undermine efforts to deal with climate change" (G20 2009). As former WTO Director-General Pascal Lamy has noted (2013): "[D]iscussion on the reform of fossil-fuel subsidies has largely bypassed the WTO. This is a missed opportunity." Fossil fuel subsidies could be regulated as an anticompetitive dual pricing scheme under Articles 1.2, 2, and 5 of the SCM Agreement (Meyer 2013), promoting more efficient markets and a faster energy transition.

Conversely, the SCM Agreement might be interpreted so as to maximise opportunities for nations to subsidise renewable energy investments and other activities that promote INDC and SDG attainment. We recognise that G20 members including China, Canada, the EU, India, Japan, and the United States have had past disagreements about how to handle renewable energy subsidies (see e.g. WTO 2011, 2012, 2013). These conflicts are counterproductive because they increase regulatory risks for clean energy investors and produce uncertainty in the clean energy marketplace—raising the cost of capital and reducing the flow of funds to both energy efficiency projects and renewable energy investments. A clear interpretation of the SCM Agreement that allows for domestic renewable energy subsidies under defined circumstances (that avoid hidden protectionism and anticompetitive practices) while retaining strong anti-dumping protections would facilitate the energy transition anticipated by the 2015 Paris Climate Change Agreement (see generally Charnovitz 2014).<sup>4</sup>

Similarly, the TBT Agreement should be interpreted to enable and not inhibit energy efficiency standards, mandatory efficiency labelling, and similar regulations. Thus, the 2016 G20 Summit might call for Section 2.2 of the TBT Agreement—which recognises "protection of human health or safety, animal or plant life or health, or the environment" as a "legitimate objective" exempted from the TBT disciplines—to be interpreted to include policies and programmes aimed at attainment of INDCs and promotion of the SDGs.

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3 They note that the International Energy Agency estimated that fossil fuel consumption subsidies were US\$548 billion in 2013 and that the International Monetary Fund estimated that "pre-tax" fossil fuel subsidies were US\$492 billion in 2011. The IMF considers a typical subsidy as a "pre-tax" subsidy and the absence of a socially optimal carbon charge as a "post-tax" subsidy.

4 He discusses how green subsidies can violate SCM Agreement obligations.

While some would see these rules refinements and reinterpretations as narrow and “technical,” they would—as a package—go a considerable distance towards reconciling long-standing trade and environment tensions and enhancing the legitimacy of the WTO in a world where sustainability has become a fundamental value.

## Sustainability in Development Assistance

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In addition to initiatives focused on the trading system, the G20 nations might also seek to align global flows of capital and aid with the requirements of the 2015 sustainability agenda. Once again, China is well-positioned to lead such an effort. Indeed, China might catalyse such a commitment by having the Asian Infrastructure Investment Bank (AIIB) produce model sustainability guidelines, which could then be adopted for other sources of economic development funds both public and private. Alternatively, China could produce the model guidelines in the context of its OBOR initiative, which aims to enhance regional trade by promoting infrastructure development. The AIIB and OBOR both seem poised to provide substantial capital to help ensure that developing countries have the requisite roads, bridges, and ports necessary for export-oriented economic development—and thus provide a critical place for the new global commitment to sustainability to be prominently embedded.

The broader argument for bringing a focus on sustainability to development assistance builds on a recognition that the mandates created by the new climate change accord and the SDGs will demand unprecedented amounts of investment. The Addis Ababa Action Agenda, adopted by the UN General Assembly in July 2015, describes a US\$1 trillion to US\$1.5 trillion annual funding gap in developing countries for infrastructure needs *alone* (United Nations 2015a). At the same moment, there is a savings glut in some places and large pools of capital looking to be deployed (Bernanke 2015). Combined with new sources of public finance like the AIIB, these funds provide an ideal starting point for a G20 initiative that would aim to expand development assistance through a new model that uses limited public resources to leverage private capital. But the long-term benefit of the projects undertaken will be judged by their environmental impacts as well as their contributions to economic growth. So the undertaking of SIAs in advance of the commitment of funds to any development project would be a breakthrough.

The SIA obligation should apply to all multilateral development banks and national aid programmes—and be encouraged for all private investors. Only if the sustainability impacts of new economic activity are carefully and deliberately managed can the world community be confident that these financial flows and investments are consistent with the 2015 sustainable development and climate change objectives.

The energy and environmental effects of proposed projects and investments must be rigorously and transparently assessed by reference to clearly-specified SIA standards that account, in particular, for long-term implications. Existing development banks must strengthen their standards, and the new AIIB can play a particular role by developing innovative approaches to impact assessments.

## Sustainability in National and Local Economic Strategies, Programmes, and Projects

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One final element of the 2016 G20 Sustainability Initiative might be a commitment from all of the assembled countries to ensure that their national as well as regional and local economic initiatives will be undertaken in ways that reinforce and do not undermine the SDGs and the 2015 Paris Climate Change Agreement. Given the importance of these strategies alongside international efforts, such a commitment would ensure alignment with the principle of sustainability as an underpinning of 21<sup>st</sup> century policies at every level

### The G20's Special Role

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The logic of having the G20 advance the proposed Sustainability Initiative reflects not only the group's role as the de facto global economic governance steering committee, but also the group's enormous economic and demographic clout. Moreover, the G20 nations include all of the world's major GHG emitters and collectively account for 75 percent of global GHG emissions (Morales 2015). In addition, the G20 nations provide 94 percent of the official development assistance that flows to the developing nations of the world through multilateral development banks and national aid programmes (G20 2013). And the G20 nations are home to the companies that represent 65 percent of FDIs across the world (UNCTAD 2016). Thus, the G20 nations both individually and as a group are the "pivotal states" when it comes to setting the global economic agenda (see Esty 1999).

The G20's commitment to making sustainability a core principle in economic decision-making at the global, regional, national, and local levels could transform the future for every citizen of the planet. In the SDGs and the 2015 Climate Change Agreement, the world community spoke loudly, clearly, and repeatedly about the need to transform the foundations of international cooperation, including the policy frameworks that guide trade, investment, and development assistance. The G20 could take the next step and operationalise this commitment to sustainability as a core principle of international economic relations—and, in doing so, help to ensure the success of the global commitment to a sustainable future that delivers on the promise of a world transformed by 2030 along the 17 dimensions highlighted by the SDGs and diminishes the threat to progress and prosperity across the planet posed by climate change.

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# G20 Hangzhou Summit 2016

## Proposals for Trade, Investment, and Sustainable Development Outcomes

Leaders from the Group of Twenty (G20) major economies will gather in Hangzhou, China in September 2016 to address a range of shared governance priorities. This year's Chinese presidency has identified trade and investment as a key priority for the 2016 summit, interconnected to and supportive of three other focus areas including growth, economic and financial governance, and inclusive and interconnected development. The International Centre for Trade and Sustainable Development (ICTSD) has provided inputs into the G20's consultative process around trade and investment in order to generate ideas for its work in the mid and long term.

Successive G20 leaders' communiqués have recognised the importance of trade and investment in driving economic growth, job creation, and sustainable development. The G20 has also affirmed the need to work to ensure that trade agreements whether bilateral, regional, and plurilateral contribute to a stronger multilateral trading system.

This volume brings together a series of short papers by leading experts and practitioners that evaluate future contributions the G20 could make to global governance in trade and investment. The pieces variously focus on how the G20 might continue to work towards strengthening and ensuring coherence between the WTO and the wider international trading system, boost global growth, refine investment rules, respond to different views on the speed and nature of economic integration, and foster inclusive global value chains that offer viable development paths, all underpinned by a commitment to sustainable development as a guiding compass for global economic governance and the trading system.



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