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**Realigning international trade
according to the full cost
principle**

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Thanks for those of our contributors who ventured to react to this question:

"While trade tensions grow, WTO predicts a sharp fall in world trade for 2020 and 2021, with strong impacts on developing countries. For decades there used to be an intellectual and political consensus that free-trade contributes to growth and development of all involved. This consensus seems to belong to the past. What kind of international trade, and trade governance, does the world need?"



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EDITORIAL

Realigning international trade according to the full cost principle

For many converging reasons – pandemic, geopolitics, backlash against globalisation, lack of progress in Doha Round negotiations initiated 20 years ago, to name the most important – free trade is today not only in danger but also its benefits are in question. For some, it is clear that policy makers should reshape the free trading world system to care more about safety and self-sufficiency.

The risk, however, is to throw the baby out with the bath water. Indeed, “one thing is tackling a public health emergency, another one is reconsidering free-trade governance.” As recalled below, while “there are elements of trade that are questionable, such as environmental aspects, the evidence shows the huge benefits of liberal trade for rich and poor countries alike”. Another challenge to the liberal trading order stems from the distribution and internal redistribution of trade benefits: “the problems lie with institutions, policies and mentalities, which do not always help to derive social profit from agricultural or industrial productions linked to international trade.”

If the pandemic should not make us ignore the benefits of free trade, it could be the catalyser paving the way for a renewed trade regime. It is not the first time that the free trade paradigm is under pressure. In 1960's the developing world – and its advocates - managed to achieve a partial relinquishment of the sacrosanct reciprocity rule in trade negotiations, in name of development. Since that time, the nature of trade has changed but its distributional effects, especially in relation to development remain ambiguous. Unlike in models of Ricardo and Smith, international trade of today is not so much about comparative costs of finished goods, but rather about corporate absolute costs of very fragmented, intermediate inputs further assembled within global value chains. According to WTO, two thirds of world trade is today value chain related!

The main difference in the world of global value chains is that for many – possibly the majority – of intermediate goods, the buyers, those who are in the chain closer to the final product, have a relatively strong bargaining position towards those who are closer to the raw material end of the chain. Thus, the supplier winning the contract, is the one who delivers the requested quantity at the lowest absolute price, at constant quality. According to some experts, 2-3% difference may make or break the deal. Fearing to lose jobs and export revenues, many developing exporting countries are hesitant to stiffen their labour legislation or increase their tax level. In such situations, the price invoiced is truncated and unjust as it does not cover the effective social (decent work) and environmental

costs. In consequence, international community is called upon to fill the gap by supporting budget deficits and development efforts that local budgets cannot afford. Fair trade organisations – mainly NGO – have spotted the problem long ago.

Today, international trade needs again rebalancing: goods should be traded at full cost, not at truncated cost as it is often the case today. This “full cost principle” has to find urgently its way into trade treaties and practice. The change may reduce slightly the volume of trade, but will – without doubt - make it more just in terms of commutative justice and will internationally increase its distributional effects: “purposefully revised and reinvigorated measures which give overriding priority to the needs of the world’s most deprived.

Virgile Perret & Paul H. Dembinski

“... this issue is a matter of bargaining power ...”

The consensus in question was based on a partial view of David Ricardo's relative cost theorem, which shows that global production increases when each country specializes in the production for which it is relatively best placed. It cannot be inferred that "all involved" benefit from it. **This issue is a matter of bargaining power. It is therefore necessary to rebalance the powers.** To do this, favor multilateral agreements - in preference to bilateral agreements, always unbalanced in favor of the most powerful - and strengthen regional cooperation, not only in economic matters but also in the monetary and military fields.



[Etienne Perrot](#)

“... the evidence shows that trade has helped countries rise out of poverty ...”

I think that the consensus on the benefits of trade is not just intellectual and political, but also empirical as the evidence shows that trade has helped countries rise out of poverty. Of course there are elements of trade that are questionable, such as environmental aspects, but I do not think that one should conclude that trade should be broadly frowned upon. Furthermore, these questions were already present before the Covid pandemic. [...] **The lessons from the Covid are more about the need to have some buffers in economic flows (storage at the various stages of the production chain, diversification of sources) than about trade per se.** At a time where emerging and developing economies will suffer from the pandemic, I think that it is important not to add to the misery by limiting their trading opportunities.



[Cédric Tille](#)

“... international governance should preserve free trade ...”

World trade slump is due to Covid-19 but also to China’s and others’ economic cycle. **International governance should preserve free trade.** There is wide evidence of counter-productive effects of trade wars. There may be business trends to reinforce fragile supply chains or to invert relocation where robotization revolutionizes cost structures. This may have negative effects on development. But free trade had hugely positive effects among European less developed countries, for example. **The problems lie with institutions, policies and mentalities, which do not always help to derive social profit from agricultural or industrial productions linked to international trade. Policies should be reoriented to reduce “stickiness” against change in places affected by relocation, and to support local demand in developing countries.**



[Domingo Sugranyes Bickel](#)

“... a return to the Havana Charter ...”

With the **weakening consensus** on the benefits of free trade (widely proclaimed but less widely serving as the basis for policy in practice) two possibilities are worth considering. **The first would be a return to the Havana Charter (drafted to be the basis for the International Trade Organisation which was abandoned in 1950 in favour of the less ambitious GATT). The rules here, in addition to trade barriers, extended to fair labour standards, restrictive business practices, and the promotion of economic development.** Another simpler alternative might focus on reinforcing national policy space regarding industrial and environmental policy. Revisions here might focus on the National Treatment obligation of the WTO agreements on trade in goods and services, which guarantees equal tax and regulatory standards for domestic and imported production within a country, and the plurilateral Government Procurement Agreement which limits more favourable treatment for local than for foreign suppliers.



[Andrew Cornford](#)

“... balancing tradefreedom and protection of domestic products ...”

The most vulnerable economies (especially the developing countries) and the most vulnerable individuals will face the most severe impact of the lockdown(s). The first and most decisive step to be taken is to stop creating our future having a uniform thinking as a raw material. The public spending should ensure the dignity of all people while the liquidity injections should be constrained by rules of international coordination, fair trade and ecological sustainability. **International trade priorities that can lead the world beyond the beggar-thy-neighbour options: balancing tradefreedom and protection of domestic products, supporting the most vulnerable in the supply chains, preparing international economic pacts that ensure both free trade and resource efficiency at local level.** Fair access to medical products and sanitary material is and has to be a human rights issue.



Christos Tsironis

“... what is lacking is an international fiscal regime ...”

Free-trade is increasingly object of criticism, from the Extreme Right ranging to Extreme Left of the political spectrum worldwide, in light of social inequalities and geopolitical considerations. Currently, the public health emergency related to the Covid-19 pandemic has stressed the necessity for governments to achieve independence in key sectors, bringing new arguments to the “ideologues” of a strong nation-State. However, one thing is tackling a public health emergency, another one is reconsidering free-trade governance. **The current international trade governance, although with some limits, does work: what is lacking is an international fiscal regime that should not tolerate tax havens or countries competing over “pro-business” environments and tax credits. The money so obtained should be devoted to build strong welfare states.**



Valerio Alfonso Bruno

“... measures which give overriding priority to the needs of the world’s most deprived ...”

UNCTAD was founded in 1964 because poor countries knew that “«For he that hath, to him shall be given: and he that hath not, from him shall be taken even that which he hath.»: (Mark 4:25) and amazingly, GATT members agreed! The international trade system was able to agree on a constant if unsteady flow of countermeasures. The pandemic has brought the underlying current back to the surface. **It calls for purposefully revised and reinvigorated measures which give overriding priority to the needs of the world’s most deprived (Brundtland definition of ‘sustainable development’ in French).**



[Edouard Dommen](#)

“... trade is essential to save both lives and livelihoods ...”

Trade is essential to save both lives and livelihoods. There is a strong need to keep trade flowing, both to safeguard the supply of essential products and to send an indication of confidence for the global economy. **In an unprecedented global health crisis, an international collaboration is needed to keep trade flowing.** Some governments are taking measures designed to ensure supply for their own population having the outcome of limiting supply for others. While governments rightly are concerned to protect their own populations, there are consequences on other countries, besides on global efforts to contain the virus and prevent damaging furthermore recurrences that can be severe. But if countries are to avoid these policies, they need to be sure that global markets will indeed supply the needed goods. Transparency and global dialogue and collaboration are essential in constructing the confidence in global supply.



[Archana Sinha](#)

“... free trade is a factor of growth but not the major one ...”

Despite global value chains generate multiple export sales inflating trade statistics, slowdown in global trade is an observable trend starting long before appearance of new protectionism policies and much earlier than the pandemic.

Real trade is strongly influenced by fluctuations of financial markets and currencies market. **Free trade is a factor of growth but not the major one. Inventories and receivables are assets of the firm that need to be financed. One third of world trade is financed by banking sector.**

Trade financing is highly important and must be insured by institutions in a time bank profitability for 2020 has undergone large downward revisions mainly due to expectations of future credit losses and flimsy profitability due to low interest rates.



[Eutimio Tiliacos](#)

LIST OF CONTRIBUTORS

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Paul H. Dembinski is the initiator and Director of the Foundation of the Observatoire de la Finance. In parallel, he is partner and co-founder (with Alain Schoenenberger) of Eco'Diagnostic, an independent economic research institute working for both government and private clients in Switzerland and elsewhere. Paul H. Dembinski is also Professor at the University of Fribourg.



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Domingo Sugranyes Bickel, KCSG. Born 29 April 1945. Spanish national resident in Madrid. Graduated from the University of Fribourg, Switzerland. Secretary General of UNIAPAC (International Christian Union of Business Executives), Brussels, from 1974 to 1981. With MAPFRE international insurance group from 1981, Executive Vice-Chairman until 2008. From 2009 to 2019, Chairman of Vatican-based Foundation Centesimus Annus Pro Pontifice. Knight Commander of the Pontifical Order of Saint Gregory the Great (April 2019)



Eutimio Tiliacos is Secretary General of the Vatican based Centesimus Annus pro Pontifice Foundation whose primary mission is the dissemination of Catholic Social Teaching since 2015. Has previously been in executive positions in several companies operating in the fields of energy, electronics, mechanical industry, transportation, financial services. Since 2009 has also acted as external expert for the European Commission in the satellite Galileo project.



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“FROM VIRUS TO VITAMIN” – JOIN THE DISCUSSION

The Observatoire de la Finance intends to seize this period of pandemic to step back and take a fresh look at our global economic system, dare to ask new questions which the current crisis brings to the fore and propose innovative ways to rebuild a more resilient and sustainable economy and society. In brief, we want to turn the virus into a vitamin for the future.

Our Discussion Board “From Virus to Vitamin” focuses on commenting issues relevant to finance and economy in relations to society, ethics and the environment from a variety of perspectives, of practical experiences and of academic disciplines. It has been designed to share and discuss information and opinions expressed in a short and concise manner.

Contributors ([Discover the list of contributors](#)) are invited to react on a question/issue that is submitted in parallel to a limited group of experts. This happens on a regular basis, through a dedicated mailing list. After the deadline for submission, the reactions are edited and published with signatures in one document on the website of the Observatoire de la finance and on its LinkedIn page. If you would like to join the discussion, you may send an email to the editor, Dr. Virgile Perret <perret@obsfin.ch>.

OF Discussion Board – Questions addressed so far

- Question 7: [While trade tensions grow, WTO predicts a sharp fall in world trade for 2020 and 2021, with strong impacts on developing countries. For decades there used to be an intellectual and political consensus that free-trade contributes to growth and development of all involved. This consensus seems to belong to the past. What kind of international trade, and trade governance, does the world need?](#)
- Question 6: [Staggering amounts of money start pouring on Western economies in order to keep the economic machine working and to avoid massive social shocks and unrests. How will this effort be financed? First step is clear: public bodies will issue debt and borrow on the markets, while central banks will pump liquidity to make the deals easier. The second step is less clear: what should the governments do to allocate these](#)

massive amounts: give away by distributing to the affected households or enterprises (helicopter money); lend them and ultimately either enforce the service and reimbursement conditions or cancel the debt; or should they provide equity to enterprises as would do an equity (sovereign?) fund, and expect future dividends - and for the big enterprises the stock price hikes - to cover, in due time, the incurred expenses?

- Question 5: In response to the crisis, the resilience of the “domestic/ household economy” proved essential for many despite the fact that this activity is not monetized and remains “invisible” for official statistics. What economic policy recommendations should be drawn from this experience ?
- Question 4 : In pandemic times the world operates thanks to GAFAs and telecoms. These giant enterprises are becoming every day more clearly the backbone of our economic, social, and political lives, which makes them players of systemic and global importance. How will/should evolve their future regulation at national and global levels? What are the rationales behind?
- Question 3 : What would you suggest as priority actions to reach out to the most exposed to the economic aftermath of the pandemic crisis in developing countries?
- Question 2 : What principles should guide us in striking the balance between « lives and livelihoods »? Or put differently, between health and GDP?
- Question 1 : How has the virus crisis affected your basic convictions about economy and society?

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