Introduction

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i.1 Introduction

Peace is the natural effect of trade. Two nations who traffic with each other become reciprocally dependent for if one has an interest in buying, the other has an interest in selling and their union is founded on their mutual necessities. But if the spirit of commerce unites nations, it does not in the same manner unite individuals. We see that in countries where the people move only by the spirit of commerce, they make a traffic of all the humane, all the moral virtues, the most trifling things, those which humanity would demand, are there done, or there given, only for money.¹

In his 1748 treatise, The Spirit of Laws, Montesquieu brilliantly captured the existing tension between the benefits and detriments of trade. ‘Commercial laws’, he further argued, ‘improve manners for the same reason that they destroy them’.² This pendulum swing between the need to legislate and the possible negative effects of the same legislation is very much perceived in today’s international trade, and, indeed, in international economic law (IEL). While the intellectual legacy of the Enlightenment liberals still largely informs the world of trade ideas, it has also been critically addressed by the new conceptual developments formulated in response to historical evolutions in order to trigger global changes.

By addressing the theoretical foundations of international economics, this introduction further elaborates on the concept of international economic law as the law supporting the architecture and functioning of international economic relations. In doing so, it positions

² Montesquieu, Spirit of Laws, p. 316.
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our own approach within the realm of international law and explains this textbook’s foundational principles and pedagogical choices.

i.2 The Law of International Economic Relations

How to define international economic law? What does it comprise of and what does it not cover? Is it public or private law? How international and truly diverse is it? Who are its subjects, actors and other recipients? Why has it been fragmented to the benefit of specialised domains like trade or international investment? Why is it important and timely to approach international economic law as a coherent and yet constantly evolving field?

International economic law has long been defined as the law of international economic relations among States. It is rooted in general public international law and addresses primarily those international economic relations in which the State is the main subject and actor. Yet with the development of international economics, decolonisation and globalisation, international economic relations have evolved dramatically towards much more complex realities. States and private actors interact at local, national, international, regional and global levels. These interactions shape and influence international economic law at its foundations, and in terms of its ability to adapt and provide legal tools to tackle contemporary issues. There is no fixed international legal order. Divisions between international public and private law are not so clear. International economic relations are fluid, in constant movement, and impact all spheres of human life. In addition, the institutions which have shaped the architecture of international economic law have been deeply challenged in their legitimacy and ability to deliver an effective as well as just and equitable world governance. The World Bank, the International Monetary Fund (IMF), the World Trade Organization (WTO), and regional structures like the European Union (EU) and the post-Second World War institutionalisation of international economic relations are in need of great reform. While multilateralism is clearly weakening, alternative scenarios are still unclear, with apparently contradictory trajectories in the direction of a renewed bilateralism on the one hand, and multiple mega-regionalist efforts on the other.

In this general context, defining international economic law proves challenging. But some principles are in place. International economic law is the law of international economic relations with the State as the primary, but not the only, subject and actor. It encompasses a vast array of specialised topics, including trade, investment, finance, development and aid. It is, however, coherent if approached as a component of general international law resting upon the same core principles (sovereignty, equality, *pacta sunt servanda*, good faith, peaceful settlement of disputes, etc.) and the same sources as those outlined in Article 38 of the Statute of the International Court of Justice (ICJ). This defragmented vision supports the unity and diversity of international economic law. It explains and justifies the need for a holistic approach in which other fields of international law (such as human rights or labour, the environment or tax, investment or monetary laws) are not artificially removed from international economic agreements or dispute settlement. Lastly, in line with the vision...
and conceptual underpinning of this textbook, international economic law is no longer – and in any case, should not be – a thing of the West or the new emerging powers. If not yet truly decolonised, it has been transformed already by the practice of the Global South and will evolve towards more diversity, more complexity, and possibly a new form of universalism.

i.2 The Law of International Economic Relations

i.2.1 Economic Foundations

The term ‘commerce’ derives from the Latin commercium, itself composed of cum (together) and merx (merchandise), while ‘trade’ comes from Middle English (path, course or track). The exchange of merchandise along many different paths has indeed marked the history of humanity since antiquity. Trade routes were designed as early as the third millennium BCE, when the Harappan civilisation of the Indus Valley, the ancestors of today’s South Asians, traded with the Sumerians in Mesopotamia, the fertile crescent now roughly corresponding to Iraq and some parts of Syria and Turkey. The Silk Road, an ancient trade trail, whose name was inspired by the commerce of silk by the Chinese Han dynasty (207 BCE–220 CE), connected the East and West through a vast network of trade routes. Much later, Vasco da Gama took over the spice trade from the Arab powers when, in 1498, he discovered the sea route to India around the Cape of Good Hope and reached Calicut (now Kozhikode). With greater trade came greater interests and greed. The Portuguese, Spanish, Dutch, British and French developed world ambitions through trade, often by using the vehicle of private enterprises, as powerful as today’s mega-multinational companies. Backed by various European States that had commercial and military objectives, these companies were key instruments in the States’ plans for territorial conquest to achieve economic growth and political hegemony. The various East India Companies created by the Dutch (1602–1799), the French (1664–1769) and the British (1600–1874) reigned over commerce with the East. The latter served as the main device for the subjugation and colonisation of India (see Chapter 11). The sinister reality of corporate looting as the tool of colonial policies claiming a civilising mission echoed another tragic history, that of the trade in humans. An estimated 17 million Africans were shipped across the Atlantic by European powers from the sixteenth century, for over 400 years. While human trafficking and slave routes were not new, European powers systematised, legalised and legitimised this trade, notably with the infamous Code Noir (Black Code), designed by Colbert for French colonisation. This

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3 On the Harappan civilisation and how to trace history on the basis of new DNA-related techniques, see T. Joseph, Early Indians: The Story of Our Ancestors and Where We Came From (New Delhi: Juggernaut Books, 2018), p. 256.
8 The Code Noir, drafted by Jean-Baptist Colbert, was a decree passed by Louis XIV of France in 1685, to define, legalise and justify the condition and existence of slavery and slave trade.
triangular trade proceeded in three steps: ships left Europe for West and Central Africa with goods to be exchanged for slaves destined for America, where agricultural goods produced by the slaves were later brought to Europe.9

It was at this very key moment in the expansion of Europe that trade theorisation took shape with the work of Jean-Baptiste Colbert (1619–83) and Adam Smith (1723–90). Europe started to dominate not only trade, but also its conceptualisation and legitimation. This intellectual domination is still very much perceptible today, considering that the concepts forged from the eighteenth-century Enlightenment provide parts of the theoretical foundations of trade, and most trade textbooks offer only a Western-centric perspective.10 A true non-Western-centric and critical approach to the history of trade and trade law would require a dedicated study beyond the scope and objectives of this textbook, but it is important to bear in mind the above to understand trade theory and its implications over the centuries.11

The theoretical foundations of international economic law are indeed greatly inspired by international trade theory. International trade theory finds its roots in Europe and has been exported – if not imposed at the time of colonisation – to other continents. International trade theory blends international economic theory with international legal scholarship and jurisprudence. International trade theory still very much informs today’s international economic law framework, while it has also been critically addressed in the context of the socialist revolutions, decolonisation and the recent development of globalisation.

International economic law must first be approached from an economic theory angle or a political economy perspective, in which economics is understood in relation to other disciplines, from political sciences to history or sociology.12

**4.2.1.1 Mercantilism**

From the sixteenth to the seventeenth century, in Europe, mercantilism emerged as a practice and economic theory to promote the State’s regulation of the economy and as a tool to expand its power. While the term, which comes from the Latin mercari (to conduct commerce), was coined by the marquis de Mirabeau in France, it was later popularised by the Scottish economist Adam Smith in his 1776 magnum opus, *An Inquiry into the Causes and Nature of the Wealth of Nations*.13 Mercantilism appeared at the time

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of absolutism (Louis XIV in France) and the conquest of the New World, which corresponded with the beginning of a systematised and theorised colonisation. In this context, ‘The Prince’, whose power was based on the amount of gold he possessed and the taxes he collected, was to further his reign through industrialisation and commerce. In other words, the dominant thought was that wealth consisted of bullion, and for countries not possessing gold or silver, having a favourable balance of trade was the only way to secure wealth. Commerce was therefore aimed at the taking of other markets and territories to allow the State to have access to precious goods and materials, but not so much to trade freely and on an equal basis. Mercantilists were protectionists. They supported the industrialisation of their own nations, but not that of their colonies or competitors. A mix of defensive (protectionism) and offensive (industrialisation and exportation) policies had to be designed by the State to support its expansion. Mercantilism put economic theory at the heart of the public space. It took various forms, with Antonio Serra in Italy and his work on currency and balance of payments, Jean-Baptiste Colbert in France and his ‘Colbertism’, supporting a proactive State leading industrialisation and commerce, as well as ‘commercialism’ in England with Thomas Mun (1571–1641), an economist affiliated with the East India Company, and the German ‘cameralism’ advocating the centralised management of the economy.

The major assault on mercantilism did not come from political rulers, but from Adam Smith, who laid bare its inherent absurdities. It is partly in response to the mercantilists, and Colbert’s theory, that Adam Smith formulated his concepts of the wealth of nations. Smith, now seen as the founder of the British school of classical economics, emphasised the importance of specialisation (division of labour) and viewed international trade as a way to specialise in what one is best at. In *The Wealth of Nations*, Smith advanced a simple yet profound idea: countries can benefit by specialising in those industries at which they excel, and trading in or exchanging those goods with other countries that specialise in other industries. Smith noted, ‘if a foreign country can supply us with a commodity cheaper than what we can make, better buy it of them with some part of the produce of our own industry’. To use a simple example, if England was able to produce cloth more efficiently than Portugal, and Portugal was more efficient than England at producing wine, both countries would be better-off if they engaged in bilateral trade. Smith’s concept of division of labour and absolute advantage made a strong case for liberal trade and open markets.

Mercantilist theories are revisited today in the context of a contested globalisation, while some would like to favour import substitution based on ‘made in’ policies and to engage in more protectionist, tariff-based instruments.

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i.2.1.2 Comparative Advantage

Another classical economist, David Ricardo (1772–1823), further developed the idea of specialisation into the principle of ‘comparative advantage’. A truly remarkable and inspirational theory of comparative advantage underpins the economic argument for free trade. According to this theory, a country will specialise in the production of a good in which it has a comparative advantage – that is, where there is labour to produce relatively efficiently, with low opportunity cost.

These principles are detailed in all international trade textbooks. However, a short explanation is in order here. There is specialisation and comparison in trade, but in a rather sophisticated and evolutive fashion. In the example of England and Portugal, which is borrowed from Ricardo’s book, assume that Portugal is more efficient than England in making both cloth and wine. It is counterintuitive to suggest that England would still benefit from bilateral trade. It all depends on each country’s relative productivity in wine vis-à-vis cloth. The question can be framed as: is it cheaper to produce in England than to import from Portugal? What is the opportunity cost? Is it based only on labour and what labour costs to produce a given good? In assuming that it is, we can define the advantage of country A, where labour is cheap compared to country B, where it is not. When less labour is needed to produce a given good in one country, it has an absolute advantage in producing that good. The Ricardian model assumes international differences in the productivity of labour. It is often referred to as a one factor model. But the issue is that trade cannot be determined on an absolute advantage alone. Absolute advantage and comparative advantage differ. When trade comes into play, the price of a good is not only determined by domestic considerations like the cost of labour, but by supply and demand. The advantage is not absolute, but comparative. Also, countries produce and can hence specialise in a variety of goods. Not to mention that to trade, a country needs to take into consideration transportation and its cost. The reality of trade is naturally much more complex than initially envisaged in Ricardo’s 1817 book, The Principles of Political Economy and Taxation. States can make multiple policy choices based on domestic resources and other opportunities or constraints. But the Ricardian model, despite its relative simplicity, remains a very useful tool to conceptualise international trade. It shows that productivity differences play an important role in trade and that the trade advantage is comparative rather than absolute.

The essence of comparative advantage is that it is impossible for all countries not to have comparative advantage in something. Producing everything or focusing on self-sufficiency is not a goal to be emulated in itself. As Paul Krugman notes, international trade is about ‘mutually beneficial exchange’.

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i.2.1.3 More Complex Models
As trade has evolved, more complex models have been developed. These trade models introduce multiple factors. In the specific factor model elaborated by Paul Samuelson and Ronald Jones, factors of production other than labour are integrated. Land and capital play a particular role. From a one-factor model (labour) we can move to a three factors conceptualisation, with labour, land and capital. Labour is seen as a mobile factor, which could move from the production of one good to another, while land and capital are specific to the production of a given good. But the complex model, which has received the most attention, was developed by two Swedish economists, Eli Hecksher and Bertil Ohlin, the latter having received the Nobel Prize in Economics in 1977. This model is often referred to as the Heckscher–Ohlin theory or factor proportions theory. It focuses on labour and capital and emphasises the interplay between the proportion in which these factors are available in different countries and used in the same. According to this model, countries tend to trade goods that are intensive in the factor they have in abundance (labour or capital). A country’s advantage in production, according to the factor proportions theory, arises solely from the relative factor abundance. Based on these traditional theories, one can rationalise Bangladesh exporting textile products to the United States and the United States exporting microchips and semiconductors to Bangladesh.

There are naturally other elements which could influence trade, from natural resources to economy of scale theories (produce a good in large scale to save on production cost), or the use of technologies providing a trade advantage. In particular, Paul Krugman’s ‘new trade theory’ suggests that significant economies of scale and network effects can determine the patterns of trade. For example, the United States and the European Union, which are both capital-intensive and have similar comparative advantages in several areas of goods or services, trade in the same category of products. Mass production leads to decline in the marginal cost of production and, as a result, in price-competitive goods. The new trade theory affirms that firms compete not only on price but also on considerations such as quality, brandings and perception. The reality and complexity of today’s free trade, however, show a mix of all classical theories.

i.2.1.4 The Case for and against Free Trade
According to the World Bank, ‘Trade is an engine of growth that creates jobs, reduces poverty and increases economic opportunity. Over one billion people have moved out of

poverty because of economic growth underpinned by open trade since 1990. The case for free trade seems pretty clear for the supporters of globalisation. Yet trade liberalisation is also highly contested today, at a time when protectionism is on the rise. The NAFTA Agreement was scrapped and replaced by a much more diluted version under the moniker USMCA. The Brexit discussions have recently come to a close and opened a new era of cooperation for the UK and Europe. And the quest for alternative and more sustainable, if not yet socially just models, is ongoing.

Arguments for free trade have been made on the basis of the theoretical approaches explained briefly above, as well as pragmatic decisions, often mixing trade liberalisation with offensive and defensive policies. Indeed, there is not a single country totally open to free trade. States use a variety of policy mechanisms to trigger and limit trade at the same time. International economic law is one of these instruments. For its proponents, free trade is seen through a cost–benefit analysis as encouraging productivity and innovation, economies of scale, general economic growth and prosperity. To quote the economist Jagdish Bhagwati, in his book *In Defense of Globalization*, ‘free trade means higher growth’, and ‘higher growth is associated with reduced poverty’. Bhagwati further argues:

> only an ignoramus would coach the poor countries to talk of ‘unfair trade’, for this is the code phrase used by the protectionists in rich countries to cut off imports from the poor countries by alleging that they obtain their competitiveness in ways that amount to unfair competition and unfair trade. Trade experts of all political persuasions have spent decades exposing the cynical use of this phrase and decrying its usage but then in come the know-nothings, who persuade the unsuspecting poor countries to embrace it. When it comes to the two sets of nations, poor and rich, battling it out as to who is the worse unfair trader, do not be surprised when the poor nations find themselves at a disadvantage.

Unfair trade might well refer to the practices of dumping or subsidisation critically addressed by international trade law (see Chapters 5 and 6), but there is more to the question of global fairness and social justice than there might seem. Equity, as noted by Joseph Stiglitz, cannot be left to politics alone, while economists and trade lawyers deal only with efficiency and security. As we will see in Chapter 16, as well as in the following paragraphs, the reality of free trade is much more complex than liberal economists would like it to be. Trade and globalisation have not necessarily benefited all, at least not in the same way. This is where international economic law could have a greater balancing role.

Free traders have not always convinced States and businesses of the validity of their arguments. Alternative schools of thought emerged in response to the classical economists’ theories as early as the nineteenth century. Alexander Hamilton (1755–1804) in the United States, John Stuart Mill (1806–1873) in the UK and Friedrich List (1789–1846) in Germany had argued in favour of various forms of protection of the domestic economy to allow infant industries to

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grow. This ‘infant industry’ theory against free trade, or limiting its development, played a key role throughout the twentieth century, in developing countries in particular, with the concept of import substitution industrialisation (ISI). Indeed, from the Second World War, a number of developing countries reclaimed their independence, using import substitution industrialisation as an engine of economic sovereignty (see Part II and Chapter 16). In this context, the infant industry argument was to support the idea that developing countries have a potential comparative advantage in manufacturing, provided that such industries are initially helped to grow to a significant level to meet international competition. Tariffs and import quotas then need to be used to the benefit of domestic industrialisation. After all, the US or Japan initially protected their economies to grow their national industries. The same is true for China, which gradually liberalised trade from the early 1980s, once Deng Xiaoping had formulated his opening-up theory in 1978. India probably gave the most extreme example of the application of the import-substitution theory in the early 1970s, when its importation of products other than oil was only about 3 per cent.27 In the context of Latin America, structuralism referred to a form of ISI theory embraced by a number of countries from the 1950s to the 1980s, under the influence of the Argentine economist Raúl Prebisch (1901–86) and with the creation of the United Nations Economic Commission for Latin America and the Caribbean (UNECLAC) (see Chapter 16). This was also related to the dependency theory popularised by Hans Singer and Raúl Prebisch, according to which resources, and natural resources in particular, were exploited in the South to the sole benefit of the North (the coloniser or former coloniser) to maintain the developing world at a stage of underdevelopment. Naturally, the dependency theory shared a number of arguments with earlier Marxist concepts on imperialism. This trade between unequals, described by Karl Marx, fitted the colonial model and its denunciation well.28 Marxists theories of international law, as we will see below, are regaining a form of popularity at a time of disillusionment with capitalism and discontentment with globalisation.

Import substitution industrialisation, however, was gradually abandoned by most developing countries after the fall of the Soviet Union and under the pressure of World Bank and IMF liberalisation policies (see Chapter 16). The ISI was not short of uncertainties. What industry to invest in? How to reach a stage of competitiveness? What role for the private sector? What policy tools to use – tariffs, quotas, exchange control, domestic content rules? Is the domestic market big enough? These interrogations posed the question of the correct trade policy instruments to apply, an issue still very much debated today when countries need to define their tariffs policy, for example (see Chapter 2). The practice of ISI often revealed the inability of developing countries to effectively implement the theory and, from the early 1990s, revealed a general opening up to the world and free trade.29 This has

27 A. Panagariya, India: The Emerging Giant (Oxford University Press, 2008).
resulted in an increased share in trade for developing countries, as well as a change in the nature of their commerce, not only in natural resources and agricultural products, but also in manufactured goods. However, the overall picture offered by this apparently simple description can be misleading given that this period also corresponded with the rise of China as a trade superpower. Most of the developing world trade is actually with and by China, which is still considered a developing country and enjoys such status in the WTO (see Chapter 16).

The issue of the inequalities produced by trade liberalisation is at the core of the contestation of globalisation, a phenomenon seen as the product of world capitalism and free trade. The immense echo of the research work of the Paris School of Economics on global inequalities and the resounding success of the book of the French economist Thomas Piketty, *Capital in the Twenty-First Century*, are revealing of contemporary questionings. Since the early 1990s, the anti-globalisation movement has gained world prominence. It has taken multiple shapes and national expressions, resulting in diverse political and economic evolutions, from populism and the rise of extremism, to the contestation of multilateralism and international organisations, (mega)regionalism, renewed bilateralism, trade wars and simply new forms of protectionism. The arguments against globalisation are many and varied, but could be summarised in the words of Joseph Stiglitz, a Nobel laureate in Economics. Stiglitz noted:

1. The benefits of globalisation might well be smaller than advertised and possibly offset by the costs.
2. The disillusionment is proportional to the initial craze for globalisation.
3. Incomes and wealth have not been equally shared, and hence the rise in inequalities.
4. The governance of globalisation is unfair, with the US, for example, having the real power in the IMF to the detriment of other nations, including the now powerful emerging countries.
5. Multinational corporations and international financial institutions are the real decision-makers.
6. The ideology applied to globalisation does not support the interests of all, including sometimes the most powerful.
7. The distribution of powers is affected negatively by globalisation.
8. Globalisation reduces the ability of governments to deal with real issues, in particular international taxation, while a number of super multinational corporations avoid tax.\(^{31}\)

Stiglitz synthesised brilliantly: ‘Globalization is the field on which some of our major societal conflicts – including those over basic values – play out. Among the most important of those conflicts is that over the role of government and markets.’\(^{32}\) For Dani Rodrik, the paradox of globalisation poses an absolute challenge: ‘we cannot simultaneously pursue

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