

# G7 LEADERS SHOULD DISCUSS INTERNATIONAL TRADE (SERIOUSLY)

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## KEY POINTS

For the first time, the G7 has an explicit ‘trade track’ as part of its discussions. This opens the door to cooperation and progress in a range of key areas.

- International trade is increasingly about services, digital products and delivery, domestic regulation, and links to non-trade areas such as health and climate change. The WTO is struggling to keep up. The UK should use its G7 Presidency to help overcome its slow progress by leading the G7 to create a system to facilitate open plurilateral agreements (OPAs).
- In addition to discussions on the role that trade can play in addressing the COVID pandemic, G7 leaders should recognise that trade and investment agreements need to make it easier for governments to pursue legitimate health policies with regard to non-communicable diseases in non-discriminatory and minimally trade-distorting ways.
- The G7 can also advance the possibility of future policy coordination over data regulation by including specific policies and recommendation on digital trade as part of the G7 communique.
- The G7 could help to reduce CO<sub>2</sub> emissions by establishing a road map for determining acceptable parameters to resolve the Carbon Border Adjustments (CBAs) trilemma and considering a climate club where countries with ambitious climate targets work together while levying a CBA on those countries with less ambitious targets.

## INTRODUCTION

The G7 summit agenda includes an explicit ‘Trade Track’ comprising of four items for discussion: WTO reform; trade and health; digital trade; and trade and climate policy.<sup>1</sup> These topics cover significant and inter-related areas of international trade policy. We commend their inclusion in the summit, but we are also conscious that they are broad and complex issues without easy or quick solutions.

In this Briefing Paper, we briefly summarise the significance of each trade track area and offer recommendations for desirable actions. We recognise that a G7 meeting can only start off a process of delivering global solutions in these areas, but every journey starts with a single step. We first deal with WTO reform, or more precisely a specific aspect of WTO reform which concerns what are known as ‘plurilateral’ agreements. This analysis and the recommendations therein also inform the discussion of climate change and digital trade.

<sup>1</sup> <https://www.g7uk.org/trade-ministers/>

## WTO REFORM: PLURILATERAL AGREEMENTS

It is widely accepted that international economic relations depend upon a smoothly functioning multilateral trading system. That trading system, institutionally underpinned by the World Trade Organization (WTO), can both stimulate economic activity and help to promote international cooperation in spheres such as climate change and migration. However, the WTO is becoming less relevant to a world in which services account for a growing share of trade, interest in environmental regulation (notably on CO<sub>2</sub> emissions) is growing, and digital technology is reshaping our lives.

These issues impinge directly on international trade and thus fall within the broad remit of international rule-making in the WTO. However, decision making in the WTO typically requires consensus from all the Members, which is difficult to achieve when Members have different ideas about what the appropriate rules for dealing with such challenges are. Thus, not only has it become difficult for countries to agree on how to move forward, but these differences are creating new tensions in the global trading system.

One solution that would help to overcome the impasse would be to facilitate those within the WTO who want to change particular rules to proceed among themselves by signing so-called ‘plurilateral’ agreements. However, at present there is insufficient trust by those who do not want change to allow those that do want this kind of change to go down this route.<sup>2</sup>

As chair of the G7 discussion, the UK could make a major contribution by leading the G7 to agree a system that made such plurilaterals more constructive and less threatening to others. The open plurilateral agreements (OPAs – Hoekman and Sabel, 2021)<sup>3</sup> that we have in mind would be fairly narrowly focussed agreements signed by a subset of WTO Members, which committed them (and only them) to take on new obligations. The rights that these obligations created for others would either (i) apply to all WTO Members or (ii) apply only to other signatories of the plurilateral, but with a condition that the plurilateral would be open to any other WTO Member to join. These agreements would have to ensure that:

- they did not curtail other Members’ existing rights but added to them, and that if the signatories did not honour the agreement they would be subject to challenge; and that
- membership would be genuinely open, including, where appropriate, technical assistance to help less well-off countries develop the capacity to meet the plurilateral’s obligations.

A new system would:

1. define a code of conduct that committed signatories to these requirements,
2. create a mechanism, involving transparency, information exchange and dialogue to try to resolve tensions within each OPA before they became full-blown WTO disputes,
3. support early analysis to optimise the design of OPAs in ways which were seen to be even-handed, and
4. establish a means for the WTO to monitor the performance and effects of OPAs.

If each G7 member committed that any plurilateral in which it was engaged would respect items (1) and (2), and if, together, they actively promoted items (3) and (4), it would go a long way towards persuading non-signatories that they had sufficient protections. This would give WTO Members as a group the confidence to welcome proposals from subsets of them to advance on certain rules and thus start the process of updating the WTO for the twenty-first century.

## TRADE AND HEALTH

The Trade Track contains a fairly detailed discussion of trade and health in the [Communique from G7 Trade Ministers](#) (28<sup>th</sup> May 2021).<sup>4</sup> It is largely concerned with the role that trade can play in addressing the COVID pandemic: it promises to ‘prioritise discussions and support work at the WTO in identifying solutions to expand global vaccine production and distribution’; ‘support[s] open, diversified, secure, and resilient supply chains in the manufacture of Covid-19 critical goods and vaccines and their components, as well as broad global availability’, and reaffirms the role for the Trade Facilitation Agreement in easing COVID-related trade. G7 leaders should certainly endorse these sentiments and commit personally to furthering them.

One thing that is missing is any discussion of so-called non-communicable diseases (NCDs), which kill an estimated 42 million people a year. Significant

<sup>2</sup> It is always open to subsets of members to sign Free Trade Agreements, subject to some conditions one of which is that the FTA has a fairly broad reach. Moreover, FTAs do not support the multilateral trading system but instead create closed clubs of countries that treat each other preferentially.

<sup>3</sup> Hoekman, B. and C. Sabel. 2021. “[Plurilateral Cooperation as an Alternative to Trade Agreements: Innovating One Domain at a Time](#),” *Global Policy*, 12(S3): 49-60: <https://onlinelibrary.wiley.com/doi/full/10.1111/1758-5899.12923>

<sup>4</sup> G7 Trade Ministers’ Communiqué: <https://www.gov.uk/government/news/g7-trade-ministers-communiqué>

parts of this are due to tobacco consumption, the excessive use of alcohol and unhealthy diets. The producer industries concerned sometimes resort to international trade and/or investment agreements to hinder governments' attempts to regulate their practices. G7 leaders could make a valuable contribution by recognising that NCDs are a major problem and that trade and investment agreements need to be written or amended to make it easier for governments to pursue legitimate health policies in non-discriminatory and minimally trade-distorting ways. Doing so would affirm that trade and health can be mutually supportive and so help to bolster the rules-based world trading order that has brought so much prosperity to the modern world.

## DIGITAL TRADE

Digital trade encompasses digitally ordered transactions such as e-commerce and digitally delivered services, ranging from publishing, telecommunications, or audiovisual services to the use of artificial intelligence (AI) in the provision of goods and services. The value of digital trade, whilst difficult to ascertain with accuracy, is huge: in 2019, the global value of international e-commerce stood at an estimated \$3.6 trillion, to which digitally delivered services would add another \$2 trillion. Thus, by some estimates, digital trade was likely worth \$5.5 - 6 trillion in 2019, or roughly a quarter of total world exports. Furthermore, digital trade is expanding rapidly: global exports of computer services, for instance, grew by 11% in 2019. Fundamentally, digitisation changes how and where goods and services are produced and consumed, and in particular can support the trading ambitions of small enterprises. In the UK, the smallest businesses—those with fewer than ten employees—were able to capture £4.5 billion worth of overseas e-commerce (digitally-ordered transactions) sales in 2019. From additive manufacturing to artificial intelligence, digitisation also leads to more and more services being used in production. In so doing, digital trade affects the competitiveness of all sectors.

Underpinning digital trade is the movement of data, which in turn requires regulatory oversight. Regulation is needed because the data that are being moved across borders may raise concerns about consumer protection, cyber security, or intellectual property rights. The uneven capacity to benefit from digitisation and digital trade, referred to as the 'digital divide', also raises distributional concerns and is—again—one reason why some less well-off countries are very reluctant to move forward on digital trade within the WTO. Moreover, countries' preferences over what is deemed optimal in each of the aforementioned

areas of public policy, from privacy to intellectual property protection, vary quite significantly. Hence, international policy coordination is prone to be difficult. Analogously to carbon leakage, there is a risk of 'data governance leakage' giving countries with less demanding regulatory regimes a competitive advantage over those with more demanding regulatory regimes.

In as much as more international coordination on digital trade policy is needed, countries also first need to have their own national conversations about their objectives in regulating digital activity and the trade-offs that this entails. These dialogues can crystallise e.g. in National AI Strategies or National Data Strategies (the UK published one in September 2020). If digital trade rules emerged from international bodies and/or trade agreements without such domestic consultations or at least broad-based implicit domestic consent, there could eventually be a backlash against trade cooperation in general.

The G7 are clearly not in a position to resolve the international policy coordination issues raised by the growth of digital trade. But the group could advance the possibility of future policy coordination by:

- Agreeing on the importance of international coordination on policies over data flow regulation. This entails exploring mechanisms for rendering the prevailing approaches to data governance more interoperable. This dialogue will have to engage China in some form, which is neither part of the G7 nor a guest at the upcoming summit.
- Recognising that the presence of a few large digital intermediary platforms entails opportunities and risks. The G7 economies are home to many of these companies and the group should therefore explore ways of coordinating on competition policy in a way that would have global benefits.
- Agreeing on the need to have better statistical evidence on the extent of digital trade, and on barriers to digital trade and their consequences.
- Supporting and endorsing the e-commerce negotiations currently underway at the WTO, which have gathered momentum in the run-up to the WTO's 12<sup>th</sup> Ministerial Conference. In April 2021, WTO Members finalised a clean text on e-signatures and authentication, and the G7 should throw their weight behind reaching agreement in other areas as well, such as online consumer protection, customs duties on electronic transmissions or open internet access, amongst others.
- Without undercutting the multilateral efforts, exploring the possibility of solutions through

a digital trade open plurilateral agreement and support this initiative with technical work, capacity building, full transparency and mechanisms for a far wider constituency than just rich countries to discuss the issues.

The completion of a digital OPA will depend on the ability to agree on a common, minimum set of regulatory principles, and a degree of flexibility that takes into account the different preferences of the OPA members; as well as transparency and monitoring and a means of discussing and addressing tensions and disputes. This will require considerable dialogue and interaction between governments, businesses, and consumer interests.

Including digital trade as part of the G7 communique could prove to be a significant step towards international policy coordination in this space, and it could be aided by creating the right conditions in the WTO for plurilaterals.

### TRADE AND CLIMATE POLICY

The impacts of CO<sub>2</sub> emissions on climate change are at the forefront of policymakers concerns. This can be seen in the ongoing revisions to national mitigation policies with many countries adopting more ambitious emissions reductions targets. It has, however, two potential unintended consequences. First, in so doing it increases costs for domestic industries, and may thus reduce their international competitiveness with respect to countries with less ambitious for policies / reductions. Second, it may encourage industries to relocate to locations with less onerous restrictions (carbon leakage) – thus undermining the global need to reduce carbon emissions.

One solution, which is being increasingly discussed and considered by policymakers, is that of Carbon Border Adjustments (CBAs). The idea behind CBAs is to tax the import of goods that have been produced in locations / countries which allow for more carbon-intensive methods. While CBAs could (in part) address the competitiveness and carbon leakage issues - from a policy point of view they raise an environmental, technical and equity trilemma.<sup>5</sup>

From an environmental perspective, CBAs should capture as many CO<sub>2</sub> emissions as possible which suggests they should be wide-ranging. From a technical perspective, calculating the amount of CO<sub>2</sub> in imported products is tricky and so the scope of CBAs should be narrow in order to increase their feasibility and cut down on red tape for businesses. From an equity and non-discrimination (WTO-compatibility)

perspective, CBAs should not discriminate between domestic producers or trading partners and should take into account the needs of developing countries, which historically have contributed less to climate change and have fewer resources to meet the challenges of climate change mitigation. The higher the rates and the wider the range of taxed imports, the more likely it is that producers and/or national governments will raise complaints regarding equity and non-discrimination.

Balancing these concerns will be extremely difficult, yet CBAs will almost certainly have to be part of the solution. The G7 could help make progress on this, by:

- acknowledging the need to resolve the CBA trilemma by establishing a road map for determining acceptable parameters for each of its elements;
- considering a climate club where countries with ambitious climate targets work together by agreeing on how to determine equivalence in domestic carbon charges, such as linking emissions trading schemes, while levying a CBA on those countries with less ambitious targets.

For a climate club to work and indeed for the resolution of the trilemma there will need to be transparency and dialogue, means for addressing tensions, and an enforcement mechanism which allows either side to impose tariffs (CBAs) if the other isn't keeping pace. If this sounds familiar – then an exclusive plurilateral (where the benefits are shared among participants only) may well be part of the viable solution.

CBAs are likely to be part of the trade-related solution to climate change, but there are other, complementary policies also to be considered including the liberalisation of tariffs in environmental goods and services, coordination/agreement on eco-labelling and policies to reduce fossil-fuel subsidies (see for example the Agreement on Climate Change, Trade and Sustainability between New Zealand, Costa Rica, Fiji and the EFTA countries<sup>6</sup>).

<sup>5</sup> See <https://blogs.sussex.ac.uk/uktpo/publications/the-carbon-border-adjustment-trilemma/> for a fuller discussion

<sup>6</sup> <https://www.mfat.govt.nz/en/trade/free-trade-agreements/trade-and-climate/agreement-on-climate-change-trade-and-sustainability-accts-negotiations/>

## CONCLUSION

As we noted at the outset, a G7 meeting cannot deliver complete global solutions in these areas - just as we have seen with regard to the G7 multinational 'tax deal'.<sup>7</sup> But the G7 and the UK's Presidency could provide the initiative and leadership to get the ball rolling. The G7's drive in actively advocating and supporting broader efforts in each of the four areas could be instrumental in generating genuine progress.

### Editorial Note:

The G7 is an influential group of the seven largest democratic economies, which meets annually at Head of Government level to discuss issues and potential solutions of global concern. The G7 countries are: Canada, France, Germany, Italy, Japan, the United Kingdom and the United States. Presidency of the G7 group of countries is on an annual rotating basis with the UK taking on this role in 2021. This gives the UK the opportunity to influence what is discussed and guide the discussion. The G7 summit is being held 11-13<sup>th</sup> June in Cornwall, and the UK has invited Australia, India, South Korea and South Africa to join as guests.

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<sup>7</sup> G7 tax deal is 'starting point' on road to global reform, Financial Times: <https://www.ft.com/content/95dd0c00-7081-4890-bcef-b9642312db4d>

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## FURTHER INFORMATION

The UK Trade Policy Observatory (UKTPO), a partnership between the University of Sussex and Chatham House, is an independent expert group that:

- 1) initiates, comments on and analyses trade policy proposals for the UK; and
- 2) trains British policy makers, negotiators and other interested parties through tailored training packages.

The UKTPO is committed to engaging with a wide variety of stakeholders to ensure that the UK's international trading environment is reconstructed in a manner that benefits all in Britain and is fair to Britain, the EU and the world. The Observatory offers a wide range of expertise and services to help support government departments, international organisations and businesses to strategise and develop new trade policies in the post-Brexit era.

For further information on this theme or the work of the UK Trade Observatory, please contact:

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