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Liberalize, Sanitize, Digitize: Three Urgent Trade Policy Priorities in a Pandemic Age

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Within a few short weeks, a microbe has accomplished what multiple wars (hot and cold) failed to achieve over the past 75 years: massive simultaneous disruptions of international and local supply chains. Initial supply disruptions from the illness in China quickly spread, like the virus itself, across the Silk Road into Europe and across the Pacific Ocean into the United States. Mobility restrictions that hopefully will slow the spread of the disease also trigger simultaneous demand, supply, and liquidity shocks, with the near-shuttering of most Group of 7 economies in addition to that of China. Global supply chains and the structure of international economic relations may never be the same again.

While unprecedented emergency measures have been implemented globally in monetary policy, fiscal policy, and financial regulation, measures regarding trade policy have been noticeably absent or have demonstrated retrograde tendencies. Throughout March 2020, export bans on medical equipment, pharmaceuticals, and personal protective gear proliferated. A few nations have begun erecting export bans on agricultural commodities.

Policymakers operating at the base of Maslow's hierarchy of needs understandably seek to keep their countries safe. However, increasing barriers to trade during this vulnerable period is likely to backfire. Rather than delivering security of supply for domestic populations, these barriers will trigger a range of inefficient reactions (such as panic-buying and hoarding), make it difficult for domestic manufacturers to acquire the supplies they need, and increase prices for buyers in a worsening economy. The novel coronavirus impacts all humans; the most efficient solution is to collaborate across borders in order to address shared challenges and decrease frictions that increase costs for struggling economies globally.

Bold action now will enable the World Trade Organization (WTO) and the global trading system to be part of the economic solution, once people emerge from social distancing and the supply chain attempts to restart. Policymakers interested in keeping trade lines open and preparing the international trading system for a post-pandemic world must take three steps immediately:

1. Eliminate import tariffs, at least temporarily.
2. Sanitize the supply chain.
3. Digitize more of the supply chain.

THE POLICY RESPONSE TO COVID-19

Policymakers around the world during March 2020 took swift and significant action to alleviate the growing economic burden associated with simultaneous supply and demand shocks across advanced economies. Most of the moves were unprecedented in size, scale, scope, and range:

- Central banks created massive liquidity support mechanisms.
- The Federal Reserve implemented comprehensive dollar-swap arrangements with partner central banks, including daily settlement with some partners.
- Fiscal policymakers deployed targeted financial lifelines for the sectors hit hardest by the pandemic's first wave (e.g., healthcare providers, airlines, small businesses). Broader fiscal support measures (direct payments to citizens, suspension of the Stability and Growth Pact in Europe) have also been implemented.
- Tax collection has been suspended temporarily for both individuals and corporations in multiple countries, including the United States.
- Financial regulators temporarily relaxed or suspended a broad range of regulatory capital, accounting, and regulatory reporting requirements in an effort to direct liquidity to borrowers and in order to avoid automatic regulatory restrictions on banks.

Trade policy, on the other hand, has been characterized by an increase in barriers to trade and relative inaction by policymakers. Responses from the Group of 20 (G20) and the WTO have been cautious. One recent speech by a WTO official indicates accurately that individual WTO members remain free to decrease tariffs or to increase trade restrictions for the purpose of protecting the health of domestic preparations.[1] While this is technically true, it does not generate leadership to decrease trade barriers. After more than 50 nations worldwide created import bans on medical equipment and pharmaceuticals, the WTO requested that countries file reports with the WTO regarding pandemic-related trade measures.[2]

These measures are insufficient. Policymakers in the trade arena must urgently match the scale and creativity of their colleagues in the central banking, fiscal policy, and financial regulation arenas.

While policymakers globally are attempting to provide as much support and liquidity as possible to the economy, WTO policymakers at the supply-chain epicenter of the economic crisis caused by the pandemic are failing to provide the bold thinking and coordinated international action needed now. Nations are not waiting for policymakers in Geneva, but their actions generate an uneven playing field.

If the WTO cannot provide a forum for decisive, constructive, joint action that preserves trade-related jobs and revenue sources, its relevance and effectiveness will remain under attack, as will gains to multilateralism in trade.

BACKGROUND: A BAD TIME FOR A PANDEMIC

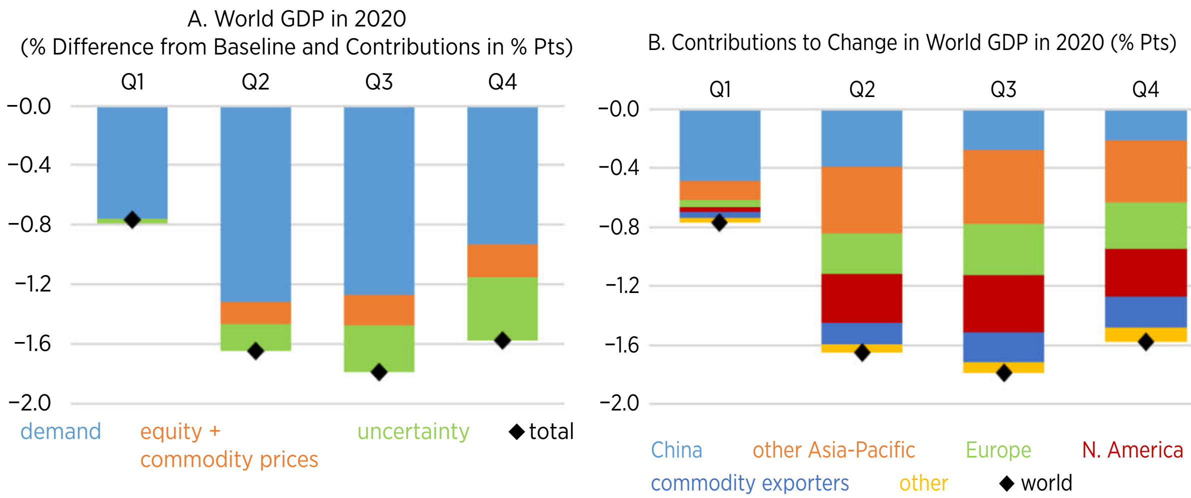
The global trading system was vulnerable when illness struck in China at the end of 2019. Backlash against globalization and cross-border trade has been growing steadily since the late 1990s. Populist politicians have claimed foreign competition as the reason for economic malaise at home. Left-leaning advocates have blamed globalization for generating disparities in wealth and income. Bilateral trade wars have become common mechanisms for pursuing managed trade policies. Environmental activists keen to reduce greenhouse gas emissions have sought to promote localized supply chains at the expense of imported goods. Cash-strapped sovereigns increasingly seek to impose taxes on digital goods produced abroad. Finally, technological advances have been transforming economies into increasingly distributed structures with complicated supply chains. Individuals connected electronically across borders increasingly view the centralized, sovereign-state, international-organization structures created after World War II as anachronistic.[3]

The WTO thus faces significant challenges when faced with a pandemic whose only real mitigation measure at present is the antithesis of global trade: mobility restrictions.

The full scope of the pandemic crisis remains unknown. Much depends on whether and how governments and medical teams can slow the loss of life within advanced economies. The longer the pandemic lasts, the greater the economic dislocation will be. Substantial, perhaps permanent, shifts in demand may occur if individuals and companies cannot physically go to work or go shopping for multiple weeks or even a full economic quarter. The potential exists for an existential challenge to the global-supply-chain structure that has to date delivered significant increases in economic growth and helped improve living standards around the world.

On March 2, 2020, the Organisation for Economic Co-operation and Development (OECD) estimated that a domino-like progress of COVID-19 into the developed world from China would generate a dramatic adverse impact on the global economy (see figure 1).[4]

Figure 1. Potential Economic Impact of Coronavirus Outbreak as a Percentage of World GDP



Notes: This figure is modeled after "Figure 8. Domino scenario: potential economic impact of the coronavirus outbreak" in OECD, *Coronavirus: The World Economy at Risk*, March 2, 2020, https://www.oecd.org/berlin/publikationen/Interim-Economic-Assessment-2-March-2020.pdf. Panel A shows the contributions to the decline in the level of GDP from the different elements of the shock. Panel B shows the contributions of different regions and countries to the decline in global GDP. Commodity exporters are Argentina, Brazil, Chile, Russia, South Africa, and other non-OECD oil-producing economies.
Source: OECD calculations using the NiGEM global macroeconomic model.

These estimates were published one week before Italy locked down its economy. They may yet be revised downward since the pandemic has not yet peaked globally.

The risk exists that international commerce may never go back to normal:

- Small businesses caught short owing to disruptions from far-flung suppliers may choose to diversify supply chains by finding more local vendors.
- Extended pandemic-related mobility restrictions can create perceptions that foreign goods are sources of pathogens that can survive on surfaces for more than a week.
- Policymakers are already pivoting toward viewing certain medical equipment as effectively part of the nation's critical infrastructure that requires domestic production capabilities.
- Inability to source components closer to home will likely increase pricing and introduce inefficient frictions into production processes.
- Small exporters around the world will suffer as external markets become closed to them.

Great dislocations can be wrenching. But they also create opportunities for innovation as entrenched ways of doing things disappear. Rather than attempt to maintain the existing system, policymakers should forge new approaches now in order to preserve the scaffolding of the global trading system.

THREE NECESSARY POLICY SHIFTS

Policymakers should take three steps to preserve the integrity of global commerce for a post-pandemic world. These steps should be implemented immediately, before the pandemic peaks, so that goods shipments can continue to flow.

1. Temporarily Decrease All Tariffs to Zero

With a significant percentage of the global population ill, out of work, or both, trade policy must mobilize to deliver to consumers the same level of support that fiscal policy, monetary policy, and financial regulation are delivering: short-term decreases in the direct and indirect taxes that govern economic interactions.

The economic crisis generated by the pandemic will be deep and unprecedented. Extraordinary central bank liquidity, fiscal stimulus, and temporary deregulation in advanced economies during March 2020 have mostly aimed to create a three- to four-month bridge for economies hobbled by COVID-19. But no comparable dramatic action has been taken regarding tariffs. Shortages and phytosanitary standards will likely increase the cost of goods crossing borders throughout 2020. Food insecurity and incentives to localize supply chains will impose additional trade costs just when exporters most need revenue and importers most need access to supplies.

Some small tariff reductions have begun, both domestically and internationally:

- In February 2020, China unilaterally cut $75 billion in tariffs on imports from the United States.[5]
- In March 2020, the United States proposed to cut or eliminate tariffs on a range of Chinese goods.[6]
- The United Kingdom has waived all tariffs on all medical equipment imports from any country until July 31, 2020.[7]
- New Zealand has led a small group of nations (including Canada and Singapore) to pledge that they will remove "any existing trade restrictive measures on essential goods, especially medical supplies at this time" in order to preserve "the viability and integrity of supply chains globally."[8] The following day, the WTO issued a rare joint statement with the United Nations Conference on Trade and Development and the World Health Organization pleading with nations to refrain from disrupting the food supply chain with nontariff barriers to trade, such as border delays for food containers and restrictions on the mobility of agriculture and food industry workers.[9]
- While the G20 Trade Ministerial Statement, at the conclusion of the G20 March 31 meeting, did pledge to maintain free and open trade policies, the statement never once used the

word “tariff” or indicated that members would decrease tariffs in unison even for medical goods or agriculture and food chain supplies.[10]

- Today, the European Union temporarily waived all import tariffs and value-added taxes on imported medical equipment until July 31, 2020.[11] It is a generous waiver, operating retroactively from January 30, 2020, but only for goods that will be distributed free of charge for disaster-relief purposes. In addition to providing immediate price reductions on life-saving equipment, the waiver effective provides companies with a small tax rebate or credit for previously paid tariffs and value-added taxes. Extensions and expansions are possible if the situation worsens by summer, although it is too soon to identify with precision the evolution of this measure.

These measures do not go far enough. Moreover, individual bilateral tariff reductions single out specific countries and sectors for special treatment and thus indirectly impose burdens on other countries and sectors. The supply-chain damage impacts the entire globe, so tariff reductions should be similarly broad.

The solution is that WTO members should jointly decrease tariffs to zero immediately for all goods in order to eliminate unnecessary and costly frictions and to maximize the relief to companies and consumers impacted by the pandemic. Treating all products from all nations in a uniform manner would also ensure that negotiations on the details do not drag on for months.

Acting together in a decisive manner could reinvigorate a sense of purpose and credibility that the WTO needs at this juncture. It would deliver a vote of confidence that trade-based growth models are welfare enhancing. It would position the WTO as an equal contributing partner in global economic stabilization with counterparts at finance ministries and central banks.

Tariff decreases need not be permanent. Financial regulation relaxations and rule suspensions have been implemented with clear sunset dates. The same could apply to tariff structures.

In a perfect world, cross-border trade would occur fully free of tariffs. However, we do not live in a perfect world. Sovereigns earn valuable revenue from tariffs. Trade negotiators’ incentive to reach a zero-tariff state provides them with the opportunity to open markets and increase ties with trading partners. But in this extraordinary situation, the marginal fiscal benefit associated with import tariffs is small to negligible if transaction volumes and global growth rates drop precipitously. Conversely, decreasing tariff-related frictions and costs could help keep trade lanes open at a time when they are most needed.

2. Sanitize the Supply Chain

Recent research from the US Centers for Disease Control and Prevention indicates that the novel coronavirus can last on hard surfaces for up to 17 days.[12] This means that one infected person involved in the shipping process can contaminate others who are thousands of miles away with respect to air shipments and at least some transatlantic shipments. Port authorities are beginning to impose two-week quarantines on freight arrivals as a consequence.

Extending quarantines for shipments, while understandable, is not a sustainable solution. Limited storage space exists on docks and at airports. Agricultural goods can degrade quickly. Merchants seeking to sell goods will incur opportunity costs as items sit idle during quarantine. Food shortages owing to disrupted global supply chains will only intensify the ongoing health and economic crises.

Currently, nations impose a range of phytosanitary standards designed to keep dangerous pathogens outside their borders. Article 20 of the General Agreement on Tariffs and Trade permits such measures if they are nondiscriminatory and are not used as an alternative form of protectionism. The parallel Sanitary and Phytosanitary Protection Agreement (SPS Agreement) permits temporary precautionary measures,[13] but regulatory changes at the national level cannot be implemented without advance notice and full transparency regarding what is expected of importers. Some of these standards have become synonymous with nontariff barriers when trading partners disagree on whether the standards in question are scientifically necessary. Collective action to craft common minimum standards regarding antiviral measures would minimize potential protectionist tendencies while providing confidence in the security of the supply chain for treatment of disease.

In a post-pandemic world, disputes could easily arise if trading partners feared that an exporting country were continuing to experience high levels of COVID-19 infection. Section 6 of the SPS Agreement specifically requires exporters to comply with “appropriate criteria or guidelines . . . developed by the relevant international organizations” when “assessing the sanitary or phytosanitary characteristic of a region.”[14] Nations with a problematic track record regarding data and transparency could easily see difficulty in resuming their traditional exporting role.

After the September 11, 2001, terrorist attacks, ports of entry first in the United States and then globally initiated a series of changes to increase cargo security. US Department of Agriculture materials indicate that a broad range of fumigation options already exists in the United States.[15] Ports of entry with such fumigation facilities should accelerate and expand efforts to incorporate antiviral agents.

However, the range of existing fumigation standards and mechanisms achieves varying degrees of success. Moreover, fumigation can create additional and unacceptable health risks for dock and freight workers. Recent research from the National Institutes of Health in the United States indicates that “between 10% and 20% of all containers arriving [from] European harbors were shown to contain volatile toxic substances above the exposure limit values . . . [that] occur not only during the fumigation, but also during freight transport (on bulk carriers and other transport vessels), as well as in the logistic lines during loading and unloading."[16]

Immediate efforts by the WTO to coordinate with medical professionals at the World Health Organization and various regional and national centers for disease control would place trade policy professionals in a position to articulate common international antiviral standards for goods in international trade relatively quickly, once the novel coronavirus is better understood. In the interim, the WTO could serve a valuable function by providing a forum for articulating common minimum agreed standards for SPS review processes and triage functions that could separate high-risk imports from low-risk imports.

Immediate action at the global level will help ensure a minimum level of security for the supply chain relevant to the coronavirus pathogen. All nations share the same vulnerability to the coronavirus; they also share a need for each other's imports. Under such circumstances, shared standards would be mutually beneficial without imposing disproportionate burdens on any one nation.

3. Digitize the Supply Chain

Immediate tariff reductions, even temporary ones, should be complemented by efforts to digitize the supply chain. Recent WTO research indicates that tariffs account for only 9 percent of costs in international trade, while paperwork and administrative customs processes (including health, safety, and quarantine measures) can generate a 134 percent de facto tariff on imports.[17]

The best solution is to eliminate unnecessary paperwork and regulatory burdens. This is a familiar issue to trade policy experts. Work has been underway within the multilateral system for quite some time on this issue, with the WTO at the forefront of modernizing and streamlining administrative processes regarding international trade. The 2013 Trade Facilitation Agreement sets important parameters for how to accelerate reductions in administrative costs.[18]

It is time to build on this solid foundation. Inaction creates the risk that the economic gains associated with international trade will dissipate during the pandemic-related slowdown.

Shippers involved in international commerce have been experimenting with blockchain-powered smart contracts and letters of credit over the past few years. Enhanced, increasingly digitized customs procedures are also gaining traction globally. These efforts need to be expanded immediately. Increased visibility regarding transit paths and product tracking can increase the efficiency of government efforts to identify quickly which shipments may pose a health security threat.

Increased digitization is not solely for developed economies. The WTO's Trade Facilitation Agreement Facility (TFAF) provides funding and training for emerging economies to adopt advanced, streamlined processes that enable companies to expand access to global trade and decrease administrative costs. Increased TFAF funding would create a fast way for emerging economies to use smart contracts and blockchain-based customs processes that speed items through customs, even as it would enhance their ability to identify potentially pathogen-laden items.

An increasingly digital supply chain would generate additional benefits with respect to shortages. Items that become scarce can become attractive targets for thieves and counterfeiters, whose activities decrease economic welfare across the value chain. A more digitized supply chain is also a more secure supply chain with fewer vulnerabilities for criminal elements.

CONCLUSION

Trade policymakers have been on the sidelines of the pandemic crisis, even though disrupted supply chains have proved to be a significant transmission mechanism for global economic shock waves from COVID-19. Trade policymakers must take bold action to liberalize, sanitize, and digitize the supply chain immediately in order to support exporters and importers. Failure to act now will only solidify perceptions that the WTO is outmoded and not relevant to the 21st century.

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NOTES

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