Financial Times (March 6, 2016)

New global trade under old national rules

Regulation has not kept pace with the growth of cross-border services

If world trade were behaving the way it used to, the global economy would be in crisis rather than just looking a touch wobbly.

During the 1990s and most of the 2000s, goods trade grew at about twice the rate of global gross domestic product. The financial crisis brought with it a 12 per cent contraction in trade volumes, which led to a great deal of hand-wringing about a repeat of the collapse in global commerce during the Great Depression. There was then a smart recovery in goods being shipped, which reassured many that business had returned to normal.

In fact, neither catastrophists nor optimists were right. While goods trade has expanded over the past five years, it has done no more than keep pace with the growth of the global economy. Economists and policymakers wondering whether this is a cause for alarm have generally concluded that it is not.

Much of the slow growth in trade seems to be to do with the changing structures of supply chains, with China in particular taking internationally disaggregated production lines inside its economy. But it still means that, with global commerce shifting from manufacturing and

agriculture to services and investment, the international rules of the game are struggling to keep up.

Ironically, given its disembodied nature, the rapid expansion of digitisation from the 1990s seems to have facilitated trade in goods much more than in services. Instant communication of demand and production meant rapid and efficient manufacturing supply chains could snake around the world.

Cross-border flows of data are growing very quickly: the consultancy McKinsey estimates that by the end of 2016, businesses and individuals will send 20 times as much data around the world as in 2008. Yet while parts of some sectors like business services have seen considerable outsourcing, others such as legal and professional services, constrained as they tend to be by domestic regulation, are subject to much less international competition.

The reality is that globalisation of much of the newer parts of the economy, particularly the service sector, has been held back by fragmented regulation and segmented markets. Attempts to unify different sets of rules have generally foundered on entrenched interests and the inertia that comes with regulatory frameworks that are time-consuming and politically difficult to change.

For example: in both the Trans-Pacific Partnership it has negotiated with 11 other Asia-Pacific countries and the Transatlantic Trade and Investment Partnership it is hammering out with the EU, the US has argued that trade in financial services is a key part of the global economy. Yet there is no appetite in the US for substantially reopening the Dodd-Frank Act to aid harmonisation of international practices.

Only recently has the apparatus of trade negotiations turned itself towards the modern services trade. The Doha round of trade talks, which died a merciful death last year after 15 years of negotiations, focused mainly on agricultural and manufactured goods. Talks over a smaller plurilateral services agreement were launched in 2012 but are a long way from conclusion. Meanwhile, the attempt to harmonise regulations in the TTIP is foundering on differences in the way the EU and US set their rules.

Patterns of trade are changing and the rapid growth in exports and imports of goods in the two decades before the financial crisis may never return. If globalisation in services is to replicate that achieved in goods, the rules that govern it must change too.