



Global Governance of Public Goods: Asian and European Perspectives

12th edition

Sessions summaries

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France Stratégie, 18, rue Martignac, 75007 Paris, France

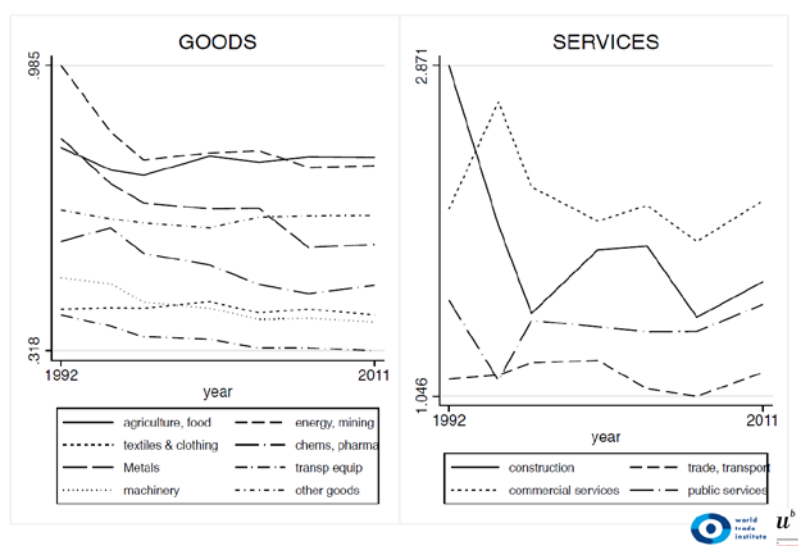
SESSION 2 - SLOWDOWN IN INTERNATIONAL TRADE

Chair: Yung-Chul Park, Distinguished Professor, Korea University

Thursday, October 1st the Cepii hosted the 12th edition of Asia Europe Economic Forum (AEEF). This conference aimed at discussing the global governance of public goods from Asian and European perspectives. The second session of the debate addressed the global slowdown in international trade. Recent downward trends in international exchanges rose concerns from trade economists. Indeed, post-crisis global trade did not recover its pre-crisis level. In that context, the causes and the possible policy responses have been investigated and debated. In particular, the discussion led by Yung-Chul Park, differentiated the cyclical from the structural component with a specific focus on the latter.

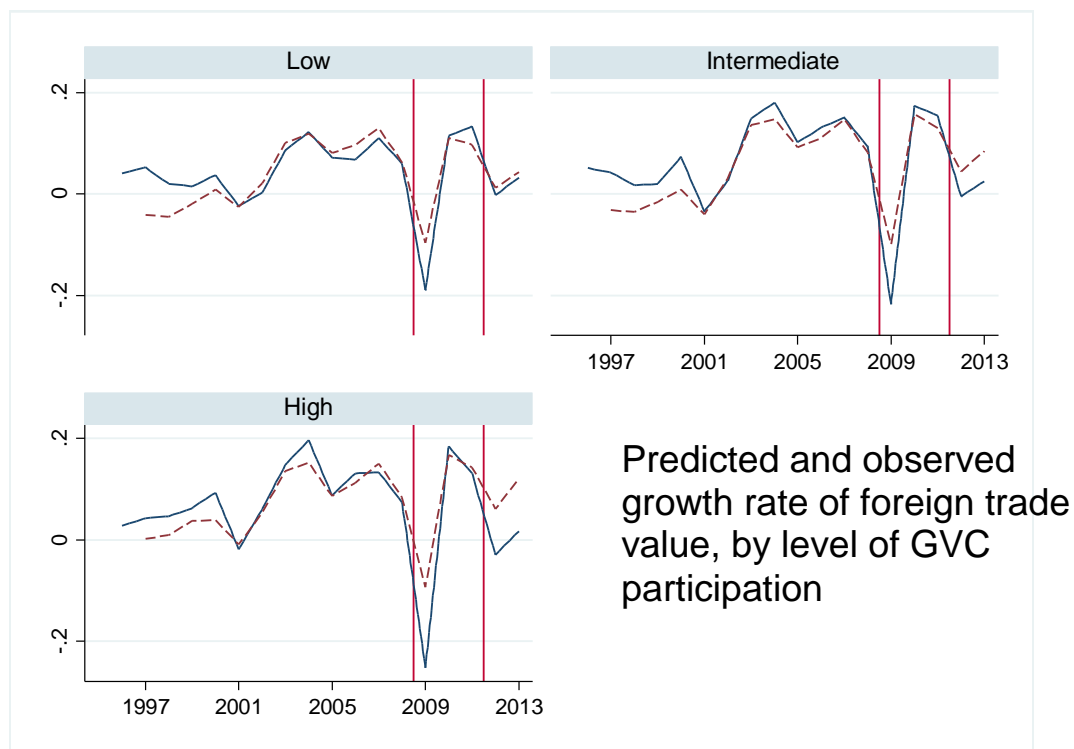
To begin with, global trends in international trade have been introduced by **Joseph Francois, Managing Director at the World Trade Institute**. Simple ratio between world trade and GDP volumes translate in leveling off tendency after the financial crisis period, while its evolution was constantly increasing since 1980. These global movements find an explanation in the increasing complexity of the production process. As a consequence of production's fragmentation, goods crossed several borders before reaching their targeted market, leading exchange flows growing faster than value-added. This is well depicted by the declining value-added share in exports value since 1990 (see graph 1 from Joseph Francois). This increasing production of fragmented goods raises the question of the cost in term of CO2 embodied. Extensive margin of trade have been addressed and quantified through social network theory. Again, a stabilization process seems to be at play after 2008 for big traders. While trade slowdown appears to be driven by the global financial crisis, the possible coincidence between both movements has been suggested. As a conclusion, the World Trade Institute director underlined the need to focus more on firms' regulation and cooperation than trade slowdown described as "a new normal".

Graph 1 - Total VA exports relative to gross export value



After a comparison of the pre and post crisis trade evolutions, **Sébastien Jean, Director of CEPII** underlined a phenomenon fitting the trade situation of most countries. The world trade slowdown is puzzling because it does not fit predictions. This is highlighted by the need for WTO to update its projections of trade volume within a year. Behind this fact, the relationship between trade and GDP is challenged. Declining gains of global value chains and China's rebalancing have been proposed as main causes of the situation. The global value chain has been one of the main drivers of trade growth during the 1990-2000 period. Taking advantages of differences between countries (in term of skills, wage, etc.), this production process led to an increase in international trade. However, most of the GVC gains have already been made and the marginal benefits of the vertical specialization are not as large as they used to be. Estimations realized on the pre crisis-period (1995-2008) have shown positive and high trade elasticity to income. Based on constant trade elasticity to output, predicted global trade growth for the post-crisis period (2012-2013) presents higher value than actual one. The gap between actual and predicted trade growth is very large and seems to increase over time, especially for Asian players and US. In order to test the global value chain's hypothesis, a decomposition of the world trade growth rate according to their global value chain participation have been considered (graph 2 from Sébastien Jean). Trade flows driven by high and intermediate global value chain participation display huge gap between predicted and observed flows during post crisis period. At the contrary, the predicted trade growth involving low GVC participation appears to be very close to the actual one. Build on a previous work with Charlotte Emlinger and Mathieu Crozet, results are consistent with the idea that the low hanging fruit of GVC has already been eaten.

Graph 2 - The gap between observed and predicted trade growth is larger where GVC participation is higher

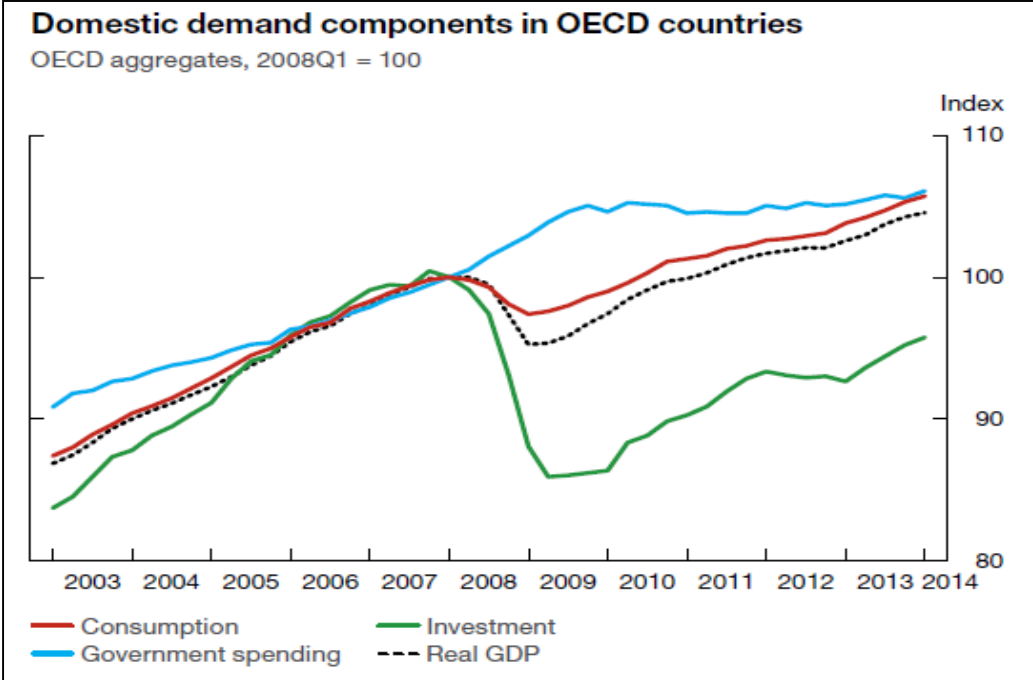


12 Source : Crozet, Emlinger and Jean, 2015.

The global financial crisis (2008-2011) has initiated new evolution perspectives for world trade as reported by **Masahiro Kawai, Senior Research Advisor at RIETI**. This caesura is illustrated by a post-crisis level of global trade much more below the pre-crisis period. Simple descriptive statistics comparing output and trade volumes show that the latter seems to be less responsive to variations of the former. This decreasing elasticity of global trade with respect to GDP can find explanations in both cyclical and structural factors. The low level of investment since 2008 can justify a downward trend in the short-term but cannot be a sufficient explanation (graph 3 from Masahiro Kawai). Structural explanations deal with China's rebalancing. The varying path of China's economic model is likely to reveal part of the trade slowdown. First, China goes progressively from an economy driven by export and investment to a consumption-led growth. Because of parts and components flows engendered by the former, this transition leads to less trade-intensive activities. A second factor related to China's changing pattern is the shift from a growth based on manufacturing activities to a services-driven growth. Again, this change is likely to bring less trade-intensive activities. Possible policy response to the global trade slowdown has been investigated through the gravity model. In particular, the role of Free Trade Agreements in promoting international flows and foreign direct investment has been examined. Data from emerging countries between 2002 and 2012 displayed a positive and high elasticity of export flows to FTA's. As a consequence, necessity for emerging economies to continue the liberalization process has been discussed. This could either be implemented through further tariffs cut or reduction of non-tariff barrier. The signature of new Free Trade Agreements is a possible way to increase trade flows between emerging economies. Hence, a special focus on actual negotiations' fulfillment (RCEP, TPP, FTAP or ASEAN-EU) has been privileged by Masahiro Kawai. The possible enlargement of the global

value chain process to emerging economies, which are not already integrate (Sub-Saharan Africa, South America, South Asia), could be another mean to benefit once more from vertical specialization.

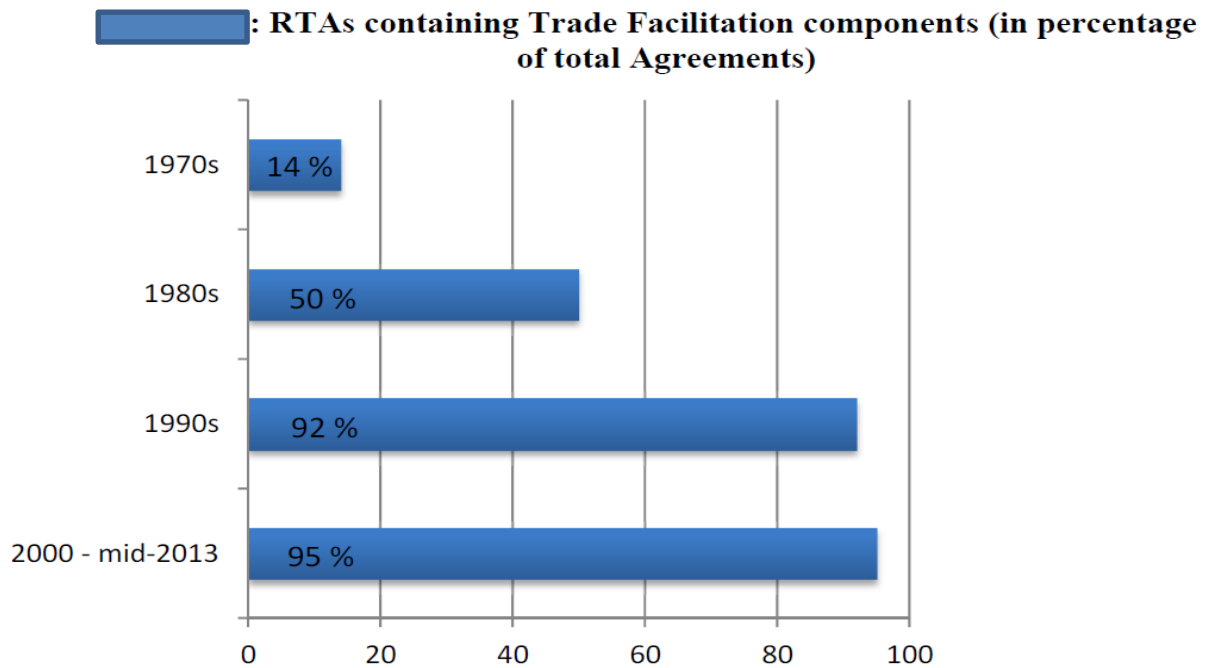
Graph 3 - Change in the composition of global demand



Note: Investment is gross fixed capital formation and comprises business, residential and government investment.

Source: Francis and Moreal (2015) from OECD *Main Economic Indicators*

To go further in the possible policy responses of the global trade slowdown, **Innwon Park, Professor at Korea University** purposed a focus on the combination of FTA's and Trade Facilitation provisions as a mean to benefit more from the FTA. This is a growing concern according to the Trade Facilitation provisions' evolution within regional trade agreements (see graph 4 from Innwon Park).Conclusions from previous works have been discussed before integrating RTA's and Trade Facilitation in a gravity model. Results suggest stronger trade-creating effect by combining both of them, according to data from 170 countries between 2000 and 2010. Moreover, the trade facilitation provisions do not divert international flows from efficient and non RTA's members to non-efficient and RTA's members, as it is the case when the effect of Regional Trade Agreements is taken on its own. In that sense, this trade policy appears as non-discriminatory. The presentation further differentiated trade effect between intermediate and final goods, underlying a higher impact on the former's flows in presence of Trade facilitation provisions. At the contrary, when Regional Trade Agreements do not contain Trade Facilitation provisions, the trade effect is stronger for final goods. According to the lecture, Trade Facilitation provisions have been effective in boosting trade without diversion effect. In that sense, it appears as a desirable policy option to complement Free trade Agreements in order to counteract declining trend in global trade. Finally, the presentation turned to the determinants of Regional Trade Agreements by assessing the importance of socio-political linkages .Taking the specific example of the Asian-pacific region, professor Innwon Park called for closer political and cultural integration in order to benefit more from Regional Trade Agreements.



Source: Neufeld, Nora (2014), "Trade Facilitation Provisions in Regional Trade Agreements: Traits and Trends," *Staff Working Paper* ERSD-2014-01, Economic Research and Statistics Division, World Trade Organization.

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To conclude, participants asked some questions and made remarks according to the presentations. The possible enlargement of the global value chain process to emerging economies, which are not already integrate (Sub-Saharan Africa, South America, South Asia), could be a mean to benefit once more from vertical specialization according to Masahiro Kawai. This argument is in line with Bernard Hoeckman's comment about the potential of Africa. However, Sébastien Jean pointed-up that these possibilities will not find equivalent gains compared to China's integration in GVC. Productivity gains through GVC are faltering because of governments becoming aware of the cost of such organization and a willingness from them to control GVC appears progressively. Moreover, the future expansion of the 3D printing, which has not been addressed during the session, will allocate goods around the world without creating trade at all, as reported by Joseph Francois.

Other factors have been tackled as possible ways to enhance international exchanges. The cyclical factors have been underestimated in the analysis according to Bernard Heckman, for whom investment could be an important part of the story. In that sense, trade flows may recover their pre-crisis growth in the future. He further highlighted the persistence of trade cost nowadays, letting professor Innwon Park insist on the need for a better quantification of them. Hence, speakers discussed the importance of improving the quality of infrastructures, business climate and regulatory coherence.