# PREPARING FOR A SECOND WAVE OF COVID-19

## A TRADE BARGAIN TO SECURE SUPPLIES OF MEDICAL GOODS

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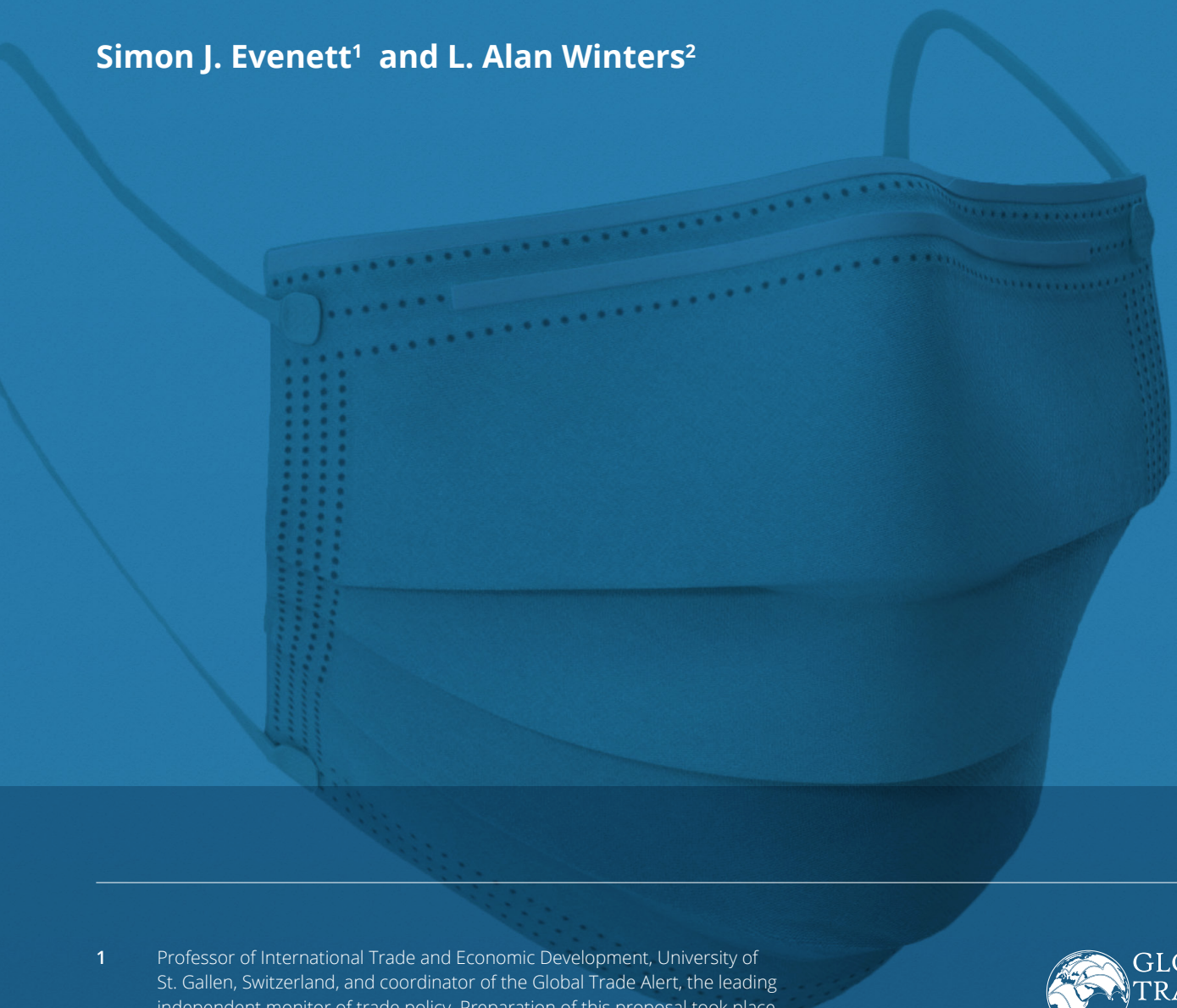

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## EXECUTIVE SUMMARY


- As they scramble to find medical supplies to tackle COVID-19, some countries are eliminating their restrictions in imports while others are curtailing their exports. The resulting market disruption and fragmented production pattern is very costly.
- To discourage importers from restoring their restrictions when markets stabilise, exporters should offer to constrain their resort to export restrictions. By linking the two policies together in a reciprocal trade bargain, exporters are assured larger markets while importers will have greater assurance of delivery.
- Larger and more predictable markets will stimulate investment and thereby increase supplies of critical medical products. Both exporting countries' domestic residents and the people importing their products will benefit from the resulting lower costs through economies of scale.
- The new bargain would significantly reduce the uncertainty facing buyers and sellers of vital medical supplies should subsequent waves of COVID-19 infection occur.

## Introduction

Much of what has been written about the $597 billion trade worldwide in medical products and medicines linked to the COVID-19 pandemic has emphasised either the prevalence or consequences of export curbs or made the case for liberalising imports, principally through eliminating tariffs. Few have linked these two policy instruments and, those proposals which have, did not draw out the logic of the basis for a deal between governments. Failure to do so obscures one of the main benefits of much needed collective action.

Matters could not be more serious. A once-in-a-lifetime pandemic has resulted in a surge in demand for medical consumables, including personal protective gear, medical equipment, and medicines, and created a scramble for supplies. This has led to elevated prices in many cases, and even accusations of piracy and other sharp practices. Resort to export bans has disrupted the public health plans of trading partners and put lives at risk.

This paper sets out a new basis for reciprocity in what might be deemed essential goods, of which the medical kit and equipment associated with COVID-19 are examples. Our proposal recognises the international concentration in the production of these goods before the pandemic, with many nations relying on international trade to meet their needs. Such specialisation is valuable in allowing producers to exploit economies of scale and take advantage of local efficiencies, both of which lower costs. Rejecting specialisation has significant opportunity costs, whether we like it or not.

Current failures to secure enough medical supplies have led in certain quarters to calls for greater self-reliance, "strategic autonomy," "repatriated supply chains," and other euphemisms that will threaten the commercial viability of existing supply routes without guaranteeing enough medical kit for the next wave of COVID-19 or the next pandemic. And such calls won't produce any medical ventilators now, won't devise a vaccine for COVID-19, and ultimately do little to alleviate current suffering.

Our starting point is grounded in the realities of today: reliance on cross-border supply of COVID-19-related medical supplies, the international nature of the supply chains that currently deliver those supplies, widespread resort to export curbs on such supplies, initiatives by dozens of governments to temporarily liberalise import regimes for these goods, and historically well-founded fears that pandemics like this involve multiple waves of infection. Our starting point is "what is" and not upending the world in pursuit of some nirvana.

We propose a trade policy bargain that, although time-limited at first, could evolve into a multilateral or plurilateral deal. As governments of net exporting nations realise that export bans do little to end shortages of medical kit in a world of international supply chains, and do much to antagonise trading partners and to embolden economic nationalists at home and abroad, this proposal provides them with a rationale for embracing a more collaborative approach that generates a commercial edge for their exporters of medical supplies. For nations reliant on foreign deliveries of these goods, our proposal provides greater reassurance that supplies will be forthcoming when they are needed—thereby diminishing the case for devoting scarce resources to an import substitution drive on medical goods.

Our approach departs from existing initiatives and proposals in meaningful ways. To get the core of the idea advanced here, we turn to the central flaw in the existing approach to reciprocal deal-making in essential goods.

## Why we need a new basis for a deal

The Uruguay Round plurilateral agreement on Trade in Pharmaceutical Products[1] is a good place to start. This accord was signed by 12 industrialised country members of the then-GATT that were manufacturers and exporters of these products. Signatories agreed to eliminate import tariffs and customs duties a on specified range of pharmaceutical products.

To the best of our knowledge, no nation that relied extensively on imported pharmaceuticals joined this accord and it is worth reflecting on why. Such net importers could, of course, scrap their tariffs unilaterally but, according to a recent WTO secretariat study of medical goods before the COVID-19 pandemic struck, a total of 61 WTO members had not. The limited membership of this Uruguay Round accord suggests that there may be some compelling countervailing arguments worth considering.

In the past weeks we have seen one reason why governments might be reluctant to permanently eliminate their tariffs on medical equipment and supplies—namely, the resort to curbs on exports of these products at the very time importers need them most. A liberal import regime in medical supplies is not worth much if there isn't much to buy at affordable prices. Currently at least 75 governments have restricted exports of medical supplies and medicines.[2]

1 See document L/7430 dated 25 March 1994.

2 At the time of writing, similar dynamics are at work in international trade in food but to a lesser degree. Twenty-six WTO members accounting the bulk of world ex-

Indeed, pressure to reverse temporary tariff cuts on imported medical products and implement import-substitution policies could increase in the months ahead should import liberalisation yield only tiny amounts of additional medical supplies. Perhaps collective amnesia will break out among trade policymakers in net importers, then this won't be a problem. More realistically, this year's widespread export curbs will fuel the reversal of the import reform efforts in this sector.[3]

At its core, the risk of export bans upsets the traditional tariff-based logic for reciprocity. Net importers will discount the gains from tariff cuts by the extent to which such risk threatens supplies at critical times.[4] In turn, net exporters will find commercial sales abroad are impeded by their reluctance to qualify their resort to export bans.

Moreover, to the extent that sales abroad allow local manufacturers to attain greater scale, which in turn delivers benefits in terms of employment, lower costs for the exporting nation's buyers of medical suppliers, and greater returns to innovation, then there is also a domestic price to be paid for eschewing limits on the resort to export bans.

It appears that these considerations have not influenced the calculus of a recent proposal for a plurilateral accord in trade in medical goods advanced by the European Union. It is telling that official reports about this proposal make no reference to export restrictions and concentrate on eliminating import tariffs.[5]

To its credit, the recent initiative of New Zealand and Singapore refers to both import tariff elimination and commitments not to "apply export prohibitions or restrictions, within the meaning of Article XI:1 of the GATT 1994", at least in a defined list of medical goods.[6] Eschewing such export curbs outright eliminates the uncertainty created by their use and thus is clearly desirable.

However, completely giving up the right to use such curbs may be unacceptable to some WTO members and the question arises whether an alternative approach might reduce the attendant uncertainty by qualifying the right to resort to export restrictions without abolishing it altogether? Our approach reflects an assessment that the reduced risk to disruptions in supply that will be valued by importing nations can be obtained by less restrictive disciplines on export curbs.

## A new *quid pro quo*

In a nutshell, in return for assurances that their supplies of medicines and medical products will not be cut off completely and arbitrarily, importing governments would eliminate their import tariffs. For their part, governments of exporters of medical products would accept qualified rights to introduce temporary export curbs on shipments abroad. For a fixed period of time—say five years in the first instance—each party would give up some discretion in return for greater security of supply of medical products or greater market access. The opportunity here is to significantly reduce the uncertainty facing buyers and sellers of vital medical supplies should subsequent waves of COVID-19 infection occur.

For sure, there are important details to be worked through (see the next section) but the advantages of this deal are that:

- Its logic can be easily explained.
- It has particular resonance at this time given the liberalising steps dozens of governments have already taken and the urgent need for cross-border medical supplies now and during a second wave of infection.
- Exporting nations are at different stages in the first wave of infection by COVID-19. An exporting nation's interests shift markedly once the number of new cases of COVID-19 starts falling towards levels that make the restoration of something approaching normal economic conditions possible. Around that time, this new *quid pro quo* has greater appeal. In short, it is a mistake to lump all net exporters of medical supplies and medicines together when assessing the attractiveness of this understanding at any one point in time.
- Proper risk management by buyers of medical products and medicines would include discounting offers from suppliers located in nations that free ride on this understanding. Exporters based in signatories to this new *quid pro quo* could draw attention to the reduced risk of disruptions to their supply through marketing initiatives, including their own labels.

ports and imports in agriculture and food released a statement on 22nd April (WTO/GC/208) committing not to introduce export restrictions on agriculture. On agri-foods, the commitment is just to observe WTO rules.

3 Compounding the concern is that multiple waves of COVID-19 could lead to temporary export curbs being imposed repeatedly.

4 To be clear, following well-established economic logic, we argue that nations gain when they reduce barriers to imported goods. Those gains include buyers paying lower prices, access to a greater variety of products, including higher quality goods.

5 See, for example, these two reports. The European Commission has yet, to the best of our knowledge, to put forward a specific proposal, but in an interview with the Financial Times (23rd April 2020) Trade Commissioner Hogan distanced himself from calls for self-sufficiency or significant on-shoring of production.

6 See WTO document G/C/W/777.

- The bargain significantly reduces the uncertainty faced by both manufacturers of medical supplies and medicines and by buyers, both public and private. Reduced uncertainty encourages investment and greater supply of vital medical supplies.
- Governments with little patience for dragged out global trade talks can move ahead without precluding the opportunity of other states to join later.
- Governments with a nationalistic bent cannot reasonably object to this initiative, not least because it has been designed to respect the Most Favoured Nation (MFN) principle.
- By qualifying resort to export bans, the bargain encourages governments to focus on alternative ways to narrow the gap between the demand and supply for medical goods, including those options involving cooperation with other governments.
- Signing up for five years rather than in perpetuity makes it easier for governments to agree.
- Once calmer times return, this understanding could form the basis of a subsequent legally binding WTO agreement on trade in medical products and medicines.

## Central elements of the proposed understanding

As the saying goes, the devil is in the details. The new *quid pro quo* would be translated into an understanding with the following central elements:

- The understanding would be open to all members of the WTO.
- The understanding would cover those medical goods and medicines listed in Annex 1 of the recent WTO secretariat study on COVID-19 and trade.[7]
- Before joining the understanding, each signatory:
  - Shall eliminate tariffs on an MFN basis on the covered medical goods and medicines.
  - Shall eliminate all export limits on any covered medical goods and medicines.
- With respect to non-tariff measures, including standards concerning medical supplies, medical equipment, and medicines, should a government suspend a national requirement or accept a foreign standard during this crisis, then within two years of doing so, the signatory commits to give serious and objective consideration to making such temporary arrangements permanent.
- A signatory may introduce an export limit relating to a covered good so long as:
  - The specific triggering event for its introduction is explained in writing to other signatories and a cogent rationale for the export limit is provided. The explanation must be posted on an externally-accessible website on the same day that the export limit is announced.
  - The product coverage of the export limit is no wider than necessary to tackle the triggering event.
  - The limit is set in quantitative terms so as to meet the contingency at hand.[8] Any such quantitative parameter must be set at a proportionate level.
  - The duration of any such export limit must be publicly stated and, in the first instance, must be no longer than 6 months.
  - Any limit can be renewed for up to six months, must be notified to other signatories, and a cogent explanation provided for the renewal.
  - The limit shall take the form of a publicly-stated percentage reduction in exports from the customary value (taken to be, for any month, the average value of exports to each trading partner in that month in the previous two years).
  - The limit shall not reduce the flow of exports by more than 50% of the customary value.
  - The limit shall not take the form of an export authorisation scheme, which involve discretion, too often are non-transparent, and can be implemented in a way that is tantamount to an export ban.
  - For the purpose of this initiative the following are taken to be export limits: outright export bans, conditional export bans, orders by public bodies to requisition more than half of domestic production of a medical good or medicine, regulations requiring manufactures to reserve part of their production for the national market, and any formal or informal agreement between a signatory

7 World Trade Organization. "Trade in Medical Goods in the Context of Tackling COVID-19: Information Note," 3 April 2020.

8 For example, if a signatory estimates it requires 1,000 medical ventilators to meet some emergency then the limit will lapse once that number of medical ventilators is obtained.

and a producer within its customs territory that has the effect of reducing the total supply of new medical goods covered by this accord.

- These qualifications to the resort to export limits apply only to the supply of newly manufactured medical goods. No qualification is implied for existing rights of a WTO member to restrict the export of any medical goods purchased, or in use before, COVID-19 was declared a pandemic by the World Health Organization.[9]

- Signatories would abide by the four trade facilitation commitments listed under heading "Facilitation of Trade in Essential Goods" of the Declaration of Trade in Essential Goods For Combating the COVID-19 Pandemic" notified by New Zealand and Singapore in WTO document G/C/W/777.

Evidently, elements of this proposal can be found in the constructive initiative by New Zealand and Singapore. However, differences exist. This proposal focuses exclusively on medical supplies and medicines, whereas the latter includes provisions on food. Nothing prevents our proposal being extended to include the latter. Secondly, our proposal provides a different approach to qualifying the resort to export limits by governments.

Separately, our proposal could also be viewed as one means to implement the G-20 Trade Ministers' recent injunction that "emergency" trade measures be " targeted, proportionate, transparent, and temporary, and that they do not create unnecessary barriers to trade or disruption to global supply chains, and are consistent with WTO rules." Every one of those criteria is met in the stipulations on export limits outlined above.

## Closing remarks

Amid the gloom and the disheartening media reports about the scramble for medical supplies—made worse by widespread resort to export curbs—an opportunity has arisen that trade policymakers should grasp. A potential bargain is on the table that would significantly reduce the uncertainty and barriers faced by both buyers and suppliers of medical products and medicines. This bargain would serve its signatories well should another wave of COVID-19 infection hit and would lay the foundation for a subsequent legally binding agreement at the WTO, perhaps through a plurilateral accord.

Given the sensitive nature of the products involved, a zero-for-zero tariff deal will not be sufficient. Importers are much less likely to put their trust in overseas sourcing of life-preserving goods if there is a significant risk of disruption created by export restrictions. A new deal—a new basis for reciprocity—is required.

Even though the shortcomings of unilateral trade policies are becoming clearer by the day, there is still little appetite for an elaborate negotiated solution at the global level, at least in the near term. A sensible starting point then is to build on what governments have already done, using the need to prepare for a second wave of COVID-19 infection and the obvious health gains from greater medical equipment trade to focus minds on an easy-to-articulate initiative that ministers can readily sign up to.

We are well aware that this proposal does not fix every problem arising from the current shortages in medical supplies resulting from the COVID-19 pandemic.[10] Our goal, instead, is more modest—rather than grand designs, our starting point is to capitalise upon the steps that many governments have implemented since the pandemic began.

This opportunity should be seized before governments that have temporarily liberalised their import regimes to medical products get frustrated with the paucity of available supplies and reverse their reforms. This appeal of this bargain will rise as more net exporters of medical kit and medicines put the worst of the first wave of the COVID-pandemic behind them.

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**9** In terms that economists at least can relate to, these qualifications to the right to use export limits apply to the *flow* of new medical supplies and not to the *stock* of pre-pandemic supplies that have been purchased previously by parties, public or private, within a signatory's customs territory.

**10** While implementation of our proposal may stimulate production of medical supplies and medicines, it is not meant to be a substitute for a package of internationally agreed steps to expand production capacity, to maintain some production redundancy (allowing output to be ramped up when necessary), to build and maintain stockpiles, and to ensuring necessary medical expertise to operate complex medical equipment. Nor does this proposal seek to address the legitimate needs of developing countries as they face fiscal difficulties during a pandemic. Nor does it address the important intellectual property right questions that will arise once a vaccine is successfully developed. It is unrealistic to expect trade policy initiatives to solve every problem caused by the COVID-19 pandemic.