

## THE FUTURE OF INTERNATIONAL ECONOMIC INTEGRATION

As part of the 1947 General Agreement on Tariffs and Trade (GATT), a compromise on domestic socio-economic issues was struck and subsequently given the name 'embedded liberalism'. *The Future of International Economic Integration* explores the multiple dimensions of the Embedded Liberalism Compromise, to understand its contemporary influence on both the scope and application of international trade law and on the content and character of parallel domestic socio-economic policy space. Top international economic law scholars have contributed chapters that look at the four principal dimensions of the topic. It sets out the history and character of the Embedded Liberalism Compromise, explores the relationship between the Compromise and WTO law, explores areas of contemporary tension that invoke the principles of the Compromise such as human rights, cultural diversity and environmental protection, and investigates what future impact the Compromise might have on new trade and investment agreements.

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# The Future of International Economic Integration

THE EMBEDDED LIBERALISM  
COMPROMISE REVISITED

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## Foreword

What a pleasure it is to be writing, in 2018, a foreword for a collection of international economic law scholarship inspired by Ruggie's writings on embedded liberalism. Ruggie introduced his notion of embedded liberalism in the early 1980s, at a time when the GATT regime was facing pressures not unlike those it faces today.<sup>1</sup> Ever since then, although it has probably never been fully internalised by the mainstream of the discipline, it has acted as a continuous source of influence and inspiration for a significant strand of thinking and writing about the GATT/WTO system. It has been deployed for a number of different purposes by different writers: as a frame for diagnosing contemporary challenges, as a yardstick for evaluation and critique of the international economic order, as a way of exposing what has been forgotten in orthodox histories of the trade regime or as a touchstone for re-imagining future possibilities for international economic law. That thirty-five years after it was written the concept of embedded liberalism can form the foundation for such a rich vein of thinking as represented in these pages, is a powerful tribute not just to the creativity and intellectual innovation of the contributors to this volume, but also to the conceptual richness of Ruggie's original analysis, as well as the traditions of thinking on which he drew.

Ruggie himself developed the term 'embedded liberalism' to help him make a number of very specific arguments. One was to show that different periods in the history of the international economic order could, and should, be distinguished not just by reference to their degree of openness but also by reference to something he called 'legitimate social purpose'. To do so, he argued, would permit us to distinguish not just between more or less liberal international economic orders but also between different kinds of liberal trading order. In particular, he was keen to show that the post-World War II international economic order differed in fundamental ways from earlier liberal international orders, such as that existing before World War I: where the

<sup>1</sup> Ruggie, "International regimes, transactions and change: Embedded liberalism in the postwar economic order," *International Organization* 36, no. 2, (Spring 1982): 379–415.

latter was based on ‘orthodox’ or ‘laissez-faire’ liberalism, the former instantiated a different kind of liberal sensibility, which he called ‘embedded liberalism’.

As the chapters in this book make clear, the precise character of this ‘embedded liberal’ sensibility remains contested and to some extent a matter of perspective. For Ruggie, its core was a set of ideas about the proper role of the state in economic life, which had emerged across a number of industrialised countries in the decades spanning World War II. This was, of course, the set of ideas which produced and sustained the welfare state in its many forms across the industrialised world during this period. It was a political compromise which generally favoured markets, which assigned to the state a series of important roles in managing economic life, including guaranteeing economic stability, cushioning the domestic economy against international shocks and dislocations, providing extensive social protections particularly for more vulnerable groups and pursuing a degree of economic equality. This set of ideas, Ruggie shows, produced not only the domestic institutional forms we associated with the welfare state of the era but also a particular kind of international economic order. Rules governing international trade – and in this context Ruggie primarily means those found in the GATT 1947 – both presumed the existence of highly interventionist welfare states and also provided an authorising and enabling international environment for the pursuit of policies associated with welfarist state forms.

Thus, in Ruggie’s account, the GATT 1947 pursued trade openness but balanced this goal against an acknowledged need to secure economic stability and the imperative to minimise its costs. To this end, the process of liberalising international trade was structured in such a way (gradually, voluntarily and on a sector by sector basis) as to minimise its disruptive effects. In addition, GATT rules contained a range of exceptions to permit a range of domestic stabilisation policies and industrial policies pursued during this period, even where they had significant trade effects. And because such interventionist policies took so many different forms during this period, the result was a trading system which was highly tolerant of institutional diversity. In Howse’s subsequent formulation:

Trade liberalization was embedded within a political commitment, broadly shared among the major players in the trading system of that era, to the progressive, interventionist welfare state; in other words, to a particular political and social vision, *including at the same time respect for diverse ways of implementing this vision* – with greater use of microeconomic intervention, such as indicative planning and public enterprise in Europe and Japan, while tax-and-transfer approaches were more typical of North America, and certainly the United States.<sup>2</sup>

Embedded liberalism, in other words, entailed a commitment both to a particular form of state–market relations and to the value of diversity in its institutionalisation.

<sup>2</sup> Howse, “From politics to technocracy – and back again: The fate of the multilateral trading regime,” *American Journal of International Law* 96, no. 1, (2002): 94–117 at 97.

If Ruggie saw the core of embedded liberalism as a shared set of normative commitments, then, he also saw it as a body of rules and institutional forms and their modes of operation. Furthermore, and importantly, Ruggie uses the language of shared normative commitments in a particular way. These are not shared values in some straightforward personal sense: He does not argue, for example, that the key architects of the GATT 1947 were in some explicit sense all personally committed to an explicit and common sense of political purpose. Rather, the story he tells draws primarily on his observations concerning the content of GATT 1947 rules, the character of the institution of the GATT, its practical operation over decades and the patterns of international trade which it produced over time. Embedded liberalism was for Ruggie a way of describing the set of ideas and commitments which best explained these arrangements, and accounted for their character. He was, in other words, identifying the ideational predicate of observed legal and institutional structures, not (or not essentially) the personal commitments of particular influential individuals. Furthermore, and in part as a consequence, the set of ideas he identified are difficult to disassociate from the very specific forms of domestic interventionism which were associated with the welfare state during that period.

All of this makes it more complicated to grasp what it might mean to revive embedded liberalism in and for contemporary conditions. There is a useful contrast to be drawn here between what we might call ‘thick’ and ‘thin’ versions of ‘new embedded liberalism’. ‘Thick’ versions see in embedded liberalism the embodiment of a set of substantive political values and understand the task of reviving embedded liberalism to be the creation of an international economic order conducive to the achievement of those values. Different authors hew more or less closely to the way Ruggie framed those values almost four decades ago. For some, the core is social solidarity – embedded liberalism here means the pursuit of global economic integration in ways which ensure both that the benefits are shared and that the costs of adjustment are collectively shouldered. Others use the language of ‘social protection’, the prioritisation of ‘social’ over ‘economic’ values or retooled versions of the language of ‘stability’ and full employment. In some accounts, embedded liberalism acts as a cipher for regulated capitalism, a middle ground of sorts between market fundamentalism and a state-led economy. For Ruggie himself, in his more recent work, the core of embedded liberalism has been characterised as the reconciliation of international markets to ‘social values’ through ‘practices of domestic interventionism [which] would tame [their] socially disruptive effects’.<sup>3</sup> In this book, Moon and Reid explore the possibilities of re-imagining embedded liberalism through the

<sup>3</sup> Abdelal and Ruggie, “The principles of embedded liberalism: Social legitimacy and global capitalism,” in Moss and Cisternino (eds.), *New Perspectives on Regulation* (The Tobin Project, 2009) 151–162, at 153.

alternative but complementary frameworks of human rights and sustainable development, respectively.<sup>4</sup>

The contemporary moment in international trade politics is in many respects amenable to projects of this kind. Recall that Ruggie's story of embedded liberalism drew heavily on Polanyi's hugely influential account of the political economy of embedded and disembedded markets in *The Great Transformation*. As many have noted, including a number of the contributors to this book, one of the more persuasive available interpretations of the current backlash (such as it is) against international trade liberalisation is an essentially Polanyian one. In this account, the period of globalisation since roughly the 1980s is analogous to prior periods of market disembedding as described by Polanyi in the sense that it has led to analogous forms of economic instability, insecurity and inequality for those left behind. Viewed through a Polanyian lens, then, what we are seeing is precisely the second half of a Polanyian 'double movement' – that is to say, a new attempt by disaffected political communities to protect themselves from such effects through a process of 're-embedding' of the market. To the extent one accepts the historical parallel, then, the task for international trade lawyers appears clear, namely to re-constitute the trade regime by reference to a modernised version of embedded liberalism, understood primarily as the re-prioritisation of the goals of economic stability and security, social cohesion and broadly shared prosperity over those of openness and intensified competition.

The formidable practical and political difficulties of effectively pursuing such values at the domestic level in conditions of contemporary globalisation are a matter of very lively public debate. But it is also worth noting how, at the *international* level, a number of changes have occurred within the international trade regime itself which make a return to some 'thick' version of embedded liberalism in the WTO very difficult to pursue and even to imagine in concrete terms. As is well known, the move away from the embedded liberalism of the GATT 1947 to the neoliberalism of the late twentieth century gave rise to a new debate about the legitimacy and effects of the international trade regime. In that context, new criticisms of the international trade regime were made, that it was contributing to the erosion of the welfare state and to the global spread of the pro-market 'neo-liberal' state in all its variegated forms. For the most part, these concerns were articulated in the language of constraint and freedom: GATT/WTO law was criticised for imposing narrow limits on the permissible institutional forms of WTO members and for limiting their regulatory freedoms. In response, the regime's defenders rejected the idea that the WTO was ideologically partisan: It was, they suggested, merely a space for negotiations, its rules were largely neutral as to the purposes of economic regulation and there was no sense in which its members held any genuinely 'shared' political or ideological commitments. Taken together, the result of these two positions is a

<sup>4</sup> Chapter 4; Chapter 13.

discourse in which it is hardly even possible to argue that the international trade regime ought to – or indeed is able to – represent *any* ‘thick’ vision of substantive political commitments, whatever its ideological valence.

This is a significant obstacle to contemporary projects to revive embedded liberalism. It has, furthermore, been reinforced by at least two further structural changes to the regime over the last two decades. The first is the virtual universalisation of WTO membership, which has made it practically more difficult to speak of WTO law as instantiating some shared values across the membership as a whole. The second is the emergence of the ‘new regionalism’, which has decentred the role of WTO law as a vehicle and cipher for the character of the international economic order more generally. Both of these developments have eroded the traction of the concept of ‘collective purpose’ as an appropriate category of analysis for the international trading system.

The ‘thin’ version of ‘new embedded liberalism’ avoids these difficulties, and indeed may in part have emerged as a response to them. I noted above that embedded liberalism always entailed some degree of ambiguity in the sense that it entailed a commitment to a particular form of state–market relations and at the same time was constitutionally open to institutional diversity. ‘Thin’ approaches focus on the second aspect, imagining the revival of embedded liberalism in WTO law as essentially a process of re-establishing at the normative heart of the trade regime the central value of the toleration of regulatory and institutional diversity. It is well known that probably the most important debate within international trade law over last three or so decades has been the debate over the right to regulate. In that context, the transition from embedded liberalism to neo-liberalism has (rightly) been told as in significant part a story of the transformation of the GATT/WTO’s regulatory disciplines: from a relatively permissive approach centred on the core norm of non-discrimination, to a more intrusive approach focussed in addition on new norms relating to regulatory harmonisation and conformity with good regulatory practices. As a result, in much of this literature a return to embedded liberalism is broadly equated with reversing the turn towards more intrusive regulatory disciplines, and ensuring adequate regulatory space for WTO members. It is true that even in such accounts the notion of embedded liberalism retains important substantive normative elements (roughly, the prioritisation of ‘non-trade’ over ‘trade’ values when they unavoidably conflict) – but the point is that ultimately the legal implications of these normative elements are imagined almost exclusively in terms of the relaxation of regulatory constraint.

There is much to like about this vision. It is certainly true that toleration of regulatory and institutional difference was at the heart of the normative vision of embedded liberalism. It is also true that one of the most salient differences between the period of embedded liberalism and that which came after it is the degree to which the latter is characterised by an aspiration towards institutional and regulatory harmonisation, or at least deep integration, within certain bounds. For that reason,

Ruggie's story draws attention to the legal flexibilities, exceptions and qualifications contained in the GATT 1947 as some of his most important illustrations of the embedded liberal character of that regime.

But it is also true that, for Ruggie, embedded liberalism is not *just* about providing space. Instead, he describes the establishment of the post-World War II international economic order (including the GATT, but also more generally to include the other Bretton Woods institutions, and indeed beyond) as providing in more positive terms some of the enabling international conditions for the consolidation and development of the welfare state in the industrial world. How did it do this? For one thing, by limiting both capital mobility as well as freely floating exchange rates, it shielded governments from some of the pressures they might otherwise face in the pursuit of their interventionist industrial and macroeconomic policies. Furthermore, by focusing the most intensive liberalisation efforts on intra-industry trade flows, the trade regime helped to produce trade flows which generally produced comparatively few rapid structural changes to industrialised economies. In addition, and more generally, since many of the policies pursued by industrial states during these years could be (and in some cases were) understood as highly distortive of trade flows, the trade regime played an important role managing and defusing resultant trade disputes or justifying them by reference to a particular understanding of fairness as reciprocity in market access commitments. That is to say, the trade regime became a venue in which many of the trade frictions that could have arisen as a result of the huge variety of forms of intervention which emerged in the post-World War II period were minimised, recharacterised or legitimised as the simply the background cost of doing business or of participation in the system. Without such efforts, the tensions caused by the pursuit of such policies in the industrialised world may have made such policies more difficult to pursue.

One of the lessons of Ruggie's story then – and in this he mirrors Polányi, on whom he drew extensively – is that there is a complex co-constitutive relationship between international and domestic economic order. The post-World War II order worked in the way that it did (with all its flaws and weaknesses), Ruggie argues, not just because the international trade regime stepped out of the way, as it were, but because it positively enabled particular kinds of domestic state forms. To the extent that this is true, it raises important questions for the contemporary emphasis on policy space as the normative core of embedded liberalism. It turns out that it is important to ask of any international economic order and any set of international economic rules, not just whether and how it constrains states' institutional choices, not just what regulatory measures it formally prohibits – but also what institutional and regulatory forms does it more positively enable and sustain? To what extent and in what ways may it provide a structure in which certain kinds of state forms find it more or less easy to thrive – and if so, for what reasons? Similarly, it follows that the question of how to revive a 'new embedded liberalism' includes, but goes beyond, the question of how to ensure that regulatory and institutional diversity and innovation are legally permitted. It may also

include the question of what international conditions might positively be required to produce and sustain such diversity?

The further we pursue this line of thinking, the closer we get to an important and highly productive ambiguity in the concept of ‘embeddedness’ – an ambiguity which is very visible in the work of Polányi, even if it is less obvious in Ruggie’s subsequent elaboration of it. On one hand, Polányi coined the term ‘disembedded’ markets to describe an economic system in which markets are permitted to operate outside direct social and political control – that is to say, a form of economic life which is governed purely by market logics to the exclusion of ‘social’ values, logics and bonds. Thus, the ‘embedding’ of markets in this first Polányian sense refers to the subjection of market dynamics to political control in the form of social protection, decommodification of labour and so on. In addition, however, Polányi also put the notion of embeddedness to another use as well, namely to express the artificiality and historical contingency of the idea that the ‘economic’ and the ‘social’ represent distinct and independent spheres. In this aspect of his argument, Polányi is one of the most powerful voices in the anti-naturalist tradition of thinking about markets – a tradition which sees markets not as pre-political or pre-social but, rather, as fundamentally produced by politics and law. In this sense, then, it was important for Polányi to stress that ‘disembedded’ markets – that is to say, the sorts of free markets associated with laissez-faire liberalism – are not a natural state of affairs but rather the artificial result of a concerted political project undertaken over the nineteenth century.

Anti-naturalist thinking about markets has a long and respectable history, and it is reasonable to assume that it was familiar – in its general impulse, even if not in the particulars – to a number of those involved in establishing the GATT 1947 at its inception. But in contemporary international economic law circles it is no longer well known, and it may end up being one of the most enduring legacies of Ruggie’s writing on embedded liberalism to put us back in touch with it, even if at one remove. This is because a number of the challenges facing the trade regime today may require us to move beyond a reified and naturalised conception of market relations in a more Polányian direction. The experience of the last four decades has shown that global economic integration does not lead to institutional homogeneity across countries – on the contrary, today’s global economy has been produced by deepening and intensifying interactions between countries which remain institutionally highly diverse in terms of the precise configuration of state–market relations they instantiate. Such institutional diversity is a strength of the global economy, but it is also a source of profound trade frictions since the institutional structure of a country’s economy can profoundly affect the competitiveness of its firms on international markets. The US–China relationship is of course the central example of this, but the issue is more general one and only likely to become more so in the future. The question of how to address the question of institutional diversity – how to set the outer boundaries of acceptable domestic institutional arrangements – will be one of the most significant tasks for in international trade law in the coming decades.



One technique for doing so, which has begun to have greater salience over the last few decades, has been to attempt to distinguish between legitimate and illegitimate institutional structures by reference to the degree of a state's deviation from an (implicit) standard of normal or idealised market institutions. For example, WTO subsidies law identifies the existence of a subsidy by comparing the position of a purportedly subsidised firm against a market benchmark to determine whether or not that firm has received a 'benefit' from the state. In addition, the question of whether domestic prices must be used for the calculation for 'normal value' in an anti-dumping investigation depends in part on the degree to which those prices are distorted or not 'market-determined'. More generally, disciplines on state-trading enterprises and state-owned enterprises in WTO law and more recently FTAs also appear to impose disciplines which seek to ensure that such enterprises do not deviate excessively from normal market behaviour. The interpretation and application of such tests will vary significantly depending on the approach which is taken to defining the content of the market benchmark. On one hand, it is perfectly possible to do so in a way which is premised on understandings of markets which acknowledge the many different forms that markets can and do take without idealising one and which recognise that the institutional structure of a market can be as much an expression of a public's values and collective aspirations as public interest regulation. On the other, however, it is also possible to apply these legal disciplines using a singular or idealised conception of market relations as the normative benchmark – with its attendant risks of institutional dogmatism and conceptual confusion. Particularly given their current position outside the mainstream of economic and legal thought, exploring the anti-naturalist conception of markets – exemplified in this context by Polanyi's and his notion of embeddedness – is likely to provide the intellectual tools to help us think through the problem of institutional diversity more clearly and rigorously.

Ruggie's narrative of embedded liberalism was written at a time when the GATT regime was facing pressures not unlike those it faces today. The revisionist history that he told in the 1980s remains as compelling and relevant as it was then, both as a framework for diagnosing the sources of contemporary political unrest over globalisation and as a repository of still fresh understandings of what the trade regime is for. In telling this story, Ruggie found it useful to turn to traditions of economic thinking which were already marginalised at the time but have only become more so over time. His story therefore also helpfully re-introduces us to a tradition of economic thought which cuts across many of our most cherished conceptions of what markets are and how they are created. Little wonder, then, that embedded liberalism remains a vivid and evocative frame for new thinking about the international economic order. As the pages of this book attest, the concept of 'embeddedness' is a rich resource for initiating new conversations about potential futures for the trade regime, and this volume is a most valuable addition to them.

Andrew Lang

## Preface

The idea for this collection was originally generated by the editors in late 2015, and the chapters were primarily developed through a workshop held at the University of New South Wales (UNSW) in Sydney in February 2016. We would like to express our gratitude to UNSW Law for its financial support for the workshop. Draft papers were presented to a closed audience and discussed in depth and subsequently revised. This allowed the book to be developed as a relatively cohesive whole while retaining the voices and interests of the individual participants.

The international political climate has changed greatly throughout the genesis of this book, at times making it difficult to navigate new political terrain. However, it is evident that this topic has emerged as more significant than ever. We wish to thank the individual authors for their perseverance with the project. We also wish to thank our families for their unfailing support.

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Edited by Gillian Moon , Lisa Toohey

Frontmatter

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Acronyms

|        |   |
|--------|---|
| AB     | Appellate Body  |
| APEC   | Asia Pacific Economic Cooperation Forum                               |
| BIT    | Bilateral Investment Treaty   |
| BRICS  | Brazil, Russia, India, China, and South Africa                        |
| CAP    | Common Agricultural Policy  |
| CETA   | Comprehensive Economic and Trade Agreement                            |
| CPTPP  | Comprehensive and Progressive Agreement for Trans-Pacific Partnership |
| CSR    | Corporate Social Responsibility                                       |
| DSB    | Dispute Settlement Body   |
| DSM    | Dispute Settlement Mechanism  |
| DSU    | Dispute Settlement Understanding                                      |
| EEC    | European Economic Communities   |
| EU     | European Union  |
| FDI    | Foreign Direct Investment   |
| FTA    | Free Trade Agreement  |
| GATS   | General Agreement on Trade in Services                                |
| GATT   | General Agreement on Tariffs and Trade                                |
| GDP    | Gross domestic product  |
| GFC    | Global Financial Crisis   |
| IIA    | International Investment Agreement                                    |
| ICCPR  | International Covenant on Civil and Political Rights                  |
| ICESCR | International Covenant on Economic, Social and Cultural Rights        |
| ICJ    | International Court of Justice  |
| ITO    | International Trade Organisation                                      |
| ICSID  | International Centre for Settlement of Investment Disputes            |
| ISDS   | Investor-State Dispute Settlement                                     |

|               |   |
|---------------|---|
| MFN           | Most-Favored Nation                                   |
| NGO           | Non-Government Organisation                           |
| NT            | National Treatment                                    |
| OECD          | Organisation for Economic Cooperation and Development |
| PTA           | Preferential Trade Agreement                          |
| RIA           | Regulatory Impact Assessment                          |
| TBT Agreement | Agreement on Technical Barriers to Trade              |
| TPP           | Trans-Pacific Partnership                             |
| TTIP          | Transatlantic Trade and Investment Partnership        |
| UNCTAD        | United Nations Conference on Trade and Development    |
| US            | United States of America                              |
| WWII          | World War Two   |
| WTO           | World Trade Organization                              |