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## Trade and Investment for Development

In the past few decades, global trade flows have grown rapidly, enabled by technological progress (particularly in transport and communications) and the liberalization of the trading environment – including economic policies that eliminated restrictions on global trade, capital, and financial flows; rising trade in services; the expanding nature of global value chains (GVCs); and the integration of developing economies and regions into the rule-based international trade system. These developments have transformed the structure of international trade, making it more complex.

At the same time, such changes in the nature of trade require comparable changes in the accompanying regulatory environment. As the WTO becomes less responsive to new trends in global production networks and the regulatory issues needing to be addressed, its central position as an arbiter of trade relations is eroding. <sup>2</sup>

World trade has been slower than expected over the past few years; simultaneously there has been a low level of global investment, despite ample capital flows. Moreover, these trends offer little prospect for an expansion in global trade over the short term. While the decline can largely be attributed to recent economic instability and uncertainty in both developed and developing countries, an equally compelling explanation is an accumulation of trade-restrictive measures. Despite a deceleration in the rate of implementation of new protectionist measures on a quarterly basis, they continue in absolute

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<sup>1</sup> The authors thank Bozkurt Aran and Ussal Sahbaz for their contributions.

<sup>2</sup> Richard Baldwin, “21st Century Regionalism: Filling the gap between 21st century trade and 20th century trade rules”, WTO Staff Working Paper ERSD-2011-08.

terms.<sup>3</sup> Moreover, it is argued that trade distortions implemented by G20 members are understated in official reports from the international organizations.<sup>4</sup>

The world economy is facing a fifth consecutive year of decline in global growth. In 2008 the total level of foreign direct investment (FDI) decreased by a quarter following the eruption of the sovereign debt crisis – and it has yet to fully recover.<sup>5</sup>

Global trade is strongly interlinked to investment flows as well as the movement of people and knowledge; these interlinkages lie at the heart of fragmented production processes, and of regional and global value chains – while also offering new possibilities for achieving developmental targets.<sup>6</sup>

The T20's 2015 discussions around trade and investment converged on issues seen as vital to the global trade agenda: the potential benefits of rising investments; reducing protectionism; and improving participation of small and medium-sized enterprises (SMEs) and Low Income Developing Countries (LIDCs) in global value chains.

On multilateral and regional trade and investment rules, the T20:

- Reexamined rising trends in trade protectionism through non-tariff barriers
- Proposed the establishment of a G20 trade and investment working group to examine trade and investment policies in G20 countries and to make recommendations to the G20 leaders on the impact of trade and investment rules on growth, jobs, and sustainable development
- Considered the role of regional trade agreements (RTAs) and mega-deals as important platforms for improving rules and standards, as well as providing novel good practices for the complex trading system of today
- Emphasized the role of RTAs in breaking artificial divisions between trade and investment
- Reiterated the need for multilateral investment rules that can guide initiatives on economic transformation and integration of developing countries into global value chains
- Underlined that PTAs should complement the multilateral structure, without downgrading its spirit and functions.
- Emphasized a balanced approach between investor–state dispute settlement

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<sup>3</sup> The most recent WTO *Report on G-20 Trade Measures*, 12 June 2015, is available at:

[https://www.wto.org/english/news\\_e/news15\\_e/g20\\_wto\\_report\\_june15\\_e.pdf](https://www.wto.org/english/news_e/news15_e/g20_wto_report_june15_e.pdf)

<sup>4</sup> Simon Evenett, *The G-20 and Protectionism—A July 2015 Update*,

<http://www.t20turkey.org/images/pdf/The%20G-20%20and%20Protectionism%20-%20A%20July%202015%20Update.pdf>.

<sup>5</sup> “FDI gains momentum in second half of 2014”, *FDI in Figures*, OECD, April 2015,

<http://www.oecd.org/daf/inv/investment-policy/FDI-in-Figures-April-2015.pdf>.

<sup>6</sup> Ram Upendra Das, “Trade and Investment Agenda under G20: Some Issues and Proposed G 20 Actions”, Policy Note submitted to the T20 Turkey Kick-off Event, Istanbul, February 10-11, 2015.

Emphasizing the link between investment, technological transfer, and sustainable development, the T20:

- Drew attention to the potential adverse effects of new multilateral and regional trade and investment rules on technology transfer to developing countries
- Provided strategies to promote global technology diffusion to help address global challenges including climate change

On improving SME access to global value chains, especially those in developing countries, the T20:

- Underlined the implementation of the WTO Trade Facilitation Agreement
- Promoted new multilateral trade rules for SMEs and the digitization of customs procedures
- Emphasized the need to support SMEs to ensure their compliance with global standards in quality in labor practices, as well as in social and environmental issues

## **1. Rising protectionism and coping with non-tariff barriers**

Trade is unfortunately sluggish and not responsive to GDP growth. There are cyclical and structural factors driving this phenomenon; some important factors include rising protectionism and the sluggishness of liberalization initiatives on a multilateral basis.

Trade data reveal the extent of the protectionist tide as countries turn inwards: the biggest distortions to trade derive from non-tariff barriers – mainly from technical barriers to trade, localization barriers, and artificial export incentives. The share of G20 exports potentially affected by trade distortions is rising relentlessly.<sup>7</sup> Significantly, the bulk of trade restrictive measures is applied by G20 members themselves.

Nevertheless, countries' anticipation of the adverse effects of protectionism on global value chains and the uncertainty it poses for market access could discourage countries employing new trade measures.<sup>8</sup>

In this regard, the G20's consideration of non-tariff barriers was insufficient in the Brisbane communiqué, and robust attention remains necessary to roll back protectionist measures.

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<sup>7</sup> Independent study by Global Trade Alert (GTA) documents almost 7,000 governmental measures since the first G20 Leaders Summit. Almost 75% of G20 exports face at least one new trade distortion, according to GTA figures. See *The Global Trade Disorder – The 16th GTA Report*, CEPR Press, 2014, available at: <http://www.globaltradealert.org/sites/default/files/GTA16.pdf>.

<sup>8</sup> World Trade Report 2014: *Trade and development: recent trends and the role of the WTO*, Geneva, WTO.

POLICY OPTION:

*The G20 could establish a “G20 trade and investment working group” to examine policies in G20 countries; to assess the impact of trade restrictive measures based on reports by IOs and other independent bodies; and to make recommendations to the G20 leaders on the impact of trade and investment policies on growth, jobs, and sustainable development.*

## **2. The WTO-PTA nexus**

Following its establishment, WTO’s remit has encompassed several functions including facilitating the administration of trade agreements, providing technical assistance to developing countries, and cooperating with other international organizations. It did well in many of these areas and was even considered remarkable in settling trade disputes among its members. However, it has proved itself to be ineffective at fulfilling its most vital task – that of providing a forum for trade negotiations and improving trade rules.

T20 considers that the world is changing rapidly, but its institutions do not always adapt in the same way and at the same speed.

WTO multilateralism has produced no concrete steps towards liberalization during the past two decades – with some minor exceptions. The stalemate in the WTO Doha Round has fostered an increased focus on the negotiation of preferential trade agreements (PTAs), including the so-called “mega-regionals”. Most of these agreements go beyond the WTO’s remit in terms of coverage, presenting a new platform to change world trade rules and bring further liberalization.

POLICY POSITION:

*The G20 should acknowledge WTO’s constitutional role that it has carried out in binding commitments, flexibilities, technical assistance, and settling disputes.*

In global summits, leaders repeatedly call for the completion of the Doha Round. Some T20 participants argued that this is not feasible within the confines of a slow multilateral process via a single undertaking, and without giving up the rule of “consensus”. The MC10 meeting of the WTO in December presents an opportunity to revisit the failures of Doha Round negotiations.

The negotiation of mega-regional deals such as the Trans-Pacific Partnership (TPP) and Transatlantic Trade and Investment Partnership (TTIP) presages the start of a new era in the global trading system. Despite this, a positive correlation between PTAs and their influential role in further opening markets

and setting universally acceptable rules has not been empirically tested in a persuasive way. This requires further investigation.

PTAs are expected by many to deliver best practice in areas that have not been appropriately handled at the multilateral level; such areas include standards, investment, and regulatory issues (i.e. WTO+ and WTO-X matters). However, provisions in PTAs are likely to have welfare-enhancing effects only for participating members, without a direct benefit to third parties unless they conform to standards and norms through indirect spillover effects. In most cases, deeper harmonization of standards requires trust and convergence of objectives among negotiators, as well as capacity, especially in the case of developing countries.<sup>9</sup> Therefore, the success of PTAs depends on how they counter challenges – that is, to reduce the risk of discriminatory impact; provide less-stringent regulatory measures for third countries; bring flexible mechanisms to boost spillover effects; and to make the system more open and trustworthy for all.<sup>10</sup>

While PTAs and mega-regionals are important platforms for improving rules for the complex trading system of today, these should complement the multilateral structure, without downgrading its spirit and functions.

#### POLICY POSITION:

*The G20 countries should focus on how multilateralism can be reinvigorated and co-exist with preferential schemes.*

### **3. Links between trade and investment**

T20 discussions emphasized a global trade agenda that connects the analysis of trade and investment for the purpose of maximizing their benefits for developing countries.<sup>11</sup>

So far, the WTO has been unable to respond effectively to the exigency of the new trends in world trade that underscore a strong link between investment and trade. The T20 emphasized the need for a well-designed multilateral investment discipline that harmonizes the multiplicity of domestic policies. There are over 3,000 International Investment Agreements (IIAs)<sup>12</sup> addressing cross-border investment, a

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<sup>9</sup> Jean-Christophe Maur and Ben Shepherd, “Preferential agreements, regional cooperation and standards”, WTO, [https://www.wto.org/english/res\\_e/publications\\_e/wtr11\\_forum\\_e/wtr11\\_22feb11\\_e.htm](https://www.wto.org/english/res_e/publications_e/wtr11_forum_e/wtr11_22feb11_e.htm).

<sup>10</sup> S. Akman, S. Evenett, and P. Low (2015), *Catalyst? TTIP's Impact on the Rest*, CEPR and TEPAV publication (VoxEU.org book), available at: [http://www.tepav.org.tr/upload/files/1432112973-6.Catalyst\\_TTIP\\_s\\_Impact\\_on\\_the\\_Rest.pdf](http://www.tepav.org.tr/upload/files/1432112973-6.Catalyst_TTIP_s_Impact_on_the_Rest.pdf).

<sup>11</sup> Discussions at the T20 Turkey Kick-off Event, Istanbul, 10–11 February 2015.

<sup>12</sup> See UNCTAD Investment Policy Hub, <http://investmentpolicyhub.unctad.org/IIA>.

situation that amplifies fragmentation and complexity, which in turn increases transaction costs and leaves gaps in coverage.<sup>13</sup>

**POLICY OPTION:**

*The relevant IOs such as OECD and UNCTAD should work with the WTO towards establishing a template multilateral investment agreement for global adoption. The text would include at least the generic elements that a “good practice” investment agreement should contain.<sup>14</sup>*

Some discussion participants drew attention to the need for better understanding of different emerging models that may have the potential to set the tone for a future multilateral investment regime: for instance, mega-regional trade agreements such as TTIP and TPP, by emphasizing non-discriminatory investment policies and assurance of basic rule-of-law protections, aim to broaden existing rules and principles and establish new and stronger international standards.

Nevertheless, most countries – both within and outside the G20 – will be obliged to comply with rules that they have not contributed to making if such mega-regional deals become “game-changers”. Despite this, a need for investment may induce individual countries to adapt to newly formed standards by engaging in a program of serious domestic reforms.

The US-China bilateral investment treaty may serve to establish a conducive platform by setting new international standards that take into account the developmental needs of emerging markets. Moreover, notwithstanding their differences, mega regionals like TTIP, TPP, and the Regional Comprehensive Economic Partnership (RCEP) may help to hasten domestic reforms in countries whether or not they are included in these agreements.<sup>15</sup>

#### **4. Dispute settlement between investors and states**

On the issue of dispute settlement between investors and states, participants underlined that sovereign rights of states need to be protected. As part of the TTIP negotiations between the United States and the European Union, the former proposed an investor-state dispute settlement (ISDS) mechanism, a form of extra-judicial arbitration scheme. This was not welcomed by several members of the European Parliament, who expressed concerns that ISDS would lead to situations in which business interests

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<sup>13</sup> Hongying Wang, “Toward A Global Investment Governance Framework: An Opportunity for the Chinese Presidency of the G20”, 2015; see T20 blogs <http://www.t20turkey.org/eng/pages/blog/b37.html>.

<sup>14</sup> Rathin Roy, “Trade, Employment and Investment: An integrated G20 Agenda”, paper submitted to the T20 Turkey Kick-off Event, Istanbul, February 10–11, 2015.

<sup>15</sup> Consultative Meeting. TEPAV-Gateway House, “Turkey, India and the G20,” October 2015.

triumphed over human rights.<sup>16</sup> The final proposal by the European Commission is to “include modern provisions in bilateral agreements, putting stronger emphasis on the right of the state to regulate” and the establishment of a new and transparent system for resolving disputes between investors and states – the Investment Court System – which would function like a traditional court composed of qualified judges, similarly to the WTO Appellate Body.<sup>17</sup>

On issues of investor-state disputes, T20 discussions in Mumbai asserted that sovereign rights need to be protected.

**POLICY OPTION:**

*The G20 should establish a working group that includes public and private sector actors and relevant IOs to explore the possibility of a WTO-like “dispute settlement mechanism” on the investment terrain that could be voluntarily adopted by individual countries (with G20 members taking the lead).<sup>18</sup>*

## **5. The link between investment, technology diffusion and sustainable development**

T20 discussions emphasized a global trade agenda that connects analysis of trade and investment for the purpose of maximizing their benefits for developing countries.<sup>19</sup> Foreign direct investment flows can help developing countries upgrade their innovative capacity. While discussions emphasized the need for a strong, transparent, and predictable multilateral investment framework, it is equally important to take into account developing countries’ needs. Despite significant convergence between emerging and advanced economies, global imbalances remain in terms of innovation capabilities, with the former lagging considerably behind the advanced economies. Such imbalances and diverging concerns between developed and emerging economies likely also stand in the way of sustainable growth in the global economy.

**POLICY OPTION:**

*The G20 could establish a study group with the WTO to analyze how interlinkages between trade in goods, services, and investment can enhance the development process.<sup>20</sup>*

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<sup>16</sup> <http://www.euractiv.com/sections/global-europe/european-parliament-backs-ttip-rejects-isds-316142>.

<sup>17</sup> *Trade for all: Towards more responsible trade and investment policy*, European Union, 2015; the European Commission’s new trade strategy document available at:

[http://trade.ec.europa.eu/doclib/docs/2015/october/tradoc\\_153846.pdf](http://trade.ec.europa.eu/doclib/docs/2015/october/tradoc_153846.pdf).

<sup>18</sup> Recommendation made by Roy, 2015 modified: Rathin Roy, “Trade, Employment and Investment: An integrated G20 Agenda”, presented at the T20 Turkey Kick-off Event, Istanbul, 10–11 February 2015.

<sup>19</sup> Discussions at the T20 Turkey Kick-off Event, Istanbul, February, 10–11 2015.

<sup>20</sup> Ram Upendra Das, “Trade and Investment Agenda under G20: Some Issues and Proposed G 20 Actions”, Policy Note submitted to the T20 Turkey Kick-off Event, Istanbul, February 10–11, 2015.

New multilateral trade rules may have potential adverse effects on technology transfer to developing countries. For instance, the Agreement on Trade-Related Investment Measures (TRIMs) prohibits many “performance requirements” – local content and export performance requirements, joint-venture requirements, technology transfer clauses – increasingly employed by governments in developing countries as a condition for market access. Under the WTO’s TRIPS Agreement, agreed rules on intellectual property rights narrow the opportunity for technology development in developing countries; similarly, TTIP could further tighten protection by expanding the scope and duration of patents to the detriment of developing countries. For instance, Article 66.2 of the TRIPS Agreement that includes provision to facilitate technology transfer to least developed countries has not been made specific and effective.

POLICY OPTIONS: <sup>21</sup>

*The G20 should promote the strengthening of provisions for transfer of technology, especially environmental technologies, to developing and least-developed countries under Art. 66.2 of TRIPS Agreement of WTO.*

*The G20 should promote extending the public health waiver from TRIPS provisions for critical environmentally sound technologies, especially for developing countries.*

*The WTO should review the provisions of TRIMs from the perspective of technology absorption and adaptation.*

Similarly, mega-regional trade agreements such as TTIP and TPP aim to broaden existing rules and principles and establish new and stronger international standards (see discussion above). The TPP’s provisions that were announced last week include extensions of restrictive intellectual property laws and patents for innovations such as in biotechnology. Most countries – both within and outside the G20 – will be obliged to comply with rules that they have not contributed to making if such mega-regional deals become “game-changers”. Most significantly, new trade rules have the potential to adversely affect technology transfer to developing countries. <sup>22</sup>

Moreover, it is important to encourage international collaboration around advanced technologies as part of the effort to deploy technology to tackle global economic problems. New technologies provide

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<sup>21</sup> Recommendations by Kumar, 2015 have been modified; Nagesh Kumar, “Sustainable Development Goals and Means of Implementation: Facilitating Access to Green Technologies by Developing Countries”, presented at the T20 Turkey Kick-off Event, Istanbul, February 10–11, 2015).

<sup>22</sup> Discussions at the T20 Turkey Kick-off Event, Istanbul, February 10–11, 2015; Think20 Workshop: A Stocktaking on Turkish Presidency, Izmir, June 13, 2015; and Consultative Meeting, TEPAV-Gateway House, “Turkey, India and the G20,” October 2015.

solutions to global challenges such as food safety and security, climate change adaptation, and mitigation, as well as healthcare. G20 governments can work towards designing cooperation models for joint R&D initiatives. One example of such public-private partnership for bilateral cooperation is the BIRD Foundation between Israel and the United States; BIRD was established by the governments of the two countries to generate mutually beneficial cooperation between technology-driven firms in the two countries.

**POLICY OPTION:**

*The G20 should establish a science, technology, and innovation network to explore new public-private partnership models and public procurement schemes, to harmonize domestic regulatory standards for technology transfer, and to facilitate global diffusion of new technologies – nanotechnology and biotechnology – that would help address global challenges including decreasing carbon emission levels.*<sup>23</sup>

T20 discussions also drew attention to the need for South-South knowledge exchange to develop products and technologies designed to address common challenges faced by these countries. As an example, frugal engineering capabilities in India have led to the development of affordable generic medicine. South-South flow of knowledge and joint R&D initiatives can help develop innovative sustainable technological solutions such as low-carbon products.<sup>24</sup>

**POLICY OPTION:**

*G20 emerging markets could lead South-South and triangular partnerships for joint R&D for development and sharing of frugal and low-carbon solutions for common challenges faced by developing countries.*<sup>25</sup>

## **6. Improving SMEs and LIDCs' access to GVCs**

Information and communication technologies and widespread transport links have enabled firms to divide the production process into its various components across different parts of the world. Global value chains provide SMEs – especially those in developing economies – with an opportunity to access global production chains and improve their capabilities.

Improving access for SMEs to global value chains requires an appropriate policy framework. This is complex and ranges across multilateral trade and investment rules to cross-country dissemination of supply chain management services through liberalization of service industries; it also encompasses

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<sup>23</sup> Selin Arslanhan, "Science, Technology and Innovation in G20 Countries", TEPAV, 2015.

<sup>24</sup> Kumar, 2015.

<sup>25</sup> Ibid.

financial system development to ease the cash constraints on firms. Equally important is the need to give support to SMEs to ensure their compliance with global standards relating to quality labor practices and social and environmental protection.<sup>26</sup> In terms of exports, high trade costs disproportionately affect SMEs, as they suffer more from administrative and border-related burdens than larger firms.<sup>27</sup>

Yet, the majority of modern trade regulation is geared towards large firms, while LIDCs rely heavily on SMEs.<sup>28</sup> The WTO Trade Facilitation Agreement that has not been implemented aims to boost SME participation in trade by shortening the time to export. The longer time to export discourages SMEs, and exports are dominated by larger firms.<sup>29</sup>

#### POLICY RECOMMENDATION:

*The G20 countries should take the lead towards the implementation of the WTO Trade Facilitation Agreement by ratifying the agreement.*

#### POLICY OPTIONS:

*The G20 could facilitate SMEs' access to GVCs by promoting new rules that allow shipments under set thresholds to forego customs clearance when the amount of duty is less than the administrative cost to process them.*

*The G20 could consider establishing a target for the digitization of customs procedures for G20 countries for the coming five years.<sup>30</sup>*

*The G20 could work together with the World SME Forum to support SMEs to ensure their compliance with global standards in quality in labor practices, as well as in social and environmental issues, to enable their access to and/or upgrade their position in GVCs.*

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<sup>26</sup> *Aid for Trade at a Glance 2015: Reducing Trade Costs for Inclusive, Sustainable Growth*, OECD/WTO, OECD Publishing, Paris, 2015.

<sup>27</sup> WTO Report 2015, supra p.91.

<sup>28</sup> *Business Access to Global Value Chains and Financing SMEs*, OECD/BIAC and B20 Turkey, June 20, 2015, <http://www.t20turkey.org/eng/pages/research/r23.html>.

<sup>29</sup> *WTO World Trade Report 2015 – Speeding up trade: benefits and challenges of implementing WTO Trade Facilitation Agreement*, Geneva, WTO, 2015.

<sup>30</sup> Kati Suominen, "Fueling the Online Trade Revolution: A New Customs Security Framework to Secure and Facilitate Small Business E-commerce", A Report of the CSIS Europe Program, April 2015.