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## **Comment** L. Alan Winters

This is an interesting and wise chapter. There is little to disagree with. Irwin and O'Rourke suggest that among the things that contribute to making a

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system reasonably robust are some rules, a hegemon, an institutional framework, and a reasonable degree of flexibility. None of this can be pinned down precisely, but it seems to me to be correct. I would also add—although perhaps this is part of their institutional framework—that transparency and procedure have a role to play. Transparency is a key ingredient of public acceptability and is also often a precursor to some flexibility: when problems are dealt with in public, the public can often see why it is that new approaches/flexibility are required. Procedure plays a slightly different role. It can assure players of some basic degree of fairness—which the behavioralists tell us is almost hard-wired into the human brain—and, by replacing or supplementing political pressures by technical fixes, it can also draw the political poison from small issues and help to avoid escalation into unmanageable conflicts.

I think it is too early to declare victory in dealing with the crisis, both so far as restoring growth in the rich economies and trade policy reactions are concerned. In 2012 the recovery has slowed, and in places reversed, because of an inability to deal with the financial fallout of the boom, and it must still be possible that the 2009 crisis will indeed degenerate into a trade policy rout. It is a matter of relief that it has not done so already, but as fiscal austerity becomes a goal more or less in itself, as it has in Europe, and the ability of expansionary monetary policy to take up the slack diminishes, I wish I could be completely confident that we will not see permanent damage to the liberal world trading order.

The basic point made by Irwin and O'Rourke that mostly it is shifts, not shocks, that change things does seem correct to me, and the rest of my comments will be about the shift they identify in the rise of China.[1] I have argued elsewhere that while the rise of China is not wholly unprecedented in terms of speed (Korea expanded its exports as fast), it is unprecedented in terms of size (Winters and Yusuf 2007). At the start of its acceleration, China accounted for one-fifth of humankind, and when such a body starts to change at rates as fast as we have ever seen you had better watch out. My question is whether this shift will, as in the past, cause a major disruption to the trading system or whether over two centuries we have learned enough to be more sensible this time around.

In terms of the world trading system, I shall consider three manifestations of the shift. First, as Irwin and O'Rourke state, China has placed huge competitive pressure on other producers. This is evident just from thinking about how the emergence of China in trading terms has changed world factor endowments and so altered everyone else's comparative advantage. It is also seen in the way firms in other countries have been squeezed in terms of their sales, pricing, and existence. The pressures to turn to protection have been resisted so far, perhaps because large western firms do not want to disrupt their profitable trades with China, but the dyke against political

1. The points made in the rest of these comments are elaborated in Winters (2012).

pressure will not hold indefinitely without a good deal of explicit reinforcement and support from major governments. As Irwin and O'Rourke observe, in the long run the world will have to accommodate a very large China in the world trading system.

Second, China has integrated into the WTO in a very institution-preserving way. Many feared that China, which generally has not liked to join institutions that it did not help to create and has certainly disliked external restraints on its policy discretion, would be disruptive in the WTO; such fears have proved to be quite misplaced. Like other members, China has pursued what it sees as its self-interest within the WTO, but always within the context of the existing rules. In disputes it has bridled against what it sees as discrimination in the use of antidumping duties based on its nonmarket status, but it has brought few cases in retaliation, tried to settle those brought against it by consultation, and complied with rulings as much as other members. China has not contributed as much to the Doha Round as some (e.g., the United States) would wish, but given its extensive liberalization in the accession process and that the Doha Round was partly to complete old business and slated to be over by 2005, this seems to me neither surprising nor inappropriate. If we take a realistic view of the Doha Round, all the evidence is that while China clearly represents a huge shift in world trade it is trying not to be a shock to the institutions of the world trading system. So far, so good.

The third area of potential strife is global imbalances. These are due to macroeconomic disequilibria—mainly China's very high rate of enterprise savings, which arises from the conjunction of low factor prices (subsidies to land and borrowing, and strong rural-urban migration that keeps wages low) and the fact that (even with private firms) dividends are low or zero. They are not due to the institutions of world trade as Rodrik (2011) maintains. Rodrik's analysis of the imbalances is that countries need to boost their tradables sectors to stimulate growth, which in China is necessary to preserve social harmony, and that, whereas left to itself the Chinese government would use industrial policy to provide the stimulus, membership of the WTO has ruled that out, so the government has to turn to exchange rate undervaluation instead.

Given that I reject Rodrik's diagnosis, it is not surprising that I should reject his prescription that the solution is to require WTO to allow subsidies and instead manage exchange rates multilaterally. This seems almost bound to lead to the collapse of the liberal trading order and without, on past form, any real prospect of managing exchange rates. Likewise, there are substantial difficulties with proposals that have circulated to treat exchange rate-undervaluation as a violation of WTO obligations and thus subject to dispute settlement and eventual retaliation in terms of trade restrictions. The WTO does not have the structure, the political clout, or the retaliatory tools to be able to manage this, and any attempt to get it to do so would very likely fail and thus discredit the whole of the WTO enforcement mechanism.

Either of these two reactions would turn a somewhat uncomfortable adjustment to a shift into a massive rout of the institutional structure and the level of international trade. They would be precisely the kind of destructive behavior Irwin and O'Rourke identify as the problem in the past.

I regret that I also see another opportunity to turn a shift into a rout, and this concerns export restrictions. The WTO has little to say about export restrictions, permitting export taxes almost at will for "ordinary" members, and having only a compromised ability to prevent quantitative restrictions because these are allowed under certain circumstances by the GATT's Article XX.[2] China has already lost one WTO dispute on export restrictions on industrial raw materials and is now subject to another on rare earths, tungsten, and molybdenum. In this case China has a virtual monopoly of global production for inputs that are critical to many modern technologies, including green ones. The fear in the West is that the restrictions will not only increase the cost of climate policy, but also cause the innovative sectors using rare earths to relocate to China, and that this will switch the locus of innovation with serious redistributive consequences. China has been a major beneficiary of the liberal order of the last three decades and if, when it has huge market power, it exploits this strongly, partners will feel that it is just not "playing the game." Couple this with export restrictions on food, as we saw mainly from middle-income countries in the last food-price hike (2006–2008), and we could easily see a fracturing of many global trade links. In this case cool heads in China and the emerging markets are what we need to avoid calamity.

To summarize, Irwin and O'Rourke have given us a wise account of the history of the world trading system and have categorized the threats as shifts and shocks. By and large, they argue, it is the former that have caused the largest problems to a liberal world trading order and I agree with this. Moreover, as an eternal pessimist I have described how it could all happen again with what is arguably the largest shift we have ever seen—the rise of China. Ill-considered policy reactions to China's rise, both in China and elsewhere, could undermine the whole trading system. The stakes are as high today as ever.

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2. "Ordinary" members in this particular context is everybody but China, because China's Protocol of Accession tightly controls its recourse to export taxes, an asymmetry that the Chinese resent.