

## **Under pressure: the end of free trade as we know it and the future of the liberal order**

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### Abstract

Liberal internationalism is based on four elements: democracy, free trade, collective security, and American leadership. Together, they represent the building blocks of global peace – at least, this was the view of Woodrow Wilson after WWI. The most institutionalized form of the liberal economic order was designed at Bretton Woods in 1944 and has been in place ever since. However, the American-led economic order is increasingly being questioned and challenged. This paper looks at the ‘free trade’ component of Wilsonianism, which is currently under threat from rising protectionism and the return of mercantilism.

The apparently declining support of free trade in global politics originates in two currently interrelated dynamics. On the one hand, neo-liberal hyperglobalization – through the widespread diffusion of global value chains – has changed the nature of international trade, which is having a deeper impact on domestic societies and generating a populist backlash. On the other hand, a relatively declining United States seems reluctant to keep offering free trade as a public good while feeling threatened by a rising China. Can the global free trade regime survive without American leadership? What are the implications for the sustainability of the liberal order? The paper argues that the future of free trade as a pillar of liberal internationalism depends on (i) readdressing the excesses of globalization and (ii) engaging China as a contributor to a redesigned liberal order in tune with 21<sup>st</sup>-century challenges.

### **Introduction**

In the novel *The Bridge on the Drina* by Nobel Prize-winning author Ivo Andrić, a lady owns an inn on the border between Bosnia and Serbia. Her business, located along trade routes connecting Central Europe to the Balkans, is thriving as merchants, travelers, and all sorts of adventurers stop overnight. Gradually, however, as 1914 approaches, business slows down, and there are diminishing cross-border flows of people, goods, and services. She watches helplessly as her entire world collapses into misery and, ultimately, conflict, and she cannot understand the irrationality of humankind, which is apparently ready to swap wealth and peace for poverty and war. With the repeal of the Corn Laws in England in 1848, which had opened up the British market to agricultural imports, and the 1860 Cobden–Chevalier Treaty, which gave British manufacturers access to the French market, Europe had in fact ushered in a ‘golden age’ of free trade and prosperity. This ‘belle époque’ of free trade declined when industrial production slowed down and international competition became fierce. One by one, European states – with the lone exception of England – raised tariffs and embraced protectionist policies: The shaky Austro-Hungarian Empire was the first

to do so in 1876. Italy and Germany followed suit in 1878 and 1879, respectively, and France immediately retaliated by putting up restrictions<sup>1</sup>.

Once WWI was over, Woodrow Wilson came to believe that this move toward protectionism had significantly contributed to pushing Europe into a previously unprecedented large-scale conflict that few really wanted or expected<sup>2</sup>. Therefore, free trade was third on the list of his Fourteen Points, which he laid out for Congress in January 1918 as the basis for sustainable peace: ‘the removal, so far as possible, of all economic barriers and the establishment of an equality of trade conditions among all the nations consenting to the peace and associating themselves for its maintenance’<sup>3</sup>. Economic openness is an integral part of Wilson’s political vision, according to which ‘free trade and socioeconomic exchange have a modernizing and civilizing effect on states, undercutting tyranny and oligopoly and strengthening the fabric of international community’<sup>4</sup>. Thus, this economic pillar was strictly connected to the other five ideas that, according to John Ikenberry, give shape to Wilsonianism: a community of democratic states as the foundation of peace, a rules-based system revolving around international law and international organizations, a collective security ‘sustained by commitments to arms control and disarmament, self-determination, and freedom of seas’, the idea that a new order was coming because ‘the world was in the midst of a major democratic revolution,’ and, finally, the guiding role played by the United States, which had almost a missionary quality to it, since for Wilson, ‘America was the great moral agent in history’<sup>5</sup>. Crucially, these five ideas are all meant to be interconnected, and any variation in the implementation of one of them has a rippling effect on the feasibility of all the others.

Wilsonianism (or, in other words, liberal internationalism) can, in fact, be shaped like a diamond with four sides: democratic government, free trade, collective security, and American leadership<sup>6</sup>. As democracies tend to cooperate, they engage in economic openness, which in turn fosters the need to build institutions of collective security that are regulated by international law – all covered and protected by ‘an America that willingly assumes the responsibilities of leadership of a community of nations pledged to peace [...], even if this means going to war to preserve it’<sup>7</sup>. These four elements jointly create a distinctive unity, a diamond of unique shining brilliance: ‘*for the promise of this unity is mutual defense and peace*, which no aspect alone can be expected convincingly to deliver, but whose possible establishment, thanks to the interaction of these various developments, is the prime tenet of liberalism’s secular faith’<sup>8</sup>. Of this faith, then, trade is just one component, albeit a fundamental one, which cannot guarantee peace and security on its own. The

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<sup>1</sup> Ann Capling and Silke Trommer, *The Evolution of the Global Trade Regime*, in John Ravenhill, *Global Political Economy*, 5<sup>th</sup> edition, Oxford, Oxford University Press, 2017, pp. 111-40, p. 114.

<sup>2</sup> Christopher Clark, *The Sleepwalkers: How Europe Went to War in 1914*, London, Penguin Books, 2013: trad. it., *I Sonnambuli. Come l’Europa arrivò alla Grande Guerra*, Bari, Laterza, 2016.

<sup>3</sup> Quoted in G. John Ikenberry, *Introduction: Woodrow Wilson, the Bush Administration, and the Future of Liberal Internationalism*, in G. John Ikenberry, Thomas J. Knock, Anne-Marie Slaughter and Tony Smith, *The Crisis of American Foreign Policy: Wilsonianism in the Twenty-first Century*, Princeton and Oxford, Princeton University Press, 2009, pp. 2-24, p. 11.

<sup>4</sup> *Ibid.*

<sup>5</sup> *Ivi*, p. 13.

<sup>6</sup> Tony Smith, *Why Wilson Matters: The Origin of American Liberal Internationalism and Its Crisis Today*, Princeton, NJ, Princeton University Press, 2017, p. 12.

<sup>7</sup> *Ibid.*

<sup>8</sup> *Ibid.*

liberal promise – drawing on the Enlightenment vision<sup>9</sup> and philosophical works like Immanuel Kant’s ‘perpetual peace’<sup>10</sup> – can be truly fulfilled only when all four elements stick together in a single piece, each with its own functions and *raison d’être*. Democratic states, supported by the middle class, which has a strong stake in free trade, are inherently against protectionism, and in order to defend economic openness and collaboration they create a system of collective security through international organizations with the help of a liberal hegemon ready to pay for public goods (the third section will elaborate on this point). But if democracies work improperly, countries return to tariffs and quotas in international trade, international institutions are weakened by uncooperative states, or the United States ceases to play its hegemonic role, the entire promise becomes less credible and the liberal mission harder to accomplish<sup>11</sup>.

This article looks at how the economic pillar of Wilsonianism evolved throughout the 20<sup>th</sup> century, effectively became the intellectual foundation of the global political economy after WWII, and is now suffering neo-mercantilist counterattacks that threaten the very foundations of the liberal order. Section one retraces the intellectual origins of economic Wilsonianism and outlines how, for classical liberalism, free and open markets are sources of prosperity, stability, and peace among nations. Section two lays out how economic liberalism was put into practice after WWII under the benevolent American hegemony and how it evolved when neo-liberalism became the dominant narrative in global economy. Section three explains how the menace of Sino-US trade wars (a consequence of the spectacular economic rise of China) has undermined the sustainability of the liberal order. Some concluding remarks address the issue of the complexity of the relationship between free trade and peace in the 21<sup>st</sup> century.

### **Classical economic liberalism as the intellectual origin of Wilsonianism**

In the 18<sup>th</sup> and 19<sup>th</sup> centuries, liberal philosophers debated the pacifying effect of trade and juxtaposed it with the ‘jealousy of trade,’ which, according to the mercantilists, was behind

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<sup>9</sup> Béla Kapossy, Isaac Nakhimovsky, and Richard Whatmore (eds), *Commerce and Peace in the Enlightenment*, Cambridge, Cambridge University Press, 2017. As evidence of the enlightened triumph of reason, *The Economist*, a British newspaper founded in 1843 and a media of reference for liberals, proudly states on the content page of every issue that it takes part in “a severe contest between intelligence, which presses forward, and an unworthy, timid ignorance obstructing our progress”.

<sup>10</sup> Immanuel Kant, *On Perpetual Peace: A philosophical sketch*, Arlington, VA, 1795/2012: trad. it., *Per la Pace Perpetua*, Milano, Feltrinelli, 2013; Michael W. Doyle, *Kant, Liberal Legacies, and Foreign Affairs*, in “Philosophy and Public Affairs”, 12 (3), 1983, pp. 205-35; Id., *Kant, Liberal Legacies, and Foreign Affairs, part 2*, in “Philosophy and Public Affairs”, 12 (4), 1983, pp. 323-53. See also Norman Angell, *The Great Illusion: A Study of the Relation of Military Power to National Advantage*, London, Heinemann, 1912: trad. it., *La grande illusione. Studio della Potenza militare in rapporto alla prosperità della nazione*, Casa Editrice Humanitas, Roma, 1913; Joseph Schumpeter, *Capitalism, Socialism and Democracy*, New York, Harper Torchbooks, 1950: trad. it., *Capitalismo, Socialismo e Democrazia*, Milano, Etas, 2001. For a difference between liberal pacifism, liberal imperialism, and liberal internationalism, see Michael W. Doyle, *Liberalism and World Politics*, in “American Political Science Review”, 80 (4), 1986, pp. 1151-69.

<sup>11</sup> Woodrow Wilson (himself the child and grandchild of a Presbyterian priest) has been constantly attacked by both realists and left-leaning constructivists for the allegedly ‘missionary’ quintessence of his ideas. This family and cultural background infused Wilson with a strong Protestant moral ethic: Tony Smith, *cit.*, p. 20.

economic wars<sup>12</sup>. For mercantilists like Bernard Mandeville and Thomas Mun<sup>13</sup>, trade was meant to accumulate wealth for the nation in the form of gold and silver reserves obtained through a permanent surplus of the balance of payments. According to them, trade is a zero-sum game: Countries with a trade surplus are the winners (they enrich their coffers by making the rest of the world buy their goods), and countries with a trade deficit are the losers (they need to import merchandise from abroad and become dependent on other countries' products). Liberals do not share this view of trade and argue, instead, that trade among nations is a win-win solution because it makes every country better off in absolute terms. They draw from the pioneering work of David Ricardo, whose name has gone down in history for his formulation of the law of comparative advantage. Ricardo showed how trade allows countries – because of their factor endowment – to specialize in the production of those goods that they can produce relatively more efficiently while importing all the rest. In his most famous example, it was more productive for England to manufacture textiles and clothing in its Manchester factories while importing wine from Portugal than to divert resources from this industry to set up implausible vineyards on the British Isles<sup>14</sup>. Thus, as a result of trade specialization (in the example, Portugal specialized in wine and Great Britain in clothing and, later, trade), the world economy as a whole would become more efficient and increase global welfare, with no waste of resources whatsoever<sup>15</sup>. This is why liberals are skeptical of laws and regulations restricting trade and giving undue protection to domestic producers. Adam Smith, who is probably one of the best-known classical liberals, even drew a social and anthropological comparison: 'It is the maxim of every prudent master of a family, never to attempt to make at home what it will cost him more to make than to buy [...] What is the prudence in the conduct of every private family, can scarce be folly in that of a great kingdom.'<sup>16</sup> In fact,

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<sup>12</sup> 'What Hume had called "jealousy of trade", in an essay of 1758, was identified as an intensification of earlier, purely political, antagonism – or jealousy – between states. Economic war was becoming a permanent condition': Béla Kapossy, Isaac Nakhimosky, and Richard Whatmore, *Introduction: Power, Prosperity, and Peace in Enlightenment Thought*, in Béla Kapossy, Isaac Nakhimosky, and Richard Whatmore (eds), *cit.*, p. 5, quoting David Hume, *Essays, Moral, Political, Literary*, Indianapolis, Liberty Fund, 1987. See also Istvan Hont, *Jealousy of Trade: International Competition and the Nation-State in Historical Perspective*, Cambridge, Cambridge University Press, 2015. On how differently realists, liberals, and socialists look at the politics of peace and war in general, see Michael W. Doyle, *Ways of War and Peace*, New York and London, W.W. Norton & Company, 1997.

<sup>13</sup> Bernard Mandeville, *The Fable of the Bees; Or, Private Vices, Public Benefits*, Edinburgh, W. Gray and W. Peter, 1714/175: trad. it., *La Favola delle Api*, Bari, Laterza, 2008; Thomas Mun, *England's Treasure by Forraign Trade*, Oxford, Basil Blackwell, 1664/1928.

<sup>14</sup> David Ricardo, *On Foreign Trade and the Benefits to be Derived from Free Trade*, excerpts from *On the Principles of Political Economy and Taxation*, 1817: trad. it., *Principi di economia politica e dell'imposta*, UTET, Torino, 2006, reprinted in Ernest K. Bramsted and K.J. Melhuish, *Western Liberalism: A History in Documents from Locke to Croce*, Longman, London and New York, 1978, pp. 310-14.

<sup>15</sup> See also John Stuart Mill, *Of International Trade*, excerpt from *Principles of Political Economy with Some of Their Applications to Social Philosophy*, London, 1848: trad. it., *Principi di economia politica*, Torino, UTET, 2006, reprinted in Darel E. Paul and Abba Amawi (eds), *The Theoretical Evolution of International Political Economy: A Reader*, Oxford, Oxford University Press, 2013, pp. 76-79.

<sup>16</sup> Adam Smith, *Of Restraints Upon the Importation from Foreign Countries of Such Goods as Can Be Produced at Home*, excerpts from *The Wealth of Nations*, New York, NY: Modern Library, 1776/1937: trad. it., *La ricchezza delle nazioni*, Torino, UTET, 2017, reprinted in Darel E. Paul and Abba Amawi (eds), *The Theoretical*

liberals' faith in individual rationality would make them believe in the superior efficiency of private property, which is the main structural feature of capitalism.

There is another difference between mercantilism and classical liberalism. While mercantilists think that states are the relevant actors in the world economy, and balance-of-power considerations are paramount, liberals would argue that individual merchants and companies are the driving force of a nation's well-being. Moreover, as their business and profits depend on free trade, they have an incentive to sustain peace among nations. The costs of a disruptive conflict would be incommensurably high: 'it is commerce which is rapidly rendering war obsolete, by strengthening and multiplying the personal interests which are in natural opposition to it'<sup>17</sup>. By putting up barriers and tariffs, those costs would decrease, thereby increasing the risk of war. Therefore, 'commerce is the grand panacea,' also because ideas, good practices, and political models travel with trade: 'not a bale of merchandise leaves our shores, but it bears the seeds of intelligence and fruitful thought to the members of *some less enlightened community* (italics are mine); not a merchant visits our seats of manufacturing industry, but he returns to his own country the missionary of freedom, peace, and good government'<sup>18</sup>. Cobden's words reveal classical liberals' faith not only in enlightened reason but also in a British *civilizational superiority* that they consider worth spreading the world over. The idea that trade had a civilizational mission and was a source of progress in itself can also be found in John Stuart Mill's reflections: 'commercial adventurers from more advanced countries have generally been the first civilizers of barbarians'<sup>19</sup>. As we will see in the final remarks, this Anglo-Saxon legacy makes the sustainability of (Western) liberalism all the more problematic today.

Merchants would be the most fervent supporters of the rationality of peace since they are the first beneficiaries of cooperation. Nations wage wars for many reasons that are often based on wrong perceptions of their self-interest: 'these prejudices, passions, and false ideas can only disappear by degrees, with the progress of enlightenment and international trade'<sup>20</sup>. This reasoning is based on the view that commerce in itself, as a mutually beneficial activity for the parties involved, conveys the need to pursue common interests, to set aside differences, and to 'soften down feuds between nations'<sup>21</sup>. Thus, human interaction through trade becomes the rational foundation for peace: 'what insulates men disposes to war, whatever brings them into relation with each other inclines them to peace. And nothing tends to secure such intimate relations between nations as commerce'<sup>22</sup>. This optimistic view stands in stark contrast to the pessimism of mercantilists like

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*Evolution of International Political Economy: A Reader*, Oxford, Oxford University Press, 2013, pp. 58-64, p. 60.

<sup>17</sup> John Stuart Mill, *cit.*, p. 79. See also Baron De Montesquieu, *The Spirit of Laws*, New York, Hafner, 1748/1949, p. 316: trad. it., *Lo spirito delle leggi*, Milan, BUR; 1989; quoted in Han Dorussen and Hugh Ward, *Trade Networks and the Kantian Peace*, in "Journal of Peace Research", 47 (1), 2010, pp. 29-42, p. 31.

<sup>18</sup> Richard Cobden, *Commerce is the Grand Panacea*, 1835, reprinted in Ernest K. Bramsted and K.J. Melhuish, *Western Liberalism: A History in Documents from Locke to Croce*, Longman, London and New York, 1978, pp. 354-57, p. 356.

<sup>19</sup> John Stuart Mill, *cit.*, p. 79.

<sup>20</sup> Emile De Laveleye, *On the Causes of War, and the Means of Reducing their Number*, 1872, reprinted in Ernest K. Bramsted and K.J. Melhuish, *Western Liberalism: A History in Documents from Locke to Croce*, Longman, London and New York, 1978, pp. 379-83, p. 379.

<sup>21</sup> *Ivi*, p. 380.

<sup>22</sup> *Ibidem*. See also John Stuart Mill, *cit.*, p. 79.

Johann Fichte, who denies Kant's 'unifying function' of commerce because 'commercial interests were too heavily implicated in the unstable power dynamics of the European states system', with the result that market relations reflected a 'Hobbesian state of war'<sup>23</sup>. De Laveleye, however, acknowledged that wars are often an outcome of unsettled disputes that might arise in international trade. But he had a solution for this, too. In order to reduce the risk of war, and in tune with Kantian logic, he became a firm advocate of establishing an International Court of Arbitration: According to classical liberals, international law, international organizations, and the judicial settlement of conflicts are an essential component of global order. This is a theme that would become central to Woodrow Wilson's perspectives on collective security.

Finally, we should end here with a specific remark to temper the image of classical liberals as insensitive to the human cost of unfettered markets. Even Adam Smith, whose thought has been vulgarized in the slogan of the 'invisible hand of the market,' is cautious about this. For example, whenever (for reasons related to restrictions on the import of foreign goods) domestic manufacturers have grown so much that they employ a great number of workers, 'humanity may in this require that the freedom of trade should be restored only by slow gradations, and with a good deal of reserve and circumspection'<sup>24</sup>. Because, 'were those high duties and prohibitions taken away all at once, cheaper foreign goods of the same kind might be poured so fast into the home market, as to deprive all at once many thousands of our people of their ordinary employment and means of subsistence'<sup>25</sup>. Therefore, according to liberals, trade at the *individual level* does produce losers – in principle, these people are employed in import-competing industries<sup>26</sup>. Although this reasoning would indeed form the basis of all anti-dumping regulations the world has become familiar with, the broad lesson of making open markets compatible with the well-being of the domestic workforce would easily be forgotten in the economic neo-liberalism that would come to dominate the latter part of the 20<sup>th</sup> century.

### **From Bretton Woods to neo-liberalism**

After WWI, the trade protectionism that Wilson regarded as one of the causes of the conflict was not reversed – quite the opposite. The Smoot–Hawley Act of 1930 raised US duties to unprecedented levels and precipitated a downward spiral of retaliation in global trade – in fact, by the mid-1930s, it would fall 'by about two-thirds'<sup>27</sup>. It was only with the Reciprocal Trade Agreements of 1934, which transferred the power to increase or lower tariffs from the Congress to President Franklin Delano Roosevelt, that a new era of trade liberalization appeared on the horizon. Before WWII started, the US had put in place 21 free trade agreements, which would lay the groundwork for the post-war international trade regime<sup>28</sup>. At the Bretton Woods Conference in

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<sup>23</sup> Béla Kapossy, Isaac Nakhimovsky, and Richard Whatmore, *Introduction, cit.*, p. 12, in reference to the work of Johann G. Fichte, *The Closed Commercial State*, New York State University Press, Albany, NY, 2013: trad. it., *Lo Stato Commerciale Chiuso*, Padova, Edizioni di AR, 2009.

<sup>24</sup> Adam Smith, *cit.*, p. 64.

<sup>25</sup> *Ibid.*

<sup>26</sup> Dani Rodrik, *Populism and the economics of globalization*, in "Journal of International Business Policy", 1 (1), 2018, pp. 12-33, p. 14.

<sup>27</sup> Ann Capling and Silke Trommer, *cit.*, p. 115.

<sup>28</sup> *Ibid.*

1944, the US and its allies set up the International Monetary Fund and the International Bank of Reconstruction and Development (World Bank), but it was only in 1948 that they signed an agreement establishing the International Trade Organization (ITO). However, the ITO never came into existence, as the US Congress failed to sign the treaty – evidence, once more, of the representatives’ sensitivity to the matter. Countries fell back on the General Agreement on Tariffs and Trade (GATT), a set of trade rules based on principles of reciprocity and non-discrimination aimed at de-politicizing trade issues, which had been signed in 1947<sup>29</sup>. Signatories to the GATT would commit to reducing tariffs through several negotiating rounds, one of which (the Uruguay Round) ended in 1993 with the transformation of GATT into a proper institution, the World Trade Organization (WTO), which now has near-universal membership<sup>30</sup>. The round also extended the scope of the trade regime to services, agriculture, and some trade-related aspects of investment and intellectual property rights. Furthermore, it included provisions on technical barriers to trade, as well as sanitary and phytosanitary measures, which started to interfere more with domestic legislation, thus contributing to the (re-)politicization of international trade issues<sup>31</sup>. Some authors have argued that the increasing scope of the global trade regime centered on the WTO stimulated greater social resistance to free trade<sup>32</sup>.

The entire Bretton Woods system was based on a compromise between international liberalization and the need for states to intervene in the economy in case market forces disrupted the economic fabric of society. It was a qualified liberalism as liberalization was ‘embedded’ in national economic policies that prioritized domestic economic growth and full employment<sup>33</sup>. The aim of this liberalism was to avoid the trade protectionism that had become so widespread in the 1930s. But qualifying it also meant learning from the shortcomings of the pre-WWI gold standard, when the fixed exchange rate system was guaranteed by a balance of payments adjustments via domestic price changes. In fact, the consequent downward pressure on salaries forced by the logic of the system, at a time of social upheavals and the democratic extension of universal suffrage, made the gold standard politically unsustainable. It resumed after WWI but was definitively abandoned in 1931. John Maynard Keynes, one of the main architects of the Bretton Woods system<sup>34</sup>, had previously noted that those ‘fundamental truths’ of 19<sup>th</sup>-century liberalism could no longer function ‘as a working political theory’ in the 20<sup>th</sup> century<sup>35</sup>. Thus, the monetary

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<sup>29</sup> *Ivi*, p. 117.

<sup>30</sup> The WTO currently has 164 member states.

<sup>31</sup> On the politicization of trade, in the case of the North American Free Trade Agreement, and of the European Union, respectively, see for instance: Tamara Kay and R.L. Evans, *Trade Battles: Activism and the Politicization of International Trade Policy*, Oxford, Oxford University Press, 2018; Alasdair R. Young, *Two wrongs make a right? The politicization of trade policy and European trade strategy*, in “Journal of European Public Policy”, 26 (12), 2019, pp. 1883-99.

<sup>32</sup> Arlo Poletti and Dirk De Bièvre, *Judicial Politics and International Cooperation*, London, ECPR Press, 2016.

<sup>33</sup> John G. Ruggie, *International Regimes, Transactions, and Change: Embedded Liberalism in the Postwar Economic Order*, in “International Organization”, 36 (2), 1982, pp. 379-415.

<sup>34</sup> The rivalry between the United Kingdom and the United States inflamed discussions at negotiations at Bretton Woods, the New Hampshire town where delegates from 44 nations convened in July 1944: Benn Steil, *The Battle of Bretton Woods: John Maynard Keynes, Harry Dexter White, and the Making of a New World Order*, Princeton, NJ, Princeton University Press, 2013: trad. it., *La Battaglia di Bretton Woods. John Maynard Keynes, Harry Dexter White e la Nascita di un Nuovo Ordine Mondiale*, Roma, Donzelli Editore, 2019.

<sup>35</sup> John M. Keynes, *National Self-Sufficiency*, in “Yale Review”, 22 (4), 1933, pp. 755-69, p. 755 and p. 757, quoted in Isaac Nakhimovsky, *The Closed Commercial State: Perpetual Peace and Commercial Society From*

arrangements accompanying the birth of the IMF left capital controls in the hands of governments, which were allowed to adjust the fixed exchange rate (to the dollar) in case a country faced a 'fundamental disequilibrium'<sup>36</sup>. In trade, evidence of embedded liberalism can be found in all sorts of safeguard clauses in the GATT system, allowing states to put up temporary restrictions in the case of balance-of-payments imbalances or specific sector difficulties<sup>37</sup>.

At the beginning of the 1970s, the entire Bretton Woods system started to unravel, and embedded liberalism came under attack. Following the 1971 'Nixon shocks,' when the US unpegged the dollar from gold, the United States (in 1974) and the United Kingdom (in 1979) liberalized international private capital movements, first and foremost to attract the huge financial flow of 'petrodollars' generated in oil-producing countries during the two oil crises of that decade. A neo-liberal movement, as well as coordination problems among industrialized countries<sup>38</sup>, was behind these policies and turned classical liberals' faith into an absolute dogma trusting 'individual choice' and 'markets' as the most efficient instruments to allocate capital efficiently and impose 'an external discipline on governments pursuing inflationary or fiscally unsustainable policies'<sup>39</sup>. Free market fundamentalism spread to both industrialized and developing countries as many governments, fearful of experiencing destabilizing capital flights, started to deregulate their economies and adopt market-friendly, capital-attracting policies. Both domestically and internationally, the institutions that had to limit, contain, and constrain the excesses of financial markets were 'retreating'<sup>40</sup>.

The abandonment of the Bretton Woods system was not without domestic consequences for the states. The embedded liberalism that sustained it was rooted in a *basic bargain*, a social compact based on a virtuous cycle of production, consumption by the middle class and by workers receiving a salary in line with productivity, and consequently, enough savings to finance investments, which in the end made everyone better off<sup>41</sup>. Neo-liberalism brought this cycle to an end, thus (at the end of the Cold War) leading to the 'shipwreck' of the liberal order because it disowned a pact between capitalism and democracy about mutual corrections of each other's imperfections and shortcomings – as capitalism puts a premium on efficiency, which generates inequalities, while democracy is based on the principle of equality<sup>42</sup>.

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Rousseau to Fichte, Princeton, NJ, Princeton University Press, 2011, p. 3. Keynes had also been a fierce critic of the Treaty of Versailles, which had imposed excessive punishments on Germany: John M. Keynes, *The Economic Consequences of the Peace*, New York, Harcourt, Brace, and Howe, 1920: trad. it, *Le Conseguenze Economiche della Pace*, Milano, Adelphi, 2007.

<sup>36</sup> Eric Helleiner, *The Evolution of the International Monetary and Financial System*, in John Ravenhill, *cit.*, pp. 199-224, p. 204.

<sup>37</sup> Ann Capling and Silke Trommer, *cit.*, p. 118.

<sup>38</sup> For a theoretical discussion of coordination problems in dealing with public goods' provision, see Vinod K. Aggarwal and Cédic Dupont, *Goods, Games, and Institutions*, in "International Political Science Review", 20 (4), 1999, pp. 393-409.

<sup>39</sup> Eric Helleiner, *cit.*, p. 207.

<sup>40</sup> Susan Strange, *The Retreat of the State: The Diffusion of Power in The World Economy*, Cambridge, Cambridge University Press, 1996: trad. it., *Chi Governa l'Economia Mondiale? Crisi dello Stato e Dispersione del Potere*, Bologna, Il Mulino, 1998; Susan Strange, *Casino Capitalism*, Oxford, Oxford University Press, 1986.

<sup>41</sup> Vittorio Emanuele Parsi, *Titanic: Il naufragio dell'ordine liberale*, Bologna, Il Mulino, 2018, p. 58, quoting Robert B. Reich, *Aftershock: The Next Economy and the American Future*, New York, Knopf Doubleday Publishing Group, 2010: trad. it., *Aftershock. Il future dell'economia dopo la crisi*, Milano, Fazi, 2010.

<sup>42</sup> *Ibid.* See also Vittorio Emanuele Parsi, *La fine dell'uguaglianza. Come la crisi economica sta distruggendo il primo valore della nostra democrazia*, Milano, Mondadori, 2012.



An extreme version of globalization, which was the product of the unfettered liberalization of financial markets, trade, and investments, broke the alliance between capitalism and democracy. National governments started to forget Karl Polanyi's lesson that states and markets are inextricably linked in capitalist societies<sup>43</sup>. This generated Dani Rodrik's famous trilemma: In a triangle between hyperglobalization, the nation-state, and democratic politics, you can simultaneously have any two of the three, but it is impossible to have all three in place at the same time<sup>44</sup>. You can combine the nation-state with hyperglobalization, but in that case you have to restrict democracy in a 'golden straitjacket' (much like what happened during the age of the gold standard at the beginning of the 20<sup>th</sup> century); in a system of nation-states and democratic politics, you have to 'limit globalization' (much like in the Bretton Woods compromise); and finally, you can 'globalize democracy' (making the global economic sphere coincide with a global polity) by giving up on national sovereignty<sup>45</sup>. Hyperglobalization, in other words, corroded the iron chains that had kept the four elements of Wilsonianism together. And when markets were completely freed in the late 1980s and 1990s, they grew so much as to dominate politics and dictate their rules. Economic openness was no longer a source of stability and progress but became a destabilizing factor: By resorting to short-time capital movements of speculative nature, financial actors could, in fact, threaten the 'exit'<sup>46</sup> from states that would not adopt market-friendly policies, aimed at domestic deregulation and liberalization, in line with the script of the 'Washington Consensus'<sup>47</sup>. The political-economic compact in democratic societies also started to unravel due to rising inequality and because the policies enriched capital at the expense of labor<sup>48</sup>. The Great Recession of 2007–2008, which, unlike the peripheral financial crises of the previous decade, had originated in Wall Street, at the core of the liberal system, was the last straw and precipitated 'the crisis of capitalist democracy'<sup>49</sup>.

Neo-liberalism also had a systemic effect on the globalization of production. The liberalization of trade and financial flows led to a massive surge in foreign direct investment (FDI).

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<sup>43</sup> Karl Polanyi, *The Great Transformation. The Political and Economic Origins of Our Time*, Boston, MA, 1957: trad. it., *La Grande Trasformazione*, Torino, Einaudi, 2000.

<sup>44</sup> Dani Rodrik, *The Globalization Paradox: Democracy and the Future of the World Economy*, New York, NY, W.W. Norton & Company, 2011: trad. it., *La globalizzazione intelligente*, Bari, Laterza, 2015, p. 201.

<sup>45</sup> *Ivi*, p. 200.

<sup>46</sup> Albert O. Hirschman, *Exit, Voice, and Loyalty: Responses to Decline in Firms, Organizations, and States*, Cambridge, MA: Harvard University Press, 1970, trad. it. *Lealtà, defezione, protesta. Rimedi alla crisi delle imprese, dei partiti e dello Stato*, Bologna, Il Mulino, 2017.

<sup>47</sup> The economist John Williamson coined the term 'Washington Consensus' to describe the policy directives that the IMF, the World Bank, and the US Treasury would suggest to both developing and developed countries, all of which were based on neo-liberal principles advancing unfettered markets: John Williamson, *What Washington Means by Policy Reform*, in John Williamson (ed.), *Latin American Adjustment: How Much Has Happened?*, Washington (DC), Institute for International Economics, 1990.

<sup>48</sup> Vittorio Emanuele Parsi, *La fine dell'uguaglianza*, cit.; Thomas Piketty, *Capital in the Twenty-First Century*, Cambridge, MA, The Belknap Press of Harvard University Press, 2014: trad. it., *Il capitale nel XXI secolo*, Milano, Bompiani, 2018; Joseph Stiglitz, *Freefall: America, Free Markets, and the Sinking of the World Economy*, New York, W.W. Norton & Company, 2010: trad. it. *Bancarotta. L'economia mondiale in caduta libera*, Torino, Einaudi, 2014; Joseph Stiglitz, *The Great Divide: Unequal Societies and What We Can Do about them*, New York, W.W. Norton & Company, 2016: trad. it., *La Grande Frattura. La disuguaglianza e i modi per sconfiggerla*, Torino, Einaudi, 2017.

<sup>49</sup> Richard A. Posner, *The Crisis of Capitalist Democracy*, Cambridge, MA, Harvard University Press, 2010: trad. it., *La crisi della democrazia capitalista*, Milano, Università Bocconi Editore, 2014.

UNCTAD<sup>50</sup> data shows that, between 1982 and 2008, ‘FDI flows (in current prices) increased from \$59 billion to 1,697 billion’ and ‘the ratio of world FDI inflows to global gross domestic capital formation (a measure of domestic investment) increased from 2 per cent [...] to 12.3 per cent [...]’<sup>51</sup>. The removal of trade and investment barriers, in fact, allowed multi-national companies (MNCs) to fragment the manufacturing process in several phases in different geographical locations. Components were produced and exported to other countries, either for final assembly or to add some value and re-export them. Global value chains (GVCs) became so complex that components were sometimes crossing borders several times before ending up in the final product<sup>52</sup>. In 2008, MNCs and their affiliates ‘accounted for one-third of total world exports of goods and services’<sup>53</sup>. Trade and investment, then, have become closely linked, and nations have competed to attract MNCs by adopting neo-liberal market-friendly policies – actually, states’ ‘competitive advantage’ came to be seen as more important than Ricardo’s ‘comparative’ endowment of nations<sup>54</sup>. In fact, while short-term speculative capital movements could generate shocks to foreign exchange reserves and to the balance of payments, long-term FDI (or its absence) could determine a country’s industrialization and growth path<sup>55</sup>. On the one hand, it could be said that, all in all, the Ricardian logic of factor endowment still holds as MNCs would invest in low-end manufacturing in labor-abundant (usually developing) countries, while they would invest in capital-intensive activities in developed countries, thereby maximizing – on aggregate – global efficiency. On the other hand, MNCs’ investment decisions could instead be based on systemic reflections on the appropriate governance of GVCs *for a specific product*, aim for internal (profit-maximizing) efficiency, and take into account the entire complexity of inter-firm and intra-firm transactions, how this complexity can be codified, and the available skills of suppliers<sup>56</sup>.

This new stage of globalization has been made possible by the spread of information and communication technologies (ICT). Technology-driven GVCs are more disruptive than trading in final goods because ICT, unlike tariffs, ‘cannot be controlled or slowed’<sup>57</sup>. In addition, MNCs would tend to directly control innovation and design, as well as marketing and after-sales services (the initial and final stages of GVCs), capturing the highest added value while outsourcing to suppliers manufacturing assembly activities, which is where the added value is the lowest<sup>58</sup>. These activities, which can be transferred easily from one location to another, tend to be concentrated in emerging

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<sup>50</sup> United Nations Conference on Trade and Development.

<sup>51</sup> Eric Thun, *The Globalization of Production*, in John Ravenhill, *cit.*, pp. 174-195, p. 176.

<sup>52</sup> Gary Gereffi and Miguel Korzeniewicz (eds), *Commodity Chains and Global Capitalism*, Westport, CT, Praeger, 1994.

<sup>53</sup> Eric Thun, *cit.*, p. 175, quoting UNCTAD data.

<sup>54</sup> Michael Porter, *The Competitive Advantage of Nations*, Macmillan, London, 1990: trad. it., *Il vantaggio competitivo delle nazioni*, Mondadori, Milano, 1991.

<sup>55</sup> On the importance for countries to establish a national institutional framework conducive to the attraction of FDI see for instance: OECD, *Foreign Direct Investment for Development: Maximising Benefits, Minimizing Costs*, Paris, OECD, 2002. Online: <https://www.oecd.org/investment/investmentfordevelopment/1959815.pdf>, accessed 25/11/2019.

<sup>56</sup> Gary Gereffi, John Humphrey, and Timothy Sturgeon, *The Governance of Global Value Chains*, in “Review of International Political Economy”, 12 (1), 2005, pp. 78-104.

<sup>57</sup> Richard Baldwin, *Misthinking Globalisation: Twentieth-Century Paradigms and Twenty First-Century Challenges*, in “Australian Economic History Review”, 54 (3), 2014, pp. 212-19, p. 215.

<sup>58</sup> Ram Mudambi, *Location, control and innovation in knowledge-intensive industries*, in “Journal of Economic Geography”, 8, 2018, pp. 699-725.

countries, thus leaving workers in developed countries with a sense of dispossession and impotence. The diffusion of GVCs has also been helped by the development of industrial capacity in key countries in East Asia: Japan in the 1960s and 1970s and Hong Kong, Singapore, Korea, and Taiwan (newly industrializing countries, or NICs) in the following decades. Especially Japanese investments in the NICs were crucial in triggering the fragmentation of production across Asia<sup>59</sup>.

There is another aspect complicating matters even further. As GVCs multiply trade flows, more workers are affected in some (often unknown) measures by international trade, creating winners and losers, not within sectors (as Ricardian logic would predict) or at the skills level but 'at the stage of production level'<sup>60</sup>. In other words, GVCs have 'de-nationalized' the comparative advantage, and 20<sup>th</sup>-century policies designed by governments to compensate losers are no longer effective as they are based on 'sectors/skills distinctions [which] are missing much the pain caused to citizens'<sup>61</sup>. In fact, welfare state provisions can be seen as a compensation mechanism for the losers from an open economy: In post-WWII Europe, this has actually been the 'constitutive bargain between capital and labor that couple[d] the open economy with generous safety nets'<sup>62</sup>. Thus, GVCs can increase both intra-state and interstate inequality. There is a need for serious reflection on how the governance of GVCs should be reformed in order to make them compatible with sustainable income growth (especially in developing countries) and the reduction in rent-seeking opportunities (in the hands of MNCs in developed nations)<sup>63</sup>. In that sense, domestic and international institutions are not neutral, as they can change the incentive structure for firms to organize production across states and sectors, thereby shaping GVCs in ways that could be more or less harmful to national economies<sup>64</sup>. In sum, the symbiosis of trade and investment through GVCs now has a deeper impact (with 'a much finer degree of resolution') on societies than traditional trade in finished goods<sup>65</sup>. In turn, it creates disruption across sectors and skills, leading to economic anxiety and insecurity because the consequences are not clearly seen and generating an identity crisis in a downward spiral of political extremism, nationalism, and eventually interstate conflict.

As trade and investment liberalization has allowed producers to outsource production segments to countries applying different (in most cases, lower) standards and (often less strict) rules, people have developed a sense of unfairness, which is even more detrimental to social

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<sup>59</sup> Bruce Cumings, *The Origins and Development of the Northeast Asian Political Economy: Industrial Sectors, Product Cycles, and Political Consequences*, in "International Organization", 38 (1), 1984, pp. 1-40.

<sup>60</sup> Richard Baldwin, *cit.*, p. 217.

<sup>61</sup> *Ivi*, p. 219.

<sup>62</sup> Dani Rodrik, *Populism and The Economics of Globalization*, *cit.*, p. 18. On the direct link between trade liberalization and increase in public spending see for instance: David R. Cameron, *The Expansion of the Public Economy: A Comparative Analysis*, in "American Political Science Review", 72 (4), pp. 1243-61; Dani Rodrik, *Why Do More Open Economies have Bigger Governments?*, in "Journal of Political Economy", 106 (5), pp. 997-1032.

<sup>63</sup> Raphael Kaplinsky, *Globalisation and Unequalisation: What can be learned from value chain analysis?*, in "Journal of Development Studies", 37 (2), 2000, pp. 117-46.

<sup>64</sup> Timothy J. Sturgeon, *From Commodity Chains to Value Chains: Interdisciplinary Theory Building in An Age of Globalization*, in Jennifer Bair (ed.), *Frontiers of Commodity Chain Research*, Stanford, Stanford University Press, 2009, pp. 110-35; Jappe Eckhardt and Arlo Poletti, *Introduction: Bringing Institutions Back in the Study of Global Value Chains*, "Global Policy" 9 (2), 2018, pp. 5-11.

<sup>65</sup> Richard Baldwin, *cit.*, p. 218.

cohesion than inequality itself<sup>66</sup>. Therefore, even though technology is more responsible than trade for job losses, ‘globalization became tainted with a stigma of unfairness that technology evaded’<sup>67</sup>. Moreover, there is evidence that ‘capital-account liberalization leads to statistically significant and long-lasting declines in the labor share of income and corresponding increases in the Gini coefficient of income inequality’ while favoring top income shares<sup>68</sup>. Not surprisingly, then, some studies have found a correlation between trade shocks and the rise of (both right-wing and left-wing) populism<sup>69</sup>: In the United States, the China trade shock has increased political polarization<sup>70</sup>, while in Europe larger import shocks from China have coincided with stronger support for nationalist and far-right parties<sup>71</sup>. Finally, in Britain, the districts that have suffered the most from imports of China tended to vote for Leave in the Brexit campaign<sup>72</sup>. Thus, we must now turn to the China factor.

## China-US trade wars

As if neo-liberalism was not enough to dismantle the Wilsonian architecture, another liberal pillar was simultaneously being eroded at its foundations: American hegemony. In the Bretton Woods years, the American economy was by far the largest economy in the world, with no serious rival (and competitors like Germany and Japan were easily tamed in the 1980s). At the end of the Cold War, the diffusion of neo-liberal economic principles allowed MNCs to find new markets for the location of their GVCs. One market was – potentially – the largest of all: China. Deng Xiaoping’s opening up of the country and subsequent reforms ultimately brought Beijing into the WTO in 2001, inextricably

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<sup>66</sup> Dani Rodrik, *Populism and the Economics of Globalization*, *cit.*, pp. 18-19. In fact, Rodrik notes how psychologists have found that people are less concerned with economic inequality as such – at least, as long as it is a reward for some kind of merit – than with unfairness: Christina Starmans, Mark Sheksin, and Paul Bloom, *Why People Prefer Unequal Societies*, in “Nature: Human Behaviour”, 1 (0082), 2017.

<sup>67</sup> Dani Rodrik, *Populism and the Economics of Globalization*, *cit.*, p. 23. Negative economic shocks, on the one hand, demand more inclusive social policies (traditionally appealing to the left) but, on the other hand, generate distrust in the institutions led by cosmopolitan elites, thus increasing the appeal of right-wing parties: Yotam Margalit, *Political Responses to Economic Shocks*, in “Annual Review of Political Science”, 22, 2019, pp. 277-95.

<sup>68</sup> *Ivi*, p. 21, referring to Davide Furceri, Prakash Loungani, and Jonathan D. Ostry, *The Aggregate and Distributional Effects of Financial Globalization*, IMF Working Paper WP/18/83, Washington, DC: International Monetary Fund, 2018. Online: <https://www.imf.org/en/Publications/WP/Issues/2018/04/11/The-Aggregate-and-Distributional-Effects-of-Financial-Globalization-Evidence-from-Macro-and-45772>, accessed 25/11/2019. On global inequalities, see also Branko Milanovic, *Global Inequality: A New Approach for the Age of Globalization*, Cambridge, MA, Harvard University Press, 2016.

<sup>69</sup> Dani Rodrik, *Populism and the Economics of Globalization*, *cit.*

<sup>70</sup> David Autor, David Dorn and Gordon H. Hanson, *The China Shock: Learning from Labor Market Adjustment to Large Changes in Trade*, in “Annual Review of Economics”, 8, 2016, pp. 205-40; David Autor, David Dorn, Gordon H. Hanson and Kaveh Majlesi, *Importing Political Polarization? The Electoral Consequences of Rising Trade Exposure*, NBER Working Paper 22637, 2017.

<sup>71</sup> Italo Colantone and Piero Stanig, *The Trade Origins of Economic Nationalism: Import Competition and Voting Behavior in Western Europe*, in “American Journal of Political Science”, 62 (4), 2018, pp. 936-53. The authors note that as austerity in Europe dried up public funds available for welfare as a compensation mechanism, people started to support protectionism. In response, populist politicians offered a package including trade defense (for the workers) and lower taxes (in order to appeal to the middle class)

<sup>72</sup> Italo Colantone and Piero Stanig, *Global Competition and Brexit*, in “American Political Science Review”, 112 (2), 2018, pp. 201-18.

linking China with Western economies. Already in the 1990s, MNCs had rushed in to invest, produce, and re-export, and China became soon the ‘factory of the world’. On aggregate, and in line with Ricardian efficiency, the world economy was better off, as consumers in the West could consume more (and cheaper) goods, while China – offering a vast pool of unskilled, low-cost labor force – was able to lift hundreds of millions of people out of poverty and become the second-largest economy in the world and is destined to overtake the US in the next few years.

The problem is that China’s development created imbalances in the world economy, as China has maintained a constant surplus in the balance of payments, while Europe and the US have always been running deficits. Chinese imports in the United States increased by 1,156% from 1991 to 2007, while US exports to China grew much less<sup>73</sup>. Economists have found that, while *on aggregate* these imports have benefited the US economy, local labor markets in import-competing industrial districts in the US have experienced higher employment, lower labor force participation, and reduced wages. Between 1990 and 2007, imports from China were responsible for one-quarter of the total decline in US manufacturing jobs<sup>74</sup>.

Having been elected on an ‘American First’ agenda, it is not surprising that President Donald Trump adopted a neo-mercantilist approach against China. Although largely overlooked, there was even a degree of continuity with his predecessor, as the Obama administration had already conceived the Trans-Pacific Partnership (TPP) – technically a regional free trade agreement among 12 countries of the Asia-Pacific – as a means to contain Beijing<sup>75</sup>, but there was a drastic change in policies, as President Obama had never given up on trade liberalization as a principle. Moreover, whenever the US wanted to take issue with China, it would sue the country under the framework of the WTO Dispute Settlement Mechanism (DSM)<sup>76</sup>. By contrast, in order to address the imbalances in the US balance of payments, Trump adopted a policy of *fairer* trade aimed at protecting American (import-competing) manufacturers. This policy consists of three pillars: (i) withdrawing from trade agreements not yet ratified by Congress, like the TPP, and re-negotiating existing ones; (ii) acknowledging that the WTO has deep flaws and that the DSM is not working to defend the American interest; and (iii) using tariffs to limit China’s and other economies’ unfair advantage as a result of the adoption of non-market practices<sup>77</sup>. This negative attitude – shared in Congress by Republicans and Democrats alike – is based on the wide perception that China has been free-riding on the liberal economic order. American hegemony in the liberal order requires that Washington

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<sup>73</sup> David H. Autor, David Dorn, and Gordon H. Hanson, *The China Syndrome: Local Labor Market Effects of Import Competition in the United States*, in “The American Economic Review” 103 (6), 2013, pp. 2121-68, p. 2158.

<sup>74</sup> *Ivi*.

<sup>75</sup> Arlo Poletti, *Containment through trade: explaining the US support for the Trans-Pacific partnership*, in Marco Clementi, Barbara Pisciotta, Matteo Dian (eds), *US Foreign Policy in a Challenging World – Building Order on Shifting Foundations*, Chan, Springer International, 2017, pp. 45-62.

<sup>76</sup> Arlo Poletti, *Trump e il sistema aperto, tra globalizzazione e protezionismo*, in Alessandro Quarenghi (ed.), *Trump e l’Ordine Internazionale. Continuità e Discontinuità nella Politica Estera Statunitense del XXI secolo*, Milano, Egea, 2018, pp. 63-84, pp. 70-1.

<sup>77</sup> Office of the United States Trade Representative, *2019 Trade Policy Agenda and 2018 Annual Report*, Washington, DC, 2019. Online: [https://ustr.gov/sites/default/files/2019 Trade Policy Agenda and 2018 Annual Report.pdf](https://ustr.gov/sites/default/files/2019%20Trade%20Policy%20Agenda%20and%202018%20Annual%20Report.pdf), accessed 07/10/2019.

pay the cost of public goods such as open markets<sup>78</sup>. But inasmuch as the US was generously opening its market to China (although this view ignores the fact that many of the imports from China were goods produced in China by American MNCs through GVCs), Beijing kept parts of its economy closed to foreign capital, encouraged intellectual property right theft through forced technology transfers<sup>79</sup>, manipulated its currency, favored state-owned enterprises through state subsidies, and limited public procurement market access to domestic companies. To add a further and probably the ultimate offense against US interests and values, China was developing by engaging strategically in the global economy, selectively mixing elements of mercantilism and economic liberalism, much in line with the developmental state experience of Japan, South Korea, and Taiwan<sup>80</sup>. For liberals with faith in unfettered markets' power to generate economic growth, China's state-led economic rise is puzzling. Indeed, Beijing has been 'beating the West at its own game'<sup>81</sup> by adopting a particular mix of top-down and bottom-up approaches that has been defined as 'Sino-capitalism'<sup>82</sup>. For some, China's rise can only be explained by the comfortable idea that China must have been conspiring against the West for a long time, and now it is time for the country to reap the rewards of a 'secret strategy' to overthrow the US and become the sole superpower<sup>83</sup>.

Therefore, Trump's neo-mercantilist policies come in response to a 'call to action' for the West to take measures against China's growing economic might and a foreign policy activism that many influential voices have been airing in the political and intellectual debate in the US (including that of Peter Navarro, an economist now serving as Assistant to the President and Director of Trade and Manufacturing Policy)<sup>84</sup>. It all started in early February 2018 when the US imposed a 20% tariff on washing machine imports (worth US\$ 1.8 billion) and a 30% tariff on all solar panel imports (worth US\$ 8.5 billion). In March, building the legitimacy of tariffs on a national security clause contained in the WTO treaties, Washington approved a 10% duty on aluminum and a 25% duty on steel. This prompted retaliation by the European Union (EU), which adopted a 25% tariff on US\$ 3.4 billion of US exports while filing a complaint with the WTO under the DSM. At the same time, Trump granted exemptions to some countries, including Canada and Mexico – in this case, as tactical leverage in the negotiation of the new United States-Mexico-Canada trade agreement (USMCA). In April, it was China's turn to retaliate with tariffs worth US\$ 2.4 billion on pork, fruits, and nuts, whose producers in the US have subsequently received compensation from the Trump administration in a clear attempt to mitigate the financial and political damage. The US struck back by approving (under section 301 of the 1974 Trade Act) a 25% tariff on a list of Chinese products,

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<sup>78</sup> Charles P. Kindleberger, *The World in Depression, 1929-1939*, Berkeley and Los Angeles, 1973; Robert Gilpin, *The Political Economy of International Relations*, Princeton, NJ, Princeton University Press, 1987: trad. it., *Politica ed economia delle relazioni internazionali*, Bologna, Il Mulino, 1990.

<sup>79</sup> Office of the United States Trade Representative, *cit.*, p. 7.

<sup>80</sup> Giuseppe Gabusi, *The reports of my death have been greatly exaggerated: China and the developmental state 25 years after Governing the Market*, in "The Pacific Review", 30 (2), 2017, pp. 232-250.

<sup>81</sup> Stefan Halper, *The Beijing Consensus: How China's Will Dominate the Twenty-First Century*, New York, Basic Books, 2010, chapter 1.

<sup>82</sup> Christopher McNally, *SINO-CAPITALISM: China's Reemergence and the International Political Economy*, in "World Politics", 64 (4), 2012, pp. 741-76.

<sup>83</sup> Michael Pillsbury, *The Hundred-Year Marathon: China's Secret Strategy to Replace America as the Global Superpower*, New York, Henry Holt and Company, 2015.

<sup>84</sup> Peter Navarro and Greg Autry, *Death by China: Confronting the Dragon — A Global Call to Action*, Upper Saddle River, NJ, Pearson Education, 2011.

including machinery. Since then, the script has been played again and again in an escalation of trade wars whose end is still nowhere in sight<sup>85</sup>. Going against the spirit of GATT and WTO, trade has been re-politicized, and free trade has come under attack from all sides of the political spectrum, despite its benefits, which have never been disproved since Ricardo's time<sup>86</sup>.

The world is clearly experiencing a return to geoeconomics, which is defined as 'the use of economic instruments to promote and defend national interests, and to produce beneficial geopolitical results; and the effects of other nations' economic actions on a country's geopolitical goals'<sup>87</sup>. Interdependence has been 'weaponized'<sup>88</sup> – a far cry from neo-liberal institutionalists' argument that interdependence fosters cooperation<sup>89</sup>. Realists' claims that relative gains matter and that international primacy is the only way to shape the order in such a way that the superpower's interest is protected<sup>90</sup> are gaining ground. Liberals' counterargument, namely that states would play a lose-lose game by competing against each other in a rush to be No. 1, seems outdated<sup>91</sup>.

Does all this mean that states are turning autarchic and that globalization is over? Not necessarily. In a sense, GVCs have strengthened the pro-openness coalition among economic actors as traditional constituencies of exporters have been joined by producers willing to import intermediate products at cheap prices<sup>92</sup>. Even if they are somehow re-shaped, globalization and the liberal order could be more resilient than we might think. The recent case of the Chinese telecom company Huawei is evidence of how MNCs could force states to constrain their mercantilist tendencies: In May 2019, maintaining that the company has strong links with the Chinese state, Trump banned Huawei from selling 5G equipment in the US and American companies from doing business with it. This ban was suspended almost immediately as MNCs voiced their concerns to the President and predicted a possible double-sided boomerang effect: On the one hand, the ban would hurt American business; on the other hand, the Chinese company would be forced to accelerate the development of its indigenous innovative technologies<sup>93</sup>. In other words, the trade–investment–technology nexus might make 19<sup>th</sup>-century-style, zero-sum mercantilist policies obsolete,

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<sup>85</sup> For an update chronology, see Peterson Institute for International Economics, *Trump's trade war timeline: an up-to-date guide*, Washington, DC, 2019. Online: <https://www.piie.com/blogs/trade-investment-policy-watch/trump-trade-war-china-date-guide>, accessed 08/10/2019.

<sup>86</sup> Douglas A. Irwin, *Free Trade Under Fire*, Princeton, NJ, Princeton University Press, 2015; Paul R. Krugman, *The narrow and broad arguments for free trade*, in "The American Economic Review", 83 (2), pp. 362-66.

<sup>87</sup> Robert D. Blackwill and Jennifer M. Harris, *War By Other Means: Geoeconomics and Statecraft*, Cambridge, MA, The Belknap Press of Harvard University Press, 2016, p. 20.

<sup>88</sup> Henry Farrell and Abraham L. Newman, *Weaponized Interdependence: How Global Economic Networks Shape State Coercion*, in "International Security", 44 (1), 2019, pp. 42-79.

<sup>89</sup> Robert O. Keohane and Joseph Nye, *Power and Interdependence*, Boston, Little Brown, 1977.

<sup>90</sup> Samuel P. Huntington, *Why international primacy matters*, in "International Security", 17 (4), 1993, pp. 68-83.

<sup>91</sup> Robert Jervis, *International Primacy: is the game worth the candle?*, *ivi*, pp. 52-67.

<sup>92</sup> Jappe Eckhardt and Arlo Poletti, *The politics of Global Value Chains: import-dependent firms and EU-Asia trade agreements*, in "Journal of European Public Policy", 23 (10), pp. 1543-62.

<sup>93</sup> Kiran Stacey and James Politi, *Google warns of US national security risks from Huawei ban*, in "Financial Times", 2019, June 7. Online: <https://www.ft.com/content/3bbb6fec-88c5-11e9-a028-86cea8523dc2>, accessed 07/10/2019.

ineffective, and even sidelined. Trade wars become ‘unwinnable’<sup>94</sup> in the medium to long term, unless Washington wants to achieve a complete decoupling of the American economy. In that case, global capitalism could be consigned to the history books<sup>95</sup>. A recent decision by a WTO panel authorizing the US to adopt compensatory measures against the EU’s subsidies to Airbus<sup>96</sup> could also convince the Trump administration that a multilateral trade regime based on rules and norms administered by a quasi-judicial body still has its merits and that efforts should instead be directed at reforming the WTO and updating its structure and scope to account for the complex trade reality of the 21<sup>st</sup> century<sup>97</sup>.

## Conclusion

Wilson himself understood that the ‘animal spirits’ of markets should somehow be made compatible with collective welfare, as in their search for profits they would not necessarily abstain from labor exploitation but produce inequalities that would cause rage and disaffection and, thereby, erode public support for democracy and capitalism. Reflecting on the Bolshevik Revolution in Russia, Wilson asked himself: ‘Is the capitalist system unimpeachable... have capitalists generally used their power for the benefit of the countries in which their capital is employed and for the benefit of their fellow men? Is it not, on the contrary, too true that capitalists have often seemed to regard the men whom they use as mere instruments of profit, whose physical and mental powers it was legitimate to exploit with a slight cost to themselves as possible, either of money or sympathy?’<sup>98</sup>.

In the end, the collapse of the Soviet Union and the end of the Cold War brought the world a neo-liberal hubris – a pride in the natural virtues of self-regulating markets that would automatically produce a trickle-down effect and bring peace and prosperity to all, if everyone simply adjusted to price signals. That was a (self-serving) illusion: Neo-liberalism sowed the seeds of discontent<sup>99</sup> and anger, as it had done at other moments in history, including in 1917 in Russia<sup>100</sup>.

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<sup>94</sup> Weijian Shan, *The unwinnable trade war: everyone loses in the U.S.-China Clash – but especially Americans*, in “Foreign Affairs”, November-December 2019. Online: <https://www.foreignaffairs.com/articles/asia/2019-10-08/unwinnable-trade-war>, accessed 09/10/2019.

<sup>95</sup> Chad P. Bown and Douglas A. Irwin, *Trump’s assault on the global trading system – and why decoupling from China will change everything*, in “Foreign Affairs”, 2019, 12 August. Online: <https://www.foreignaffairs.com/articles/asia/2019-08-12/trumps-assault-global-trading-system>, accessed 07/10/2019.

<sup>96</sup> World Trade Organization, *European Communities and Certain Member States – Measures Affecting Trade in Large Civil Aircraft*, WT/DS316/ARB, Geneva, 2019, October 2. Online: [https://www.wto.org/english/tratop\\_e/dispu\\_e/316arb\\_e.pdf](https://www.wto.org/english/tratop_e/dispu_e/316arb_e.pdf), accessed 07/10/2019.

<sup>97</sup> Government of Canada, *Joint Communiqué of the Ottawa Ministerial on WTO Reforms*, Ottawa, 2018, 25 October. Online: <https://www.canada.ca/en/global-affairs/news/2018/10/joint-communique-of-the-ottawa-ministerial-on-wto-reform.html>, accessed 07/10/2019.

<sup>98</sup> Arthur Stanley Link et al., *The Papers of Woodrow Wilson*, Princeton, NJ, Princeton University Press, 1966-1994, 68, 7/1923, p. 394f, quoted in Tony Smith, *cit.*, p. 19.

<sup>99</sup> Joseph Stiglitz, *Globalization and Its Discontents*, New York, W.W. Norton & Company, 2002: trad. it., *La globalizzazione che funziona*, Torino, Einaudi, 2006.

<sup>100</sup> Pankaj Mishra, *Age of Anger: A History of the Present*, London: Allen Lane, 2017: trad. it., *L’età della Rabbia. Una storia del presente*, Milano, Mondadori, 2018.



In the end, the primacy (indeed, supremacy) of the economic side of the diamond obscured the other three dimensions of Wilsonianism and precipitated a snowball effect on the sustainability of the liberal order, menacing democracy, international institutions, and (paradoxically) economic openness: 'Left to its own machinations, open world markets alone were no guarantee of a better world, any more than capitalism left to its own devices would automatically be at the service of democracy in the United States'<sup>101</sup>. In truth, the size and power of corporations were left increasingly unchecked by political authorities, creating a 'supercapitalism'<sup>102</sup> not necessarily in tune with the principles of classical liberalism.

Moreover, neo-liberalism plunged democracy into a crisis at the very moment when China's rise was being felt in Washington as a threat to the hegemony of the United States. In 1985, when Japan was seen as the main challenger, the United States used the Plaza Agreement to force Tokyo to revalue the yen, thereby making Japanese exports to the U.S. less convenient, with the result that Japan paid the cost of adjustment with at least two decades of recession or slow growth. But while Tokyo was a military ally and American companies had not been investing billions of dollars in Japan, Beijing is now a military and strategic competitor, and American multinationals are deeply involved in GVCs revolving around China. In other words, Washington cannot easily replicate a Plaza Agreement with China without escalating the risk of conflict and disrupting essential parts of the American economy. In 2018, Cui Tiankai, China's ambassador to the US, said: 'Give up the illusion that another Plaza accord could be imposed on China'<sup>103</sup>. Thus, the Trump administration turned to tariffs as an instrument to force China to change its behavior either by revaluing the yuan or by further reducing all remaining restrictions on its domestic market access in terms of imports, investment, or public procurement. In other words, the US ceased to perform its (benevolent) hegemonic role of supplier of a fundamental public good (i.e., open markets).

This neo-mercantilist approach of the United States produced yet another crack in the Wilsonian four-sided 'diamond' described by Ikenberry and signaled an end to the post-WWII 'liberal hegemonic international order'<sup>104</sup>. A vicious cycle started: As extreme openness generated inequalities and a perceived unfair advantage of China, the American public opinion started to criticize the 'liberal elite' in their country and elected a president who had promised to adopt very different mercantilist policies that would undermine the collective (trade) security guaranteed by international organizations like the WTO. After WWII, liberals conceived the GATT (and then the WTO) as an instrument to put trade disputes outside the realm of politics and under the jurisdiction of arbiters or even judges, much in line with Cobden's ideas. Further disengagement from the WTO and a re-politicization of international trade now mean that the economic cost of conflict diminishes and, consequently, the risk of conflict arises.

The world was a different place in 1919. America was on the rise and the weakened hegemonic power of the British Empire was struggling to survive. The United States was not ready to recognize that it was time to assume the role of a new hegemon, while Great Britain could not

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<sup>101</sup> Tony Smith, *cit.*, p. 19.

<sup>102</sup> Robert B. Reich, *Supercapitalism: The Battle for Democracy in an Age of Big Business*, Cambridge, Icon Books, 2008: trad. it., *Supercapitalismo. Come cambia l'economia globale e i rischi per la democrazia*, Roma, Fazi Editore, 2008.

<sup>103</sup> Quoted in *The Economist*, *As the trade war heats up, China looks to Japan's past for lessons*, 2019, 23 May. Online: <https://www.economist.com/finance-and-economics/2019/05/23/as-the-trade-war-heats-up-china-looks-to-japans-past-for-lessons>, accessed 02/10/2019.

<sup>104</sup> G. John Ikenberry, *Liberal Internationalism 3.0: America and the Dilemmas of Liberal World Order*, in "Perspectives on Politics", 7 (1), 2009, pp. 71-87, p. 76.

play its traditional function as guarantor of the international economic order: A hegemonic transition was underway<sup>105</sup>. But it was a transition within the white, Anglo-Saxon, and Protestant liberal world. Now this Anglo-American era has come to an end<sup>106</sup>. The world in 1945 was also different from the global landscape that we face today. Back then, the United States emerged from WWII as the uncontested economic power, since Britain was suffering a heavy cost for its war efforts, Japan and Germany had been brought to their knees, and the Soviet Union was gradually retreating from the free and open world. Non-communist countries willing to engage in the global economy had no choice but to join the West, led by the US. Today, there is an alternative: China. In fact, for many developing countries, China is an alternative source of trade, aid, and investment. Above all, as noted above, its economic success has made it a source of inspiration.

Beijing does not pose a direct challenge to the liberal order *per se*. However, by articulating a Sino-centric mode of governance, China has started to engage in parallel-order shaping<sup>107</sup> to enhance China's national interest, thereby undermining the very political foundations upon which the US-led liberal order is based. The question then becomes: How can a liberal order survive when the second-largest (soon the largest) economy in the world accepts two out of the four pillars of Wilsonianism (i.e., economic openness, albeit strategically managed, and, with some reservations, multilateral institutions as instruments of collective security) but is totally opposed to the other two, namely liberal democracy and American leadership? What would a much flatter 'liberal international order 3.0'<sup>108</sup> look like? For sure, a new liberal international order 'will increasingly find itself concerned with the internal governance of states'<sup>109</sup>. Would it still be possible to engage China in the liberal order (even though Beijing's concept of multilateralism is somehow different<sup>110</sup>), or does the end of the illusion that China would be fully integrated via economic liberalization into the liberal order mean that 'we have lost China'? 'Managing diversity' in the international system of states would be crucial in the 21<sup>st</sup>-century world<sup>111</sup>, where China and other non-Western countries simply do not fit completely into the liberal template. Indeed, without the active collaboration of Russia and China, the liberal order can no longer be maintained<sup>112</sup>. For sure, as things stand, it is out of the question that these states will simply join the liberal order. Shiping Tang, an influential scholar at Fudan University, argues for instance that the West-centered and supposedly liberal order was

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<sup>105</sup> Charles Kindleberger, *cit.*

<sup>106</sup> Ian Buruma, *The End of The Anglo-American Order*, in "New York Times Magazine", 2016, 29 November; Amitav Acharya, *The End of American World Order*, Cambridge, Polity Press, 2014; Robert Kagan, *The World America Made*, New York, NY, Vintage, 2013.

<sup>107</sup> Zhimin Chen, *China, the European Union and the Fragile World Order*, in "Journal of Common Market Studies", 2016, 54 (4), pp. 775-92; Anna Caffarena and Giuseppe Gabusi, *China's Belt and Road Initiative in Eurasia: Space-Shaping as Oding*, in Serena Giusti and Irina Mirkina (eds), *The EU in a Trans-European Space: External Relations Across Europe, Asia and the Middle East*, London: Palgrave Macmillan, 2019, pp. 65-85.

<sup>108</sup> G. John Ikenberry, *Liberal Internationalism 3.0, cit.*, pp. 80-84.

<sup>109</sup> Ivi, p. 81.

<sup>110</sup> See for example Hongying Wang, *Multilateralism in Chinese Foreign Policy: The Limits of Socialization*, in "Asian Survey", 40, (3), 2000, pp. 475-91; Joel Wuthnow, Xin Li, and Lingling Qi, *Diverse Multilateralism: Four Strategies in China's Multilateral Diplomacy*, in "Journal of Chinese Political Science", 17 (3), 2012, pp. 269-90.

<sup>111</sup> Anna Caffarena, *Diversity Management in World Politics. Reformist China and the Future of (Liberal) Order*, in "The International Spectator", 52 (3), 2017, pp. 1-17.

<sup>112</sup> Vittorio Emanuele Parsi, *Titanic, cit.*, p. 112.

liberal only in its economic aspect, but for the rest, it was a hegemonic (not really a global) order imposed by the United States after its victory in WWII. He thinks that multiple ‘international orders’ will emerge, as an ‘enterprise contested by multiple actors and ideas, with overlapping regional, sub-regional, and global order(s)’<sup>113</sup>, even though it is far from clear how to manage the relationships among different orders. As (neo-liberal) capitalism itself becomes infused with neo-statism, the most likely result is a ‘chaotic mélange’ whose final outcome is uncertain and potentially dangerous<sup>114</sup>. We could also see a world based on the coexistence of multi-level, issue-based, and region-oriented forms of governance in a functionalist way *à la Mitrany* that would be more in tune with a diverse membership of the international system<sup>115</sup>.

In this sense, Wilson could teach our troubled present a lesson. One of his Fourteen Points was self-determination against colonial powers, intended as ‘the right of peoples to autonomous development and the sovereign right of nations to political and economic independence and territorial integrity [...] The right of a people [...] to govern itself in its own way’<sup>116</sup>. Recognizing diversity and coming to terms with the fact that the liberal prophecy in the case of China simply did not materialize is in line with Wilson’s message of respect for self-determination, and it should be the first step of any attempt to accommodate the order to the new reality. The other lesson that we can learn from Wilsonianism is that open liberal democracies – a crucial pillar of the liberal order – can properly function only if they guarantee welfare, social justice, and the right to work. Otherwise, public opinion will turn against trade, support national autarky<sup>117</sup>, and vote for nationalist parties with authoritarian tendencies. Indeed, Wilson had a progressive agenda at home and supported reforms to tackle vested interests<sup>118</sup>. Far too often, we forget the link between domestic and international politics and the need for any global order design to be compatible with internal economic growth and an acceptable degree of domestic equality. The liberal order born in Bretton Woods was based on a ‘connection between progressivism at home and liberal internationalism abroad’<sup>119</sup>.

It is not necessarily true that Wilsonianism can only offer ‘a better guide’ to meeting 21<sup>st</sup>-century challenges if it is ‘properly adapted and updated’<sup>120</sup>. Wilson’s insistence on the tight interconnection between the four pillars of his entire architecture simply has to be re-read (and put in the right light). Open trade in itself is not enough to secure peace, even though there is evidence

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<sup>113</sup> Shiping Tang, *The Future of International Order(s)*, in “The Washington Quarterly”, 41(4), 2018, pp. 117-31, p. 129.

<sup>114</sup> Christopher McNally, *Chaotic Mélange: Neo-liberalism and Neo-statism in the age of Sino-capitalism*, in “Review of International Political Economy”, 2019. Online: <https://www.tandfonline.com/doi/full/10.1080/09692290.2019.1683595>, accessed 27/11/2019.

<sup>115</sup> Shaun Breslin, *Leadership and Followership in Post-Unipolar World: Towards Selective Global Leadership and a New Functionalism?*, in “Chinese Political Science Review”, 2, 2017, pp. 494-511; David Mitrany, *A Working Peace System*, Chicago, Quadrangle, 1966.

<sup>116</sup> Anne-Marie Slaughter, *Wilsonianism in the Twenty-first Century*, in G. John Ikenberry, Thomas J. Knock, Anne-Marie Slaughter and Tony Smith, *cit.*, pp. 89-117, pp. 92-3.

<sup>117</sup> This is exactly Fichte’s logic: Isaac Nakhimovsky, *The Closed Commercial State*, *cit.*, p. 5. Nakhimovsky even notes some ‘recent efforts to reenlist Fichte as a theorist of distributive justice’: *Ivi*, p. 6.

<sup>118</sup> “[...] He took on vested economic interests to lower tariffs, regulate banking, increase the federal government’s role in monetary policy through the creation of the Federal Reserve, and strengthen antitrust laws’: Anne-Marie Slaughter, *cit.*, p. 95.

<sup>119</sup> G. John Ikenberry, *The End of Liberal Order?*, in “International Affairs”, 94 (1), pp. 7-23, p. 21.

<sup>120</sup> *Ivi*, p. 92.

of the correlation between trade and peace in the post-WWII decades<sup>121</sup>. Wilson's vision was much more articulated and comprehensive since economic openness was an instrument, not an end in itself: Wilsonianism was meant to 'remov[e] the obstacles to social development and economic growth internationally'<sup>122</sup>, as he had done domestically. Acknowledging this is the first step in restructuring a liberal order that would be sustainable and appealing to most countries and ensure a prosperous, conflict-free, and democratic international system because all the available alternatives – including a 'new international economic disorder'<sup>123</sup> (El-Erian 2011) – seem to carry more risks of tensions, frictions, and wars.

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<sup>121</sup> Han Droussen and Hugh Ward, *cit.*

<sup>122</sup> *Ivi*, p. 108.

<sup>123</sup> Mohamed Aly El Erian, *The New International Economic Disorder*, in "Project Syndicate", 2011, December 21, online: <https://www.project-syndicate.org/commentary/the-new-international-economic-disorder?barrier=accesspaylog>, accessed 03/10/2019.