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COVID-19 AND WORLD TRADE: IN THE EYE OF THE PERFECT STORM?

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The collapse of world trade in 2020 due to lockdowns in response to the COVID-19 pandemic has fuelled a rethinking of globalization, with policies being reoriented towards strategic autonomy and local production by means of near-shoring and in-sourcing. Comparing the impact of the COVID-19 trade shock to the Great Depression, this article focusing on resilience and recovery argues that international value chains and the global trading system have helped to weather the impact of the global unprecedented response to a health shock.

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I. INTRODUCTION

In response to the outbreak of COVID-19 in early 2020, China imposed strict lockdown measures. The health policy measures, in particular, the strict shelter at home orders, and the closure of firms had an impact on Chinese production, imports and exports and, as China is a major trading country and a hub of international value chains, that impact was global as well.

The Chinese health policy measures did not stop the spread of the virus that arrived soon in Europe and somewhat later in North America. COVID-19 provoked unprecedented lock-downs when hospitals were overwhelmed with patients and death rates increased, and in Europe and North America the economy also came to a standstill. With the three major trading hubs of the world economy thus being closed down, world trade in goods and services (in particular travel and tourism) collapsed.

This article takes a closer look at global trade in goods, that is, world merchandise trade. The reasons for the focus on merchandise trade are two-fold. Firstly, better and more timely data exist for merchandise trade, basically because goods can be better observed than services. Secondly, that long time series exist for merchandise trade, allowing for an analysis that covers a long period of time. The analysis of world trade collapses needs to take a long-term perspective because these events are rare by historic standards and a shorter period of time would ignore what we can learn from earlier episodes.

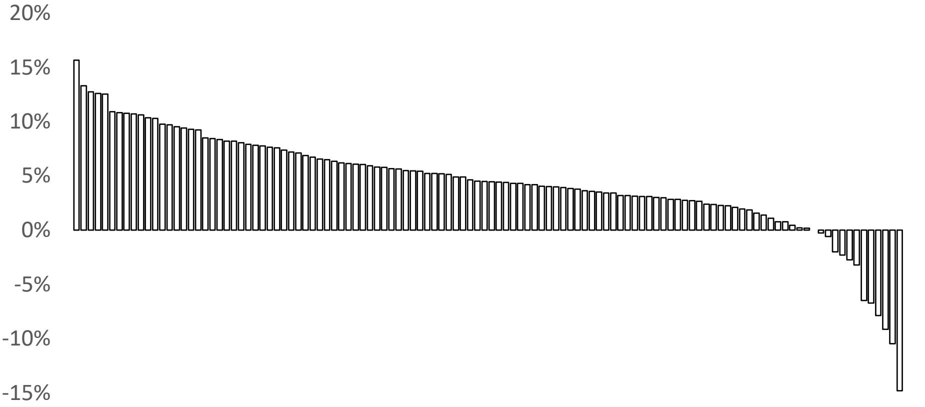
Real contractions of world trade, have already been observed twice since the start of the century – during the Great Recession in 2008-09 and the COVID-19 pandemic in 2020-21 – both being extraordinary events. Typically, world trade has historically been on an upward trend, as illustrated by the development of the world merchandise trade volume in Figure 1. Using annual trade data for the period 1881−2020, inclusive, the top panel of Figure 1 illustrates the infrequency of negative annual growth rates for world merchandise trade: ninety per cent of the annual real growth rates are positive. Only some ten percent of the growth rates are negative. Decreases in the volume of world merchandise trade are thus relatively unique in recent history, but they do occur.

It is, however, not only the fact that negative world trade growth happens to occur with a very low frequency which makes the 2008-09 and 2020-21 world trade collapses intriguing phenomena. The actual strength of the decrease is also remarkable, as illustrated by the bottom panel of Figure 1, that identifies three decades consisting of several recurring contractions of the world merchandise trade volume.

These phases of deglobalisation are: first, the Great Depression (marked in black), second, the oil crises of the mid 1970s and early 1980s (marked in grey) and, third, the recent two trade collapses (the Great Recession and the collapse during the early phase of the COVID-19 pandemic). The trade collapses of the 21st century are both in the top 3 of contractions observed since 1880. Importantly, the two recent collapses thus stand out because of both - their frequency as well as their strength, suggesting that global trade may be at risk at an intensity only observed during the Great Depression in the 1930s. This risk is, moreover, further increasing due to the economic sanctions in the context of the Ukraine crisis.[1]

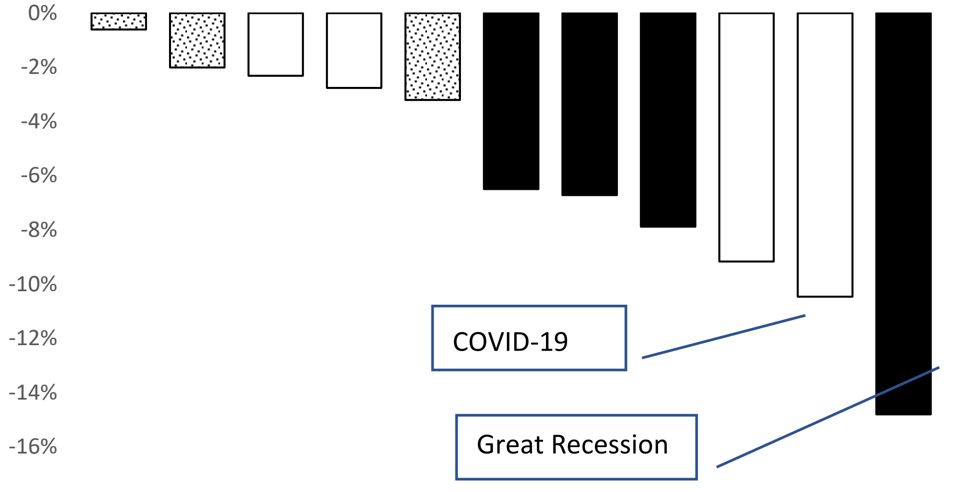
Figure 1. Contractions of world merchandise trade are exceptional.

Panel a) Real annual growth world trade 1881-2020



[1] Sylvanus Afesorgbor & Peter van Bergeijk, *Economic sanctions will hurt Russians long before they stop Putin's war in Ukraine,* THE CONVERSATION (Mar. 1, 2022), https://theconversation.com/economic-sanctions-will-hurt-russians-long-before-they-stop-putins-war-in-ukraine-178009. Peter A.G. van Bergeijk, Economic sanctions and the Russian war on Ukraine: a critical comparative appraisal, ISS working paper 699, Erasmus University Rotterdam.

Panel b) Real annual contractions world trade 1881-2020



Note: 1930s in black, oil crises contractions (1975-1982) in gray

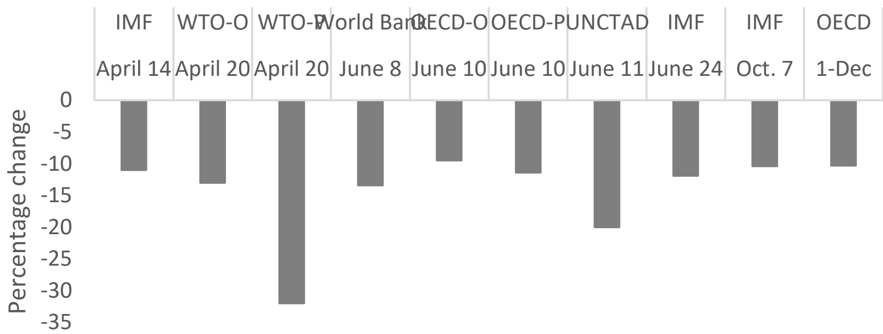
Source: updated from Peter A.G van Bergeijk, On the Brink of Deglobalization: An alternative perspective on the causes of the world trade collapse (Edward Elgar Publishing) (2010).
** Figure 1.3, p. 8 using calculations based on World Bank World Development Indicators accessed February 22, 2022, average of series NE.EXP.GNFS.KD and NE.IMP.GNFS.KD*

In this article, we will first take a closer look at these events. Section 2 puts the collapses of the world merchandise trade volume during the 1930s and in the first part of the 21st century further into historical perspective, while paying special attention to differences and communalities between the two periods. We will see that the resilience during the two recent trade collapses was remarkable and that this is related to the avoidance of protectionism, the maintenance of long-run relationships in international value chains, and the existence of a multilateral trading system. Section 3 then discusses the threats to these stabilising factors that can be observed in strategic trade policy developments of the major trading blocs: 'America First', 'Made in China 2025',the European Union's (EU) 'Strategic Autonomy', and the trade policy responses to the COVID-19 that have increased the stakes. Section 4 draws conclusions.

II. A HISTORICAL PERSPECTIVE ON THE GREAT TRADE COLLAPSE AND THE COVID-19 CRUNCH

The impact of COVID-19 on world trade was, from the start, a cause for grave concern to international policy makers. Projections for the contraction of the annual volume of world trade in 2020 ranged from minus 10 to minus 32 percent (Figure 2). Currently, the International Monetary Fund (IMF) (2022)[2] estimates the contraction for the year at -8.2%.[3]

Figure 2. Forecasts for the volume of world trade (international economic organisations; forecasts at different dates in 2020)



Source: Updated from Gerdien Meijerink et al, Covid-19 and world merchandise trade: Unexpected resilience (Oct. 2, 2020) https://voxeu.org/article/covid-19-and-world-merchandise-trade.

Note: O = Optimistic scenario, P = Pessimistic Scenario

The reports of the expected dearth of the global merchandise trade volume, however, were – with hindsight – quite exaggerated. Admittedly, the fall in world trade had initially been exceptionally strong, indeed. Recovery, however, set in early, compared to the two major historical episodes of trade collapse during the Great Recession and the Great Depression, suggesting stronger resilience of world trade

[2] IMF, *Rising Caseloads, a Disrupted Recovery, and Higher Inflation,* World Economic Outlook Update (Jan. 2022) [hereinafter *IMF Report*].
[3] Economic data are being revised for a considerable period after the end of a year. *See* Peter A.G van Bergeijk*, The accuracy of international economic observations,* 47(1) BULLETIN ECON. RES. 1-20 (1995) and Peter A.G van Bergeijk, *Making data measurement errors transparent: The case of the IMF*, 18(3) WORLD ECON. (2017).

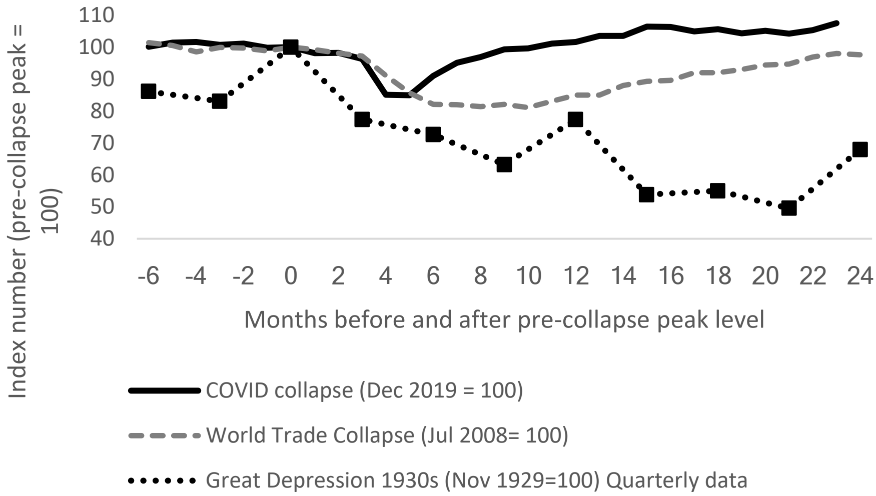
than anticipated by the international organisations.[4] Figure 3 compares the developments of the world merchandise trade volume during the three major world trade collapses that occurred during the Great Depression in the 1930s, the financial crisis in 2008-09, and the lockdowns during the first wave of the COVID-19 pandemic.

The comparison starts six months before the pre-trade-collapse peak that we use to identify period 'zero'. The contractions in 2008-09 and 2020, both started to bite after a quarter but in the fourth month of the COVID collapse, world trade was already 15 percent below previous peak level, while this was 'only' 8 per cent during the 2008-09 World Trade Collapse. Global merchandise trade in May 2020, however, bottomed out, and full recovery was achieved in October 2020. At the comparable point of the 2008-09 trade collapse, the volume of world trade was still 17% below pre-crisis peak level. In the 1930s, world trade one year into the collapse was 28% below pre-crisis peak level, with further decreases to 50% below pre-crisis peak level on the horizon. Clearly, the two world trade collapses before the COVID-19 contraction were both deeper and much more protracted.[5]

[4] Similar resistance can be observed with respect to capital flows such as remittances and Official Development Assistance and to a somewhat lesser extent for Foreign Direct Investment. *See* World Bank, *COVID-19 Crisis Through a Migration Lens*, Migration and Development Brief 35 (2021) and U.N. Conference on trade & development, *Global Investment Trend Monitor, No. 39*, U.N. Doc. UNCTAD/DIAE/IA/INF/2021/2, (Oct. 18, 2021).

[5] PETER A.G VAN BERGEIJK, DEGLOBALIZATION 2.0: TRADE AND OPENNESS DURING THE GREAT DEPRESSION AND THE GREAT RECESSION (Edward Elgar Publishing) (2019) [hereinafter Bergeijk (2019)]; PETER A.G. VAN BERGEIJK, PANDEMIC ECONOMICS (Edward Elgar Publishing) (2021).

Figure 3. Comparing the COVID collapse to the 2008-09 world trade collapse and the Great Depression.



Source: Updated from Sylvanus Kwaku Afesorgbor et al, Covid-19 and the Threat to Globalization: An Optimistic Note 29-44 (Elissaios Papyrakis ed., Springer) (2022).

The resilience of world trade during the two most recent trade collapses has drawn scientific attention;[6] the historic comparison with the 1930s, however, may be more relevant than the differences and communalities between the World Trade Collapse and the COVID-19 trade shock.

A. Commonalities

From this historic perspective, the 'Roaring Twenties' of a century ago and our own epoch (the 'Roaring 2000s') have a lot of similarities (Table 1). The starting point just before the onset of crisis is one of significant optimism and confidence in the future possibilities and persistence of globalisation. Markets are open and international, if not global, and capital flows freely cross borders at an unprecedented level and speed. In the daily life, completely new products, financial innovations and an improved life expectancy create hope and strengthen confidence. New industries boost productivity and living standards and fuel stock exchange booms. A cluster of

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[6] Peter A.G van Bergeijk et al, *Heterogeneous economic resilience and the great recession's world trade collapse,* 96(1) PAPERS IN REGIONAL SCIENCE 3-12 (2017); SYLVANUS KWAKU AFESORGBOR ET AL, COVID-19 AND THE THREAT TO GLOBALIZATION: AN OPTIMISTIC NOTE 29-44 (Elissaios Papyrakis ed., Springer) (2022).

trade enhancing factors are also key in understanding these periods, that, although separated by a century, share a common belief in globalisation as an unstoppable force. This cluster covers key technological innovations, long-run reductions of trade costs, and new modes of transportation and communication. The world's 'mental horizons' were shrinking so that new far-away markets were increasingly becoming realistic opportunities. In technical economic terms, the extent of potential markets increased significantly. That outlook, however, changes dramatically.

Table 1. Differences and communalities of the Great Depression and the 21st Century

	1930s	21st century
Long-run reductions of trade costs	●	●
New modes of transportation	●	●
Revolution in communication	●	●
Entry of new countries (recent capitalist countries)	●	●
Key innovations	●	●
Financial innovation and capital account liberalization	●	●
Changing hegemony	●	●
Pandemics	●	●
Banking and financial crisis	●	●
Substantial presence of international value chains		●
Multilateral trade governance		●
Protectionism	●	
Initial international policy coordination		●

First and foremost, there is the impact of the financial crisis that gives rise to the idea of secular stagnation, thereby increasing uncertainty. In the international arena, the erosion of the hegemon's position and the emergence of previously peripheral countries in the global trade system are important elements. This is because countries in the periphery grow faster than the rich industrial countries in Europe and North America, and this convergence with (if not competition from) the previous-outs creates doubt on the future rules and norms of the world trading and investment system. Connectivity increases and global flows of people make a globalised world more vulnerable to the spread of contagious diseases. To some observers the Spanish Flu and COVID-19 pandemics could be signalling that the world has integrated too fast, and although this is an exaggeration, these pandemics are definitely a reminder that globalisation also carries a cost that is often neglected. Pandemic risk has been associated with global travel, human–wildlife interaction, intensification of global food production, and densification of population.[7]

[7] Peter Daszak, *Anatomy of a pandemic,* 380 THE LANCET 1883–84 (2012).

B. Differences

Of course, important differences can also be observed between these two periods. From a purely scientific point of view, the differences are excellent news, because we could not learn if the Roaring Twenties and the Roaring 2000s were identical twins. Moreover, from a policy perspective the dissimilarities, as we will see, are even better news. After all, these differences may to a large extent explain why the disastrous trajectory of the 1930s was avoided, despite the fact that already two major trade collapses have occurred in the current century.

One important difference is the role of international networks of firms that self-organise into international value chains. Trade in the 1930s was mainly inter-industry (that is, countries exported and imported dissimilar goods) and based on absolute and comparative advantages. Modern trade predominantly is intra-industry with the export and import of similar goods by the same country, although often at different stages of production. The mainstream analysis has argued that such networks are a key driver of recent trade collapses, as problems in one country spill-over to other countries, both downstream and upstream. To the casual observer this is what happened during the Great Recession when faltering demand in the USA impacted emerging markets and developing countries as well as during the COVID-19 pandemic when lockdown measures restricted supply and thereby created shortages all around the world. These observations are missing two points. The first is the obvious argument that the same mechanism enhances the speed of recovery: once the trade system gets into reserve, world trade recovers faster than without international value chains. The second point is less obvious. Trade in international value chains is often based on trust and long-run relationships that, for example, enable risk-sharing and the provision of informal trade credit between partnering firms.[8] Trust is not destroyed by common adversity and may be one reason why trade relationships have been so quickly revived after the recent trade collapses.[9]

Policy-wise, the availability of the multilateral trade governance of the World Trade Organization (WTO) stands out as a saving buoy for the Great World Trade Collapse and the COVID-19 trade shock. It is true that trade governance was

[8] Peter A.G van Bergeijk, *The world trade collapse and international value chains: A cross-country perspective*, 27(1) INT'L. ECON. J. 41-53 (2013); Kim Tùng Đào & Peter A.G. van Bergeijk, *Global Trade Finance, Trade Collapse and Trade Slowdown: A Granger Causality Analysis* (Intl. Institute of Social Studies, Working Paper No. 633, 2018).

[9] *C.f*. Gary Gereffi et al., *Resilience Decoded: The Role of Firms, Global Value Chains, and the State in COVID-19 Medical Supplies*, 64(2) CAL. MANAGEMENT REV. 46-70 (2022).

severely compromised by the US, upholding appointments in the appellate body,[10] but the consequence was not a return to an epoch of rogue trading since the majority of countries exercised restraint and adhered by and large to the rules and regulations of an open multilateral trading system.

Indeed, the most important difference in my view is the fact that tit-for-tat protectionism was avoided in recent times. In the 1930s, countries were leapfrogging beggar-thy-neighbour policies, competitive devaluations, tariff wars, and buy-national procurements created the tsunami of protectionism that, as illustrated in Figure 4 , led to the contraction of world trade that actually led to a world that was less open in the 1950s than at the start of the 20th century. In recent times, we have seen problems in currency alignment and the Trump trade wars, but the point is that this never became a self-reinforcing problem of ever-increasing protectionism. Counter measures were taken, but the targets of foreign beggar-thy-neighbour policies always exercised restraint. In this sense, one of the major lessons of the 1930s was well received in policy quarters.

III. Strategic Autonomy

There is, however, an area where concern is in order: the tendency towards deglobalisation that can be discerned since the start of the Great Recession in 2008.[11] The strive for strategic autonomy is one of the symptoms of the deglobalisation phase that characterises the current international trading system. Figure 4 illustrates that openness since 2008 has been on a capricious but clearly downward trend, as illustrated by the 6-year moving average (the dashed line in Figure 4).

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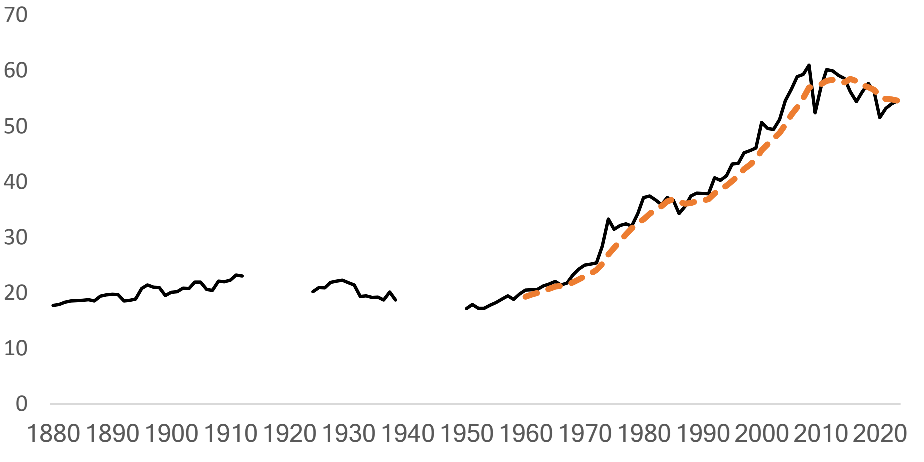
[10] Kristen Hopewell, *When the hegemon goes rogue: leadership amid the US assault on the liberal trading order*, 97(4) INT'L AFFAIRS 1025–43 (2021).

[11] Early publications on deglobalization include Bello (2005) for a normative view and Hillebrand (2010) for a quantitative scenario analysis. *See* WALDEN BELLO, DEGLOBALIZATION: IDEAS FOR A NEW WORLD ECONOMY (Zed Books, 2005) and E. E Hillebrand, *Deglobalization scenarios: who wins? Who loses?,* 10(2) GLOBAL ECON. J. (2010).

Figure 4. Openness of the world economy (1880-2023)



Note: - - - - 6 year moving average

Source: Updated from Peter A.G van Bergeijk, Deglobalization 2.0: Trade and Openness During the Great Depression and the Great Recession (Edward Elgar Publishing) (2019) using World Bank World Development Indicators (accessed January 21, 2022) and IMF (2022) forecasts.[12]

More important than the numbers, however, are the qualitative changes in the field of trade policy that have gained ground during the last decade, and in particular, the re-evaluation of the mutual dependency that is inherent to international specialization. The three major trade blocks have their own guise of this re-evaluation: 'Make America Great Again', 'Made in China 2025' and the EU's 'Strategic Autonomy' are all fruits from the same tree.[13] Indeed, the analytical tools, findings, and policy implications regarding neo-mercantilism[14] and strategic trade

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[12] IMF Report, *supra* note 2.

[13] Bergeijk (2019), *supra* note 5; Mehtap Akgüç, *Europe's open strategic autonomy: Striking a balance between geopolitical, socioeconomic and environmental dimensions*, (European Trade Union Institute) (2021); Ryan, Michael & Valbona Zeneli, *America is Back. Is Europe Back Too*?, 66 Orbis 14-25 (2022).

[14] The key characteristic of neo-Mercantilism is the idea that a country could and should benefit at the expense of other countries and that exporting is better than importing and can be recognized in many recent theories and policies. The idea that exports are superior to imports is simply wrong: just as consumption is the ultimate goal of production, it is importing that is the ultimate goal of exporting. Indeed, economic growth requires imports of capital goods, raw materials, intermediate goods and essential consumer goods. A key element of the neo-Mercantilist approach is the view on trade as essentially a zero-sum game which implies that surpluses on one's own trade balance are to the detriment of other

policy apply to our current situation as well.[15] The main issue here is that trade policy arguments that are key for small open economies, including the analytical finding that unilateral steps towards trade liberalisation are welfare enhancing, do not apply when we think about the largest actors in the world trading system. Large economies with monopolistic (supply) and monopsonistic (demand) market power can realize an improvement of their terms of trade when they restrict their demand and/or supply on world markets.[16] Typically, the costs of trade-restrictive policies are relatively small for large countries because large players are able to pass on these costs to their smaller counterparts.

The COVID-19 pandemic has brought the issue of 'strategic dependence' again on the policy agenda as the impact of international value chains has become clear in terms of shortages and scarcity driven price increases. Hence, the buzz words of trade policy makers have changed from out-sourcing and off-shoring to in-sourcing and near-shoring.[17]. The vaccines and the scarcity of medical equipment have also brought to the fore export restrictions and intellectual property rights restrictions imposed by the advanced economies.[18] While such restrictions may seem logical to national health care policy makers under pressure of an unfolding pandemic, they do not add value and, at most, buy very limited time and often are counterproductive. An example is the finding that the Trump tariff war against China actually reduced the availability of masks, face shields, respirators, and

countries and thus reduce their capacity to arm themselves and wage (economic) war and vice versa. While theories inspired by this idea have influenced policy making to some extent, the revival of Mercantilism and the transparency of its application towards countries with which no clear military conflict exists, is noteworthy, also from a historical perspective.

[15] If you write as long on international trade economics as I do, then old work becomes topical again due to the policy cycle in trade policy making, *See* Peter A.G van Bergeijk & Dick L. Kabel, *Strategic trade theories and trade policy*, 27 J. WORLD TRADE, 175-186 (1993). While the characters on the world stage have changed the analysis and implications survived three decades and have a direct bearing in today's trade policy context.

[16] PETER A.G. VAN BERGEIJK, ECONOMIC DIPLOMACY AND THE GEOGRAPHY OF INTERNATIONAL TRADE (Edward Elgar Publishing) (2009).

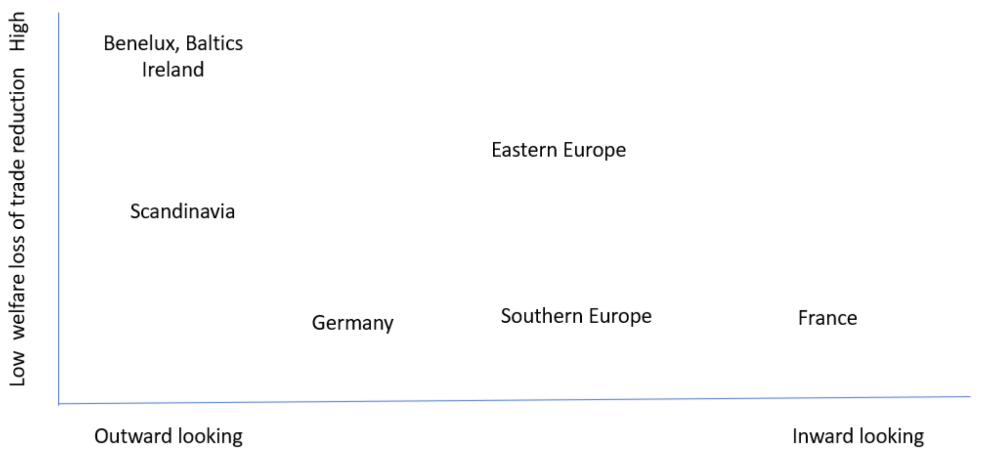
[17] Alexandre Gielens, How will the backshoring trend evolve after the COVID-19 crisis? Towards a new paradigm of regionalisation? (2021) (Thesis, Louvain School of Management) (on file with DIAL.mem, Université catholique de Louvain).

[18] 2021 COVID-19 AND TRADE POLICY: WHY TURNING INWARD WON'T WORK (Richard E Baldwin & Simon J. Evenett eds., 2021); Simon Evenett, et al., *Trade policy responses to the COVID-19 pandemic crisis: Evidence from a new data set* 342-64 (World Bank, Working Paper No. 9498, 2021); Bernard Hoekman et al., *COVID-19, public procurement regimes and trade policy* 409–429 (World Bank , Working Paper No. 9511, 2021); Peter A.G van Bergeijk, *The political economy of the next pandemic,* 14(1) REV. ECON. ANALYSIS 29-51 (2022).

protective garments before the outbreak of COVID-19, thus putting the US at a pandemic preparedness disadvantage.[19]

These mechanisms can be recognised more generally in economic studies on the impact of limitations of value chain activity and international trade. While this literature, of course, has been stimulated by recent experiences, this issue has been on the table for longer.[20] Firstly, recent economic research shows that in-shoring and near-sourcing and other forms of import substitution entail very high costs for small open market economies such as the Netherlands, Belgium, Ireland, and the Baltic States,[21] and also that greater autonomy can limit their pandemic resistance. In contrast, the costs in percent of production for the large world trading nations and institutions are small. Large countries may, thus, be tempted to consider the trade costs of strategic autonomy to be a small price for potential geopolitical gains. Interestingly, this heterogeneity can be recognized in the positions that EU member countries take on the European Commission's plans for open and strategic autonomy (incidentally, a *contradictio in terminis*). Figure 5 illustrates that the lower the costs of trade disruption, the more likely a member state is to embark on an inward-looking trade policy strategy.

Figure 5. Costs of value chain restrictions and policy orientation in the EU



Source: the author

[19] Chad P. Bown, *How COVID-19 Medical Supply Shortages Led to Extraordinary Trade and Industrial Policy* (Peterson Institute for Intl. Econ., Working Paper 2011-11, 2021).
[20] *See* Richard Baldwin & Rebecca Freeman, *Risks and global supply chains: What we know and what we need to know* (National Bureau of Econ. Research, Working paper 29444, 2021).
[21] Peter Eppinger et al. 2021, *Decoupling Global Value Chains* (Center for Economic Studies, Working Paper No. 9079, 2021).

Secondly, the problem with autonomy in the wake of a pandemic is that restricting trade and international value chain activities increases the reliance on the domestic sheltered sector of an economy that, as we have seen during the pandemic, is actually the most at-risk during periods of non-pharmaceutical interventions such as restrictions on group size, firm closures, and shelter at home strategies that all have been prominent instruments of health care policies.[22]

Thirdly, even for such obvious instruments as strategic stockpiles, empirical analysis reveals that alternative methods may be more appropriate.[23] Especially so because the two most important health care resources cannot be stockpiled. Machines and equipment can be produced in advance, but there is a clear limit to the number of well-trained medical staff and space for quality care during pandemics.

The conclusion of this section is clear. COVID-19 has further stimulated thinking about restrictive trade and investment policies that would set limits to international specialisation, and that may have shifted the balance in policy quarters. At the same time the pandemic, however, clarified that the costs of such a strategy, while small for the major trading nations are very high, if not prohibitive, for the small open economies that form the vast majority in the multilateral trade system. Most importantly, world trade has shown an unprecedented reliance to this shock, and this to a large extent may be due to the activities that are organised by private firms in global networks and international value chains. The outcome of these counterbalancing forces and powers is yet uncertain, but students of global world trade and investment governance are well advised to monitor developments closely because these antipodal forces will determine the future of the international trade system.

IV. CONCLUDING REMARKS

The collapse of world trade in 2020 due to unprecedented lockdowns in response to the COVID-19 pandemic has fuelled a rethinking of globalisation, with policies being reoriented towards strategic autonomy and local production by means of near-shoring and in-sourcing. This movement towards deglobalisation was already clear before the events that made such big impressions on our generation, including the Trump Presidency, Brexit, and the COVID-19 pandemic. Our comparison of the impact of the COVID-19 trade shock and the Great Recession on the one hand and on the other hand, the Great Depression, demonstrated significant resilience and

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[22] Barthélémy Bonadio et al., *Global supply chains in the pandemic*, 133 J. INT'L ECON. (2021).
[23] Wilgis J., *Strategies for providing mechanical ventilation in a mass casualty incident: distribution versus stockpiling*, 53(1) Respiratory Care 96–103 (2008); Martin I Meltzer & Anita Patel, *Stockpiling ventilators for influenza pandemics*, 23(6) EMERGING INFECTIOUS DISEASES 1021–22 (2017).

speedy recovery – beyond the dismal expectations of international organisations early in the pandemic. These findings strongly suggest that trade is not the problem but part of the solution. Indeed, international value chains and the global trading system in all likelihood have helped to weather the impact of the world's unprecedented response to a health shock. Rather than developing costly inward looking policy responses, the world should embrace the contribution of global trade and investment.