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China as the New Raison d'Être for Reviving Multilateralism

[Opium was] a mere incident to the dispute . . . the cause of the war is the kowtow—the arrogant and insupportable pretensions of China that she will hold commercial intercourse with the rest of mankind not upon terms of equal reciprocity, but upon the insulting and degrading forms of the relations between lord and vassal.

—US President John Quincy Adams, on China's attitude to trade

In 1910, Norman Angell, future Nobel Peace Prize Winner, published *The Great Illusion*, a pamphlet-turned-book that acquired cult status for propagating the view that Europe had become so interlaced economically through trade, credit, and finance that war was impossible (Ahamed 2009). Twentieth-century wars would be so economically devastating even to the aggressor that waging it would amount to self-inflicted folly.[1]

Notwithstanding the fact that Angell was proved so catastrophically wrong, one would have to maintain that the world today has once again become so, and so much more, intertwined that not just wars but even economic aggression by dominant powers must be very low probability outcomes. The world's trade-to-GDP ratio in 1913 was about 15 percent; today it is close to 50 percent. Global financial integration—measured as the stock of world external liabilities/assets to world GDP—amounted to about 20 to 30 percent in 1913; today it is closer to 200 percent.[2]

More broadly, there are many more active participants in, and beneficiaries of, globalized trade and finance than ever before. Further, prior to World

1. In the words of Lord Esher, who was Angell's most earnest disciple, the inevitable consequences of "commercial disaster, financial ruin, and individual suffering," would be "pregnant with restraining influences" (Tuchman 1962, 12).

2. The trade data are from Maddison (2001); financial globalization data for 1913 from Schularick (2006) and for 2009 from an update of Lane and Milesi-Ferretti (2007).

War I, while the world was globalized, the flows were mostly unidirectional: Capital and manufactured goods flowed from Europe (and to a lesser extent the United States) to the periphery, commodities the other way, and labor from Europe to the United States. In contrast, modern trading and financial relationships, notably the slicing up of the value-added chain and foreign direct investment (FDI) have created greater two-way flows of capital, goods, and ideas—leading to the phenomenon of "criss-crossing globalization" (Mattoo and Subramanian 2010)—which create enmeshing and interlocking private interests to a greater degree than ever before.

China itself embodies this criss-crossing globalization. It is the hub for many of the modern value-added chains resulting in a high level of imports and exports and its outward FDI is beginning to catch up with FDI inflows into China.[3] Moreover, as argued in earlier chapters, China—with its unusually high dependence on trade for completing the catching up process—will have a vested interest in an open trading system and hence act, even lead, to preserve it. And if the renminbi ascends to become an international reserve currency, China might be reluctant to lose the prestige, and any associated benefit, that comes with that status by disrupting financial and trade relations in any serious way.

So, is the current open, rules-based economic system safe? History's lesson is that one can never be sure. One cannot be certain that the enmeshing of interests will be strong enough to sustain the status quo. Nor is there a cast-iron guarantee that the current ideological embrace of markets as the predominant basis for organizing economic relations will survive the vicissitudes of intellectual fashion, the selective and self-serving interpretations of policymakers, and the financial crises that will inevitable shock the modern global economy. There is tail-side risk that interests, ideology, and institutions, both domestic and international, will be inadequate to the task of preserving the current system. And then there is always the unforeseeable and the irrational. World War I, after all, did happen.

So, there remains a small possibility of an eventual unbenign exercise of dominance by a hegemonic or near-hegemonic China. President John Quincy Adams's remarks, hysterically off the mark at the time they were made, might nevertheless carry some resonance in the future. What economic forms might such hegemony take? A dominant China could reverse some of its past liberalization (as for example it has done with its exchange rate policy); it could maintain or pursue industrial and quasi-protectionist policies domestically; it could attempt to capture essential resources (energy, food, and commodities) abroad and enter into bilateral and discriminatory arrangements with selected partners, all of which given the country's size could affect the fundamental character of the current economic system.

Historically, the United States during Pax Americana was noteworthy in refraining from exercising most if not all these forms of dominance. With ex-

3. In 2009, the outward and inward FDI figures were, respectively, $57 billion and $94 billion.

ceptions noted in chapter 1, its markets remained open, and until recently, it practiced nondiscriminatory trade. And as a net importer of energy and commodities, it ensured access to these resources through political and security arrangements (for example, in the Middle East and Gulf). This followed the recognition that ensuring access through ownership of these supplies across the globe was not a viable strategy in the face of a strong desire on the part of resource-owning nations not to allow majority-foreign ownership of energy resources (Yergin 2008).

China's economic dominance going forward is more likely to manifest itself in its own protectionism more than via monopolizing access to resources or by entering into discriminatory arrangements. As Aaditya Mattoo and I (forthcoming) argue, energy is becoming more diversified in terms of type and geographic location; and barriers in other countries have come down in a way that makes discriminatory trading arrangements by China less of a threat. So, it is preventing a reversal of liberalization of the Chinese market and facilitating its further opening that will be of main concern to outsiders.[4] But can these be achieved through international cooperation?

Limits to the Efficacy of Trade Reciprocity with a Dominant China

The previous chapter argued that after World War II, reasonably successful cooperation between the two dominant trading powers—the United States and Europe, the G-2 of that era—was achieved in the GATT/WTO via reciprocal exchange of market-opening commitments. Can this same mechanism help or be effective going forward with China as a dominant trader? Will it be possible to avoid the unbenign exercise of China's dominance and get greater market opening in China and reduce its policy barriers, especially in all those areas that are not covered by WTO rules such as China's government procurement, investment rules, technology indigenization, and service sector policies?

There might indeed be a structural problem, limiting the scope for reciprocity. When the United States and European Union dealt with each other in the postwar period, their markets were open, and in some areas closed, but broadly to the same extent. This symmetry facilitated reciprocity. In the future, problems could arise because the United States and European Union are in policy terms more open than China. This is a structural problem for cooperation going forward stemming from a situation in which economically dominant powers for the first time are at different stages of development.

China, although highly open in terms of trade outcomes, and although it has made great strides in removing policy barriers as part of WTO accession, is,

4. Charles Kindleberger argued that a benign hegemon needed to perform three functions to provide systemic stability: maintain open markets, provide countercyclical long-term lending, and supply short-term liquidity in a crisis. In the case of China, it is the first that seems most in question and hence the focus of the discussion here.

however, more closed in policy terms especially outside the traditional goods area, for example, in services, technology, and government procurement, with the closed policies taking the form of continuing state control over a large part of economic activity.[5] According to Gootiz and Mattoo (2008), China's service sector policies are about three times as restrictive as those of the United States. In any future bargain, the United States will, by virtue of previous liberalization, have less to offer China.

The paradox will be that China will have greater leverage in bargaining by virtue of its much larger trade and market size but will also have the greater policy barriers. It is as if in a duel, one party offers both the smaller target and has the pistol with greater range of shot. For example, by 2020, China's imports will be one-and-a half times that of the United States and twice as large as Germany, conferring the kind of power that comes with being able to determine access to its markets, the power that the United States has enjoyed during much of the postwar period. Future bargaining will therefore be structurally imbalanced in China's favor, and reciprocity therefore more difficult to achieve.

This structural imbalance will be a persistent source of tension between the United States and China. If the US manufacturing sector hollows out, and as the United States comes to rely to an even greater degree on services and intellectual property, it will seek to open markets overseas, including and especially in China. If China's future opening is slow, the United States, over time, might be increasingly tempted to play the unfairness card based on the disparate levels of policy openness: Why should US markets be more open than that of a rival and equal?

This imbalance in bargaining could remain at the level of sparring and skirmishing without systemic consequences. But suppose the United States has difficulty addressing its structural economic problems: high unemployment, stagnating median household income, rising inequality, and declining economic mobility, all creating a large, disaffected, and beleaguered middle class. And suppose that in this climate, the intellectual consensus in favor of openness gets increasingly frayed, as has been evident in the last few years. Recall that a stellar cast of intellectuals—from Paul Samuelson to Paul Krugman, Alan Blinder, and Larry Summers—has expressed misgivings about different aspects of globalization.[6]

5. It is important to stress that China is mercantilist but open in terms of trade outcomes, the latter reflecting in part that its policy barriers in agriculture and goods are reasonably low. But exceptional trade and mercantilist outcomes, which relate largely to traditional areas, are consistent with China being restrictive and maintaining high barriers in the new areas.

6. Samuelson (2004) argued that the rise of developing countries such as China and India could compromise living standards in the West by worsening the terms of trade—that is, by making imports more expensive. Krugman (2009) has focused on the impact of imports from developing countries, and China in particular, on the distribution of income in rich countries and wages of their less-skilled population. His conclusion is that, "It is likely that the rapid growth of trade since the early 1990s has had significant distributional effects," and more specifically that "it is

If the United States is frustrated by an unwillingness on China's part to open new sectors of its economy, lacks the carrots to overcome this unwillingness, faces a weak economic climate and shifting intellectual certitudes, and is goaded by perceptions that China is not making its fair contribution to keeping markets open, the United States might be tempted to threaten to close its own market to China unless China further opens its own. The implicit bargaining approach here would thus not be "first-difference reciprocity"—that is, "you open your markets for my opening mine." Rather, it would be "level reciprocity"—"you open your markets for my refraining from closing mine so that we can all be similarly open."

How can this tension be best managed—it cannot be eliminated—to prevent a major trade conflict in the years ahead? Put differently, what insurance can the world take out today against the small chance of a damagingly assertive China in the future? It seems that the only real insurance is multilateralism, or more specifically, keeping China tethered to the multilateral system. The historical analogy would be the post–World War II experience of anchoring Germany in Europe and European structures. The objective and motive then were largely political although the early instruments deployed were economic. In the case of China, the motive would be to preempt economic hegemony.

One must keep in mind a broader truth, or rather the big dirty secret, about cooperation in general. Vis-à-vis a dominant power, on the one hand, no cooperation can be effective if some critical self-interest is at stake for the dominant power, and on the other, no cooperation might even be necessary if natural forces are at work that align self-interest with the collective interest. Cooperation is only necessary, and perhaps possible, for the muddy middle, the grey zone where neither the consonance of self-interest and collective interest nor the clash between the two is particularly strong.

For that grey area, multilateralism offers the best hope for placing checks on dominant economic powers. One cannot, however, be overly confident about the efficacy of multilateralism in checking China's exercise of dominance. The experience of recent attempts to persuade China to change its exchange rate policy is instructive. The more promising prospects for inducing Chinese cooperation have arisen when a number of countries, including

probably true that this increase (in manufactured imports from developing countries) . . . has been a force for greater inequality in the United States and other developed countries" (Krugman 2009, 134–35). Blinder (2009) has drawn attention to the employment and wage consequences of the outsourcing that has been facilitated by technological change and trade in services. He estimates that between 22 and 29 percent of all US jobs will be offshored or offshorable within the next decade or two. And most recently, Summers (2008a, 2008b) has highlighted the problems stemming from increasing capital mobility. Hypermobile US capital creates a double whammy for American workers: First, as companies flee in search of cheaper labor abroad (the "giant sucking sound" in Ross Perot's evocative and provocative phrase), American workers become less productive (because they have less capital to work with) and hence receive lower wages; the "exit" option for capital also reduces its incentive to invest in domestic labor. Second, capital mobility also impairs the ability of domestic policy to respond to labor's problem through redistribution because of an erosion in the tax base as countries compete to attract capital by reducing their tax rates.

emerging markets such as Brazil, India, Indonesia, and Mexico, have expressed concern about China's policy, rather than when the United States has acted alone. The sobering reality—and one that should engender realism rather than optimism about multilateralism—is that even these collective efforts have had only limited success. Hence multilateralism should be viewed as a necessary rather than sufficient insurance policy.

Thus, the aim of China's trading partners—and the list must go beyond the United States to include other major ones such as the European Union, Japan, Brazil, and India, for starters—should be to make multilateralism a habit for China rather than a distraction or inconvenience. The aim would be to make multilateralism so routine and legitimized over the next several years—the period of transition to possible Chinese dominance—that there would be serious costs to China, reputationally and substantively, if it were to depart from it once its dominance becomes entrenched.

What will it take to legitimize multilateralism and make it routine? Facilitating this might require one or even two acts of self-restraint by China's major trading powers. First, they should all refrain from negotiating bilateral free trade agreements with China, at least in relation to areas covered by the WTO (goods, services, government procurement, and intellectual property). If some of these countries negotiate bilateral trade agreements, then all of them will have less multilateral dealings with China. The problem is not just that bilateral agreements with China might be imbalanced but also that enforcement of rules and agreements is likely to be more difficult bilaterally than multilaterally. In other words, China's economic dominance might get reflected in imbalanced rules and opening as well as asymmetric adherence to them. As it is, China's trading partners are concerned that China might not live up to its WTO obligations—e.g., in the area of intellectual property rights enforcement, the United States claims lost sales of about $50 billion from trademark and especially copyright infringements (USITC 2011)—or might subtly circumvent them as it has done say with its exchange rate policy. Imagine the difficulties if these obligations had to be enforced bilaterally.

The more that countries elevate the role of bilateralism in dealings with China, the less China will be anchored in the multilateral system, and the more countries will be exposed to the exercise of Chinese dominance. It is not necessary to assume that China will exert power in undesirable ways to eschew bilateralism and embrace multilateralism. Rather it should be seen as insurance against the possibility of being at the receiving end of unrestrained Chinese power.

A more difficult question is whether a second act of self-restraint by China's major trading partners might be necessary. If those countries resist deepening bilateral ties with China but then turn around and negotiate free trade or economic partnership agreements with each other, China might well see this as economic and trade encirclement from which it is excluded. A more positive and less hostile way of keeping China anchored would be for its trading partners to pronounce that they will embrace multilateralism not only in their dealings with China but also among themselves. This would signal a belief in the intrinsic worth of multilateralism rather than just as an instrument to contain China.

Alternative Approaches: Promiscuous and Hostile Bilateralism

What are the alternatives to multilateralism as the preferred way to deal with a rising China? Two such alternatives are suggested by relaxing the acts of self-restraint discussed above that would sustain the multilateralist approach. These alternatives still remain available as options because they have not as yet been overtaken by events. Although bilateral (and regional) agreements have been proliferating, the major players—the United States, European Union, China, Japan, Brazil, and India—have for the most part not entered into bilateral agreements among themselves.[7]

Promiscuous Bilateralism

The first alternative to multilateralism is the form of bilateralism advocated most forcefully by Robert Zoellick and C. Fred Bergsten, which one might call "promiscuous bilateralism." Advocates of this approach rely on the competitive dynamic it creates: If two countries negotiate preferential reductions of barriers, one or several outsiders will be hurt. These outsiders will then have an incentive to negotiate preferential agreements themselves and so on until the goal of global free trade is achieved.

In the old debate between the bilateralists and the multilateralists, the divide was not about the endpoint: All parties wanted global free trade. Rather, the divide was whether preferential (bilateral) agreements would be, in Jagdish Bhagwati's (1999) words, a "building bloc" or "stumbling bloc" toward that final goal, with the bilateralists falling in the former category and the multilateralists in the latter. To the former, the competitive dynamic argument remains unaltered in the presence of a rising China. They would disagree with both forms of restraint suggested above, that is, refraining both from making free trade agreements with China and from China's major trading partners making such agreements among themselves. In fact, they would actively pursue both (hence the "promiscuous" description).

The difficulty with this kind of promiscuous bilateralism is twofold. The success of bilateral agreements in the past in reducing barriers and generating the competitive dynamic for further liberalization simply cannot be ap-

7. Negotiations between Brazil and Europe toward a regional agreement have recently been revived, and those between India and Europe are close to being finalized. In the past, closer trade ties between the United States and Brazil was tried in the context of the free trade area of the Americas and closer US-Japan and EU-Japan is widely discussed in Japan. Middle tier countries such as Korea and Mexico have entered into a number of bilateral agreements.

plied to China. The most important successes of such agreements—the North American Free Trade Agreement (NAFTA) and Eastern and Central Europe—have largely involved a big economic power such as the United States or the European Union negotiating with smaller countries. As such, it is the smaller countries that have done most of the incremental liberalization. In these negotiations, it is the larger countries that have held the balance of negotiating power and influence and successfully used them.

Going forward, though, with China's growing size, the balance of negotiating power will be with China rather than its partners that are seeking bilateral agreements. The key argument for multilateralism is that there will be enough combined heft among China's trading partners such that negotiating with China on market opening can be more balanced. China might be willing to open its government procurement market in return for its major trading partners opening theirs. A multilateral negotiation among these large trading countries could conceivably lead to meaningful opening. But China's willingness to open up in a similar manner in negotiations just with the United States or European Union or with some less-weighty combination in a bilateral negotiation is far from clear. If the basic problem is the imbalance of leverage arising from China's size, bilateralism will by definition be less effective than multilateralism.

If bilateralism will be less effective in securing market opening, a similar problem carries over to enforcement and the incentives to adhere to previously agreed-upon rules. China's incentive to abide by multilateral rules will be stronger than to abide by a series of bilateral agreements because the reputational costs of being seen as errant is much greater in the former context. To picture this most starkly, consider the following alternative scenarios.

In the first, China has agreed to zero tariffs separately with Indonesia, Brazil, India, the United States, and the European Union as part of five bilateral agreements. In the second, China has agreed to reduce its multilateral tariff to zero in the WTO. In the former case, if China wanted to renege on its commitment to, say, Indonesia, it would do so under a bilateral agreement with only Indonesia as the victim. Indonesia could presumably seek recourse in some (fledgling) bilateral procedure for settling disputes between Indonesia and China. But if the commitment were a multilateral commitment, as in the second case, Indonesia could set in motion a well-established multilateral dispute settlement machinery in which all partner countries have a stake. The reputational costs and the effectiveness and legitimacy of enforcement would be a more effective deterrent in a multilateral context than regionally or bilaterally.[8] It is the opprobrium that is associated with being a deviant from the global norm—rather than a bilateral one—that is the most valuable weapon

8. In fact, very few regional enforcement mechanisms—not even NAFTA, which is perhaps the most well advanced—have the credibility of the WTO's dispute settlement mechanism. For example, the United States chose the WTO rather than NAFTA as the forum for its successful complaint against Mexico's telecommunications policies.

that the world can deploy in tying China today in a way that minimizes the prospects of an aggressively dominant China in the future.

Thus, in looking ahead, bilateralism's previous appeal needs to be carefully reviewed. It is not a matter of making regionalism compatible with multilateralism. With a dominant China, regionalism will be less effective in actually securing greater liberalization because of the imbalance in size. And, perhaps more importantly, regionalism will be less effective in imposing the kind of reputational costs that will be key to keeping China moored in an open, rules-based system.

Hostile Bilateralism

Instead of relaxing both strictures against bilateralism, suppose only the second one is relaxed—that is, China's major trading partners, led by the United States and Japan, enter into bilateral agreements among themselves but exclude China. The consequence if not the aim of such an approach would be to encircle China and worsen the terms of its access to the markets of its trading partners, thereby inflicting a large cost on China presumably to induce further market opening on its part. This would be, and would be viewed by China as, an act of economic aggression on the part of its trading partners. China's trading partners could justify this as waging war to secure peace, in this instance by getting China to the negotiating table and show a willingness to open its economy and address some of the major irritants of its trade policies.

The problem with this strategy is that it will probably not be effective in the short run and will certainly sour the prospects for cooperation in the medium to long run. China is already dominant and increasingly beyond the scope of influence of outsiders, especially via the threat of sanctions. China has enough market power to offer or deny to its Asian neighbors and enough cash to dangle to all those in need, from Africa to the heart (and not just the periphery) of Europe, to deter countries from pursuing this type of hostile regionalism. Long before China's trading partners can achieve encirclement, China will have negotiated free trade agreements with, invested in infrastructure in, and helped avert financial crises in some or many of these same countries.

Hence an attempt at hostile regionalism will not only be unsuccessful but also leave behind bad memories. And the system does not need a dominant China nurturing resentments and harboring grudges against a hostile outside world.

Asian-Centered Regionalism as a Medium

If desisting from bilateral deals with China and with each other is one way of keeping China anchored multilaterally, what scope might there be for regional integration efforts such as the Trans-Pacific Partnership or the Asia-Pacific Economic Cooperation (APEC) forum? The case for anchoring China in something smaller than a robustly multilateral process such as the WTO and something larger than bilateral agreements would be the following. The WTO process, especially in the wake of the failure of the Doha Round, has proven to be ineffective and in part because it is unwieldy with too many actors creating multiple veto points and stasis. Why not choose a smaller grouping that can make progress especially if an Asian-centered grouping can increase the prospect of eliciting China's cooperation?

Advocates of this view favor something like the Trans-Pacific Partnership (TPP) and the Free Trade Area of the Asia-Pacific (FTAAP), in which it is hoped that the United States and Japan would provide the kind of counterweight to China that would remedy the basic imbalance of bargaining power while the presence of China's other Asian neighbors would create a legitimately non-US dominated structure. The ardent Asian regionalists would also point to the greater strides being made on opening the more difficult behind-the-border barriers in Asia, especially in the Association of Southeast Asian Nations (ASEAN) and APEC. Why not build on that?

The key analytical point to bear in mind, and the challenge for cooperation with China, is the growing imbalance of power and influence between China and its partners, which limits the possibilities for reciprocal bargaining that has been at the heart of successful cooperation between the larger trading countries. Whether this imbalance is easier to remedy with a large group of countries (as in the WTO) or a smaller group (as within Asia) will, and should, largely be dictated by pragmatism and expediency. By definition, the larger the grouping the better the prospect of rectifying the imbalance. Equally, larger groupings can become unwieldy and ineffective. More practically, an Asia-Pacific grouping could exclude Europe, Brazil, and possibly India, whereas a WTO type collectivity would include them all. Who all should be "in" and who can be "out" are details that will have to be ironed out in the future, but it is essential to avoid the fragmentation that would arise from promiscuous bilateralism and the ineffectiveness and ill-will from hostile bilateralism.

Impediments to Revived Multilateralism

Even if multilateralism might be the preferred approach in dealing with China, the difficulties of reviving it by tethering China to it will be considerable. The proximate challenge is contending with the Doha Round, which refuses to go away. The deeper challenges relate to institutions, attitudes, and habits around the world, not just in the United States but in the larger emerging-market countries such as India and Brazil.

Proximate Impediments: The Doha Round

It is worth recalling a long-forgotten fact about the Doha Round. Even at the start, there was little appetite for launching the round, as evidenced in the string of previous, unsuccessful attempts—Seattle, Cancún, Potsdam—to do so. It was midwifed in a bout of post-9/11 solidarity that proved transient once the horrors of the terrorist attacks gave way to the routine and sordid political realities that accompany trade negotiations. Furthermore, it is not at all obvious, unlike the GATT/WTO's previous efforts, what big change, development, or opportunity the Doha Round has sought to address. The irony is that the round was planned as a development round (its official title is Doha Development Agenda) to give a boost to the economic prospects of developing countries. But the return of convergence (chapter 4) and the depressed prospects of the industrial countries in the aftermath of the global financial crisis highlight how quaint the motivating concern for the Doha Round has become. It is now developed rather than developing countries that seem to need a development boost.

Part of the current problem seems to be the view that failure to conclude the Doha Round would have devastating consequences for the WTO and the multilateral trading system. But this view needs to be questioned. Most agree that the Doha Round's substantive benefits would be minimal, largely related to providing security of future access rather than triggering new liberalization (Martin and Mattoo 2008, Hufbauer et al. 2010). This in turn explains the lack of private-sector enthusiasm for completing it because there is not a lot for that sector that rides on concluding the Doha Round. It is telling that meetings related to the round do not even rouse the wrath of the antiglobalization protesters. If an outcome has modest substantive value, how can failure to realize it have such significant costs?

More recently, it has become evident that the failure to complete the Doha Round might itself reflect China's growing dominance. In a recent paper (Mattoo, Ng, and Subramanian 2011), we argued that China looms especially large in the markets of major trading partners in sectors where protection is greatest. China's share in these sectors in Japan is over 70 percent, in Korea over 60 percent, in Brazil about 55 percent, in the United States, Canada, and the European Union about 50 percent each. Liberalization under the Doha agenda, especially in the politically charged, high-tariff sectors, is increasingly about other countries opening their markets to Chinese exports. And China's major trading partners are disinclined to do so.

This disinclination is exacerbated by the strong political perception that China's export success has been achieved, and continues to be sustained, in part by an undervalued exchange rate. It seems unlikely and politically unrealistic to expect China's trading partners to open further their markets to China when China is perceived as de facto (via the undervalued exchange rate) imposing an import tariff and export subsidy not just in selected manufacturing sectors but across the board. Unless Chinese currency policy changes significantly, and unless there can be credible checks on the use of such policies in the future, concern will remain in many countries, both industrial and emerging-market, about the increased competition from China that liberalization under Doha might unleash.

But the argument that the WTO and the multilateral trading system would be fatally undermined by the failure to complete the Doha Round rather than its unwillingness or failure to begin grappling with the real big challenge of the future—China's dominance—is somewhat like complaining about the lack of euphony in Nero's fiddling instead of attempting to put out Rome's fires.

Deeper Impediments

Collective Action and Strategic Forbearance

The more serious impediment to tethering China to the multilateral mast relates to China's trading partners and the collective action problems that must be overcome if they are to form a unified coalition for multilateralism. Consider the daunting requirements for collective action to be possible. First, all these countries—not just the United States and the advanced countries but the other emerging-market countries as well—need to take seriously the possibility of future Chinese economic dominance and the small but finite probability of this dominance being a threat.

The temptations to flout this approach—to deepen bilateral ties with China because it offers some type of market concessions (e.g., buying more French airbuses or US Boeing products) or because it is more forthcoming on cooperation on other issues such as North Korea or Iran—will be considerable. But the consequence of doing so, which could result in not being able to restrain Chinese economic and trade dominance in the future, will become evident only with time. The pursuit of multilateralism calls for a strategic patience that will be difficult to muster in the short run.

Brazil enthusiastically embarked on closer bilateral engagement a few years ago, signing a number of agreements on trade, currency, and investment with China. But Brazil has become disenchanted as it has seen its currency appreciate and its economy lose competitiveness, while China has provided no relief by way of corrective currency action of its own or the promised investments in Brazilian resources.

The sections that follow consider two examples of deeper impediments to the revival of a China-focused multilateralism, one each from the United States and India.

Anachronistic Institutional Structures: United States

In the case of the United States, there is the question of whether domestic institutions support or impede multilateralism as the preferred approach to trade. The historical experience of the United States is instructive. The constitutional right to regulate imports in the United States is vested in Congress. This imparts a strong protectionist bias to US tariff and trade policy because liberalization and increased imports affect domestic producers, to whom members of Congress are particularly sensitive. In contrast, the benefits of liberalization are spread among many consumers who have neither the same incentives nor the institutional mechanisms to express their views. Thus the concentrated interests and power of domestic producers, with political outlets for expression, tend to prevail over diffuse consumer interests.

Schattschneider (1935, 127–28) explains this asymmetry: "The political agitation concerning the tariff is profoundly influenced by the fact that, in many instances, the benefits of the legislation to an individual producer are obvious while many of the costs are obscure. . . . Benefits are concentrated while costs are distributed."

The infamous Smoot-Hawley Act of 1931 represented the perfect illustration of this dynamic whereby initial efforts to raise tariffs in agriculture led to coalitions based on vote-trading ("logrolling") in Congress, all aimed at raising particular tariffs until the exercise bequeathed a large and across-the-board increase in protectionism (Destler 1992, Irwin 2011). The act's dire consequences, however, begat a fundamental institutional change in US trade policy. In 1934, President Franklin D. Roosevelt persuaded Congress to delegate tariff-setting authority and agenda-setting power to the administration under the Reciprocal Trade Agreements Act (RTAA). Apart from Congress losing its ability to legislate specific tariffs, this change fundamentally altered the political economy of trade policy in the United States. By making the tariff an international bargaining issue, it brought exporters into the political equation. By explicitly linking domestic tariff reductions to foreign tariff reductions, it created a stake for exporters to lobby against protectionism at home, because domestic protectionism sparked protectionism abroad, which hurt exporters. Congress retained the right to periodically approve the granting of these rights to the president but had less say over specific trade and tariff issues.

Over time, this institutional structure has been broadly preserved, with Congress granting the president fast-track authority to negotiate international agreements but retaining the right to review this authority and also the right to say yes or no to agreements negotiated by the president.[9]

Under Pax Americana, this dual role of the president and Congress has worked well in that it has allowed the two branches of government to use this duality to tactical advantage in international trade relations. Congress was a credible bad cop to the administration's good cop in terms of international trade relations. Often, the refrain of successive administrations to trading partners would be: "Please accede to this deal/demand because Congress will not agree to anything else." Or, "Please accede to this demand/deal or else

9. Destler (1992) has argued persuasively that costs have been incurred in preserving this structure and in ensuring that the risks of a serious lapse back into protectionism in the United States are kept in check. These costs, which took the form of allowing lesser forms and magnitudes of protectionism, were embodied in an elaborate system, which included: providing "relief" in the form of safeguards, antidumping and countervailing duties to domestic producers under "unfair trade" laws; providing access to trade retaliation mechanisms to export interests such as the services and intellectual property to generate a pro free-trade momentum; and allowing special protectionist deals for special cases (steel, automobiles, and semiconductors).

Congress will authorize trade retaliation under its legislative authority, which we (the administration) will be unable to control." And often this was a successful strategy because the United State generally held the balance of negotiating power and influence relative to its trading partners.

But when the United States has to turn from being wooed by to actively wooing others, an insular, instinctively unilateral Congress is no longer a credible bad cop defining the worst case options for US trading partners but rather a potential albatross around the neck of the administration, limiting its international options. When Congress saber rattles or sets unusually high standards for international trade agreements, smaller countries have to take those threats seriously. Indeed, during the Uruguay Round of trade negotiations, the outside option of facing retaliation under laws enacted by Congress ("Special 301" in that instance) if they did not raise their intellectual property standards played a key role in countries such as Brazil and India reluctantly agreeing to higher multilateral standards in the WTO on intellectual property.

But in the case of China, congressional instincts could prove counterproductive. For example, Brazil and India could conceivably come together with the United States as part of a multilateral coalition to discuss exchange rate issues with China. But they would be loath to do so if it were to happen after Congress has authorized trade retaliation against China for manipulating its currency. They would be seen as siding with a belligerent United States rather than a cooperative one. Congressional unilateralism might thus foreclose or weaken some multilateral options for the administration.

Put starkly, under US dominance, Congress limited the options for America's relatively weak partners in negotiations with a strong US administration; under Chinese dominance, Congress will limit the negotiating options for a relatively weak administration vis-à-vis a relatively strong China. These institutional structures can come in the way of successfully mobilizing a multilateral coalition to deal with China in the future.

Perhaps what might be required—and this is radical and speculative prescription—is for the United States to make the next logical change in its domestic institutional trade arrangements inspired by the history of the first such change under the RTAA in 1934. That change would be to transfer even more authority from Congress to the administration in the design and implementation of trade policy. The aim would be to facilitate and galvanize more multilateral approaches—less constrained by a unilateral, insular Congress—that will be necessary to deal with a dominant China.

Habit and Mindset: India

If institutional mechanisms can impede forging a multilateral approach to dealing with a dominant China, so can deeply ingrained habits and mindsets. India is in the throes of formulating its own strategic economic relationship with China. The challenge for India, of course, is to some extent different and arguably greater than that of China's other partners such as the United States.

Bismarck famously said of the United States that it had managed to "surround itself on two sides with weak neighbors and on the other two sides with fish." When it comes to China, India does not enjoy this luxury of splendid isolation. Both history and geography complicate matters considerably.

On the one hand, trade and economic relations between China and India are intensifying, creating opportunities for both countries. On the other, India has to contend with what is becoming, in political terms, an imbalanced economic relationship. India runs a large and growing trade deficit with China, and the pattern of trade is reminiscent of trade during the days of empire. India exports predominantly raw materials to China and imports high-value-added and sophisticated goods. Indian industry and government officials have complained about China's trade, industrial, FDI, and exchange rate policies, which aid, often opaquely, Chinese industry and exports. China's government procurement policies have impeded Indian pharmaceutical exports and the fear is of a large China using its size to create and set standards (for example, for telecommunications equipment), which others have no choice but to follow. Not just the content but the tone of these complaints can resemble the emanations from the toughest China hawks in the United States.

India also is grappling with essentially the same question that this chapter has posed: How much should it engage with China bilaterally and how much multilaterally? India recognizes that its negotiating hands are seriously tied bilaterally because of the imbalance in size, and yet it is unable to embrace multilateralism as conviction, preferring a reluctant and opportunistic multilateralism. And the reason in part is mindset.

India, it is well known, was a habitual naysayer in the international trading system. The underlying objective of Indian economic engagement was the jealous and zealous safeguarding of India's sovereignty. India was a "sovereignty hawk." India has tried its best to minimize having to do what it would otherwise not want to do. In the trading system, for example, India lobbied hard and strong over the past three decades to preserve the right to protect its economy through tariffs and quotas. Sovereignty, in this arena, was equivalent to the freedom to protect or prevent the imposition of rules and obligations that would deprive India of this freedom. Of course, this objective in turn flowed from an economic ideology that initially viewed liberalization and market opening as unhelpful to India's interest and later started to recognize the benefits of liberalization, but still as something to be undertaken at India's pace rather than dictated by trading partners.

But if India was a naysayer, it was one with a following. India was essentially one of the intellectual leaders and the spokesperson for many developing countries (sometimes called the G-77). For example, it played a key role in getting the GATT to accord special status to developing countries, which essentially relieved them of any obligation to liberalize their trade regime in the GATT. Leading a group of like-minded developing countries became not just a position that Indian diplomats and policymakers enjoyed but it became a habit, a mindset, even an entitlement. In recent years, as India's ideological moorings have shifted, it has been able, albeit gradually and episodically, to back away from playing the recalcitrant trade partner bent on obstructing efforts to open up the international economy. But its officials have been less able to walk away from the prestigious mantle of leadership and hence less willing to join multilateral coalitions where the spotlight is necessarily diffused because leadership is shared or even sacrificed. For India and Indian policymakers, it has been easier to repudiate ideology than it has been to spurn the spotlight.

In this situation, India seems to have yielded to the temptation to become a free rider. In discussions on China's exchange rate policy, India has chosen not to align itself with the United States as part of a multilateral coalition for fear of endangering the broader relationship with China ("we live in a rough neighborhood," the Indians routinely say) and because it believes that the United States can "handle" China alone without Indian participation. The consequence, of course, is the classic free rider problem where all countries thinking similarly contribute to the breakdown of cooperation. Both these assumptions are misplaced.

Even where the need for forging coalitions is recognized, the Indian instinct is still to look to deepen relationships with developing-country partners such as South Africa, Brazil, or Indonesia rather than the United States and Europe.

For the new multilateralism to be effective, however, a country such as India must accept that it can no longer be the leader and at the same time recognize that its participation is necessary for successful coalitions that seek to tether China multilaterally. In today's world, and especially going forward, the United States cannot do it alone. Coalitions must be broad, and they require easy engagement between the old powers and emerging ones. Thus, India must not just become a visceral multilateralist but learn the new habits of multilateralism and come to terms with the demotion in status that it entails and the reaching out to all partners that it requires.

The appealing symmetry of the new multilateralism is to induce a greater humility in both the United States and India: in the former, to spurn the temptation—or rather outgrow the illusion—that it can exercise exclusive leadership and dominance in shaping outcomes, and in the latter to shed the desire to do the same by stymieing outcomes and instead participate in forging cooperation as important but humble drones rather than as the queen bee.

A "China Round" for Tethering China[10]

One way to signal that the world community recognizes the need to deal with a dominant China in the future, and to do so multilaterally, would be to put

10. What does it mean to "tether" China given that it is already part of the multilateral system? One answer is that there may need to be a new bargain or equilibrium such that China has an incentive to abide by it. This would be in contrast to the existing equilibrium, which has not proven

to bed the Doha Round and embark on a new round of trade negotiations (Mattoo and Subramanian, forthcoming). The aim of such a "China Round" would in fact be to anchor China, to the maximum extent possible, in the multilateral trading system.

Recall that one of the virtues of the GATT/WTO has been its ability historically to respond to five major developments in the trading system. These include (1) promoting liberalization in the immediate aftermath of World War II in the first few rounds of tariff negotiations; (2) diluting the effects of discriminatory European integration by way of most favored nation (MFN) tariff cuts in the Kennedy Round; (3) addressing the competitiveness threat against a backdrop of US decline from a then-rising Japan, which was achieved in the Tokyo Round through disciplines on subsidies and through permissiveness in the use of contingent protection against imports; (4) bringing into the multilateral fold major developing countries as they became economically important and adding new areas such as intellectual property and services that had become sources of comparative advantage for the industrial countries, as achieved at the Uruguay Round by creating a greater symmetry of obligations between all members and by developing new rules on intellectual property and services; and (5) responding to the emergence of China as a big market access opportunity by securing unprecedentedly large policy liberalization by China in agriculture, manufacturing, and services, in the context of its WTO accession.

Having responded to China as an opportunity, the next major development on the trading horizon is China as a potential threat. A China Round is thus a natural for the WTO and one consistent with its history. It would mirror the Tokyo Round, which had as one of its main objectives the accommodation of Japan in a manner that minimized the risks to the system.

What might an agenda look like for a China Round? Mattoo and I (forthcoming) spell out a possible agenda in detail, which might potentially cover a number of items in which China's role will be crucial and where China might also have an interest in other countries opening their markets (for example, in government procurement) or in other countries committing not to restrict access to energy, food, and natural resources in a way that could help China. The aim would be to create a balanced package where China would have to "give" by way of liberalizing its own policies in return for others offering commitments of interest to China. The greater the number of China's partners that participate, the better the prospects that China would have an incentive to engage in it and the more the stigma for China if it were to distance itself from the exercise. A China Round could thus revitalize the multilateral trading system. It might not succeed but it must be tried.

to be one, reflected in the actions of China (for example, its mercantilist policies) to de facto depart from, or renege on, it. Perhaps one should pose the question as one of trying to "re-tether" China in the multilateral system.

There is a final appeal to the multilateralism proposed here, with its forswearing of promiscuous and hostile bilateralism. The discussion has been permeated of course by a sense of China as a target or a concern. But support by China itself for stronger multilateralism today might be in its interest as well, because it would be a strong and credible signal—a kind of precommitment—that China does not intend in the future to exercise the kind of dominance that could disrupt the current open and rules-based system that has served it so well over the past three decades. Strengthening multilateralism is in China's interest and the interest of its major trading partners.

Conclusion

An ascendant China might create new challenges for cooperation. As a dominant power, China will be increasingly beyond the influence of outsiders, especially on key issues such as exchange rates, climate change, and technological protectionism. Self-interest will, largely, rule. But the pursuit of self-interest need not augur badly for the open rules-based system that the world enjoys. China's unique features—especially the fact that it is one of history's most open superpowers—will invest it with a stake in broadly maintaining the current trade and financial system. And China's stake in market openness will be of primary importance because delivering development—the basis for the regime's legitimacy—is crucially predicated on markets remaining open.

The importance of trade for China going forward, the likelihood that China will exit from its mercantilism by internationalizing the renminbi, and the relative ineffectiveness of the IMF as a forum for cooperation between systemically important countries, makes it likely that engagement—and the scope for friction—between China and the other large economies will relate more to trade than macroeconomic issues. In turn, this will make the WTO not the IMF the key forum for and locus of cooperation between China and these economies.

The odds are strong that China will act to maintain the current open rules-based trading system. But history suggests that there are no guarantees and the world requires some insurance against the possibility that China exercises its dominance by either reversing its previous policies or failing to open areas of the economy that are now highly protected. If it were to do so, and given its size, the resulting conflict could undermine the post–World War II system.

The history of post–World War II relations between trading superpowers—the United States and European Union—suggests that cooperation can be successful. That success is based on the fact that key actors in the WTO engage in reciprocal market opening and share a sense of a fair bargain to which countries feel they must adhere. The broad success of the WTO dispute settlement process owes to this perception of an equitable contract between countries, which both creates the incentive to comply and confers legitimacy in governance.

Insofar as China shares this perception after its WTO accession—and the fact that it has benefited substantially from being part of this system—it is likely that China will participate in the WTO and sustain it much as the other superpowers did in the postwar period.

The difference between the past and future is the tension that might arise as a result of the uniqueness of China as a superpower. By virtue of its income level and the historic trajectory of its development, China remains less open in terms of policy barriers, especially in the nontraditional areas, than its major trading partners. But because of its distinctive development strategy it will also be an overwhelmingly large trader—much larger over time than the major partners—rendering it less susceptible to external influence.

So the United States and European Union, by virtue of being more open, will on their own be less able to engage in reciprocal market opening with China—which has been one of the keys to the success of the WTO system. And by virtue of China's size, they will be less able to influence China's policy regime. The inability of its trading partners to influence China and the temptation to try do so anyway—especially if the US economy continues to fare poorly and if perceptions of unfairness and asymmetric contributions to keeping the trading system gain serious ground—will remain a key structural tension.

One possible insurance policy that the world can take out is to keep China tethered to the multilateral trading system, so that it would be politically difficult, and economically and reputationally costly, for China to depart from or undermine the multilateral system even once it becomes dominant.

But anchoring China in the multilateral system would require all its major trading partners—not just the United States—to become more reticent about bilateral trade deepening. This reticence should extend not just to deepening bilateral relations with China but perhaps also to trade relations with each other. China's trading partners must avoid both the temptations of a promiscuous bilateralism and a hostile regionalism. The impediments to taking out the insurance of multilateralism are going to be considerable. China's trading partners must first recognize the seriousness of the looming challenges and act now, even though those challenges may seem distant. They must resist the lure of bilateral agreements that might offer short-term gains but which might leave them exposed to China in the long run. And domestic institutions and habits may need to be adapted to successfully forge a coalition to revitalize multilateralism. China, in short, might be the raison d'être for a new multilateralism. But making that multilateralism a reality will be far from easy.