

**New Zealand Trade Policy in Turbulent Times**  
**Address to the New Zealand India Trade Alliance**

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## Introduction<sup>1</sup>

The period 1995-2018 has been the ‘Golden Weather’ for New Zealand trade policy. To state the obvious, the establishment of the WTO; the legal enforceability of trade disciplines from 1995<sup>2</sup>; and a reduction of global protectionism over this period – facilitated in part by a burgeoning network of FTAs - has delivered significant benefits for our economy.

2 Unfortunately, 2019 is likely to mark the end of this Golden Weather, not least because the two basic assumptions that have underpinned our trade policy since 1995 may no longer apply. Global protectionism is no longer declining. The past two years have seen the sharpest increase in trade restrictive measures (of varying impact) since the establishment of the WTO. Our assumption that enforceable WTO rules would widen and deepen is also in trouble. Enforceability hinges on a functioning WTO Appellate Body (AB). Assuming the US does not change its position – to block the appointment of new AB members - by mid-December this body will no longer have a quorum, thereby threatening the viability of the wider system.<sup>3</sup>

3 The following is clustered into four inter-related parts:

- 1) the current domestic and international context for New Zealand trade policy;
- 2) a brief description of two specific reference points that inform our approach;
- 3) an outline of the way ahead on New Zealand’s trade policy; and
- 4) some reflections on our rapidly evolving relationship with India.

4 Before turning to the international context for New Zealand trade policy, it is worth recalling why trade matters for New Zealand. The export sector sustains more than half a million New Zealand jobs. Put another way, one in every four New Zealanders in work today depends on exports for their livelihoods. Trade is also an important driver of productivity, employment and incomes. We know, for instance that productivity per New Zealand worker is 36% greater if they are in a firm that is exporting, compared to one that isn’t.<sup>4</sup> It has also been established that employment grows 7% to 12% faster when New Zealand firms start exporting<sup>5</sup>. International research also tells us that exporting firms pay higher wages – up to 6% more than

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<sup>2</sup> Including agriculture for the first time.

<sup>3</sup> The situation is in fact even worse. If a case goes to appeal before the end of December and involves a WTO member of the same nationality as one of the remaining Appellate Body judges, that judge will have to recuse him or herself from the case. The chance of this are relatively high given that the three remaining judges are from India, China and the US – all from WTO members extensively involved in ongoing disputes.

<sup>4</sup> New Zealand Ministry of Foreign Affairs and Trade (2017) *Estimating New Zealand’s tradable and non-tradable sectors using Input-Output Tables*, Paper presented at the New Zealand Association of Economists’ Conference, 12-14 July 2017.

<sup>5</sup> R. Fabling and L. Sanderson (2010), *Exporting and performance: Market entry, expansion and destination characteristics*, Reserve Bank of New Zealand Discussion Paper 2010/17

non-exporters<sup>6</sup>. In short, trade - the rules and market access openings that facilitate this matter for our prosperity, well-being and livelihoods.

### The Global outlook is worrying

5 Internationally, the 'Golden Weather' for New Zealand trade policy has given way to a rather more uncertain outlook. Protectionism is rising. Since 2018 there has been a 30% increase in trade-restrictive measures – the sharpest such increase since the end of the Uruguay Round and the establishment of the World Trade Organisation, in 1995. It's worth also recalling that New Zealand is at a disadvantage in international trade. This is a consequence of our (small economic) scale and distance from markets, both of which are compounded by our continued, albeit diversifying, reliance on agricultural exports. These products face the highest levels of global protection - tariffs often in excess of 100% and an average of 23% - compared with an average of less than 6% for manufactured goods. And tariffs are only part of the problem. A recent New Zealand Institute for Economic Research (NZIER) analysis suggests that in the Asia-Pacific alone non-tariff barriers (non-science-based sanitary and phyto-sanitary barriers; unnecessarily burdensome labelling requirements) cost our exporters nearly \$6 billion a year.

6 In fact, setting to one side the conclusion of the WTO Trade Facilitation Agreement in 2013 and the elimination of agricultural export subsidies at the Nairobi WTO Ministerial in 2015 – the latter a key priority for New Zealand at least since the late 1980s - there has been no meaningful multilaterally-driven trade liberalization for nearly twenty five years. Nevertheless, while there has been a very limited expansion of the existing disciplines, what we do have is a functioning international rules-based system. This is something that New Zealand continues to actively support and invest in, not least through the World Trade Organisation. This body houses the world's only legally enforceable set of rules that bind all of the world's economies large and small. The WTO is therefore vitally important to New Zealand and remains our first best option for international trade rules, providing a set of mechanisms, particularly its dispute settlement function through which major economic powers like the EU, China, the US, India, Indonesia and others, can be held to account.

7 There is no doubt that the WTO and its rules are in need of modernisation to reflect the dramatic changes in the way trade now occurs. The risk, however, is that members will (again) fail to agree a reform pathway this year, leading to the gradual erosion of existing rules and the WTO itself. That will signal the beginning of the end of the current world trading order – with the foundation blocks for a new one only coming into view more slowly.

8 Discrimination will also accelerate this year alongside the potential emergence of closing regional trade blocs. The US return to bilateralism - a long-standing EU preference as well - will exacerbate this trend as Washington advances separate but very different and likely lengthy negotiations with Tokyo and Brussels. India's own

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<sup>6</sup> A B. Bernard, J. B Jensen, S J. Redding and P. K. Schott, 2012. "The Empirics of Firm Heterogeneity and International Trade," Annual Review of Economics, 4:283-313

growing activism is also noted, albeit of narrower and shallower agreements. Networks of regional and bilateral trade agreements will also proliferate.

9 The issue for international trade policy has always been whether such preferential agreements will be ‘building blocks’ or ‘stumbling blocks’ to progress at the WTO. Given the US positioning in Geneva combined with EU and Japanese signals about less than comprehensive FTAs it is hard to be optimistic. Other major players like India and China will have their own geo-strategic and economic imperatives.

10 In some ways of course, ‘twas ever thus. The larger WTO members’ commitment to a system that effectively constrained their room for manoeuvre could never be taken for granted. But this year really is an existential moment for the WTO. The threat to the enforceability of the international trading system, or at a minimum its legal enforceability in terms of the US, has a ‘drop-dead’ decision-point: mid-December 2019.

11 More generally, a slowing global economy will not dampen the rising geopolitical tensions. Indeed, the way that major economic players like China or indeed India respond to that slowdown (ie the economic instruments they may resort to) may worsen the ongoing escalations of tensions. And in the meantime, this is a year of distractions. The US-China tariff-focused negotiations are clearly one, where even a resolution may not spell good news for the rules-based system, let alone for New Zealand interests in either economy. The EU, a major global trader is grappling with Brexit; elections to the European parliament in May; and the transition to a new Commission in September. Public scepticism about trade agreements and their impact on sovereignty, employment and incomes, particularly in OECD countries – not least New Zealand (TPP is a case in point) continues unabated. This may encourage further inward looking and protectionist policies which will, in turn, further undermine the process of internationalisation that underpins much of the rules-based trading system.

12 More broadly, the challenges in the Middle East, the South China Sea, Ukraine/Russia, the Korean peninsula, the borders between India and Pakistan and so on will not fade. And in this context, the pressure on small and medium-sized WTO members like us to ‘pick a lane’ – as the US Permanent Representative to the WTO recently exhorted – can be expected to intensify. The pressures from those tectonic shifts between the major economies may yet become the defining issue for us in 2019 both geo-strategically and in terms of how we prosecute our international trade policy.

13 In sum, the hopes of many for a global trading system that delivers a Kantian ‘perpetual peace’ are fading fast. The Golden Weather is ending but it is rather less clear how inclement the new weather will be. The return to a Hobbesian ‘might makes right’ world order is already the revealed preference of several major players. The temptation for others is obvious. In fact, recent moves by several of the majors to work together in an exclusive format on certain trade issues, combined with Brussels’ (and the UK’s) apparent instincts on New Zealand’s valuable TRQs negotiated in good faith during the Uruguay Round suggest a clear direction of travel. The Melian Dialogue-type<sup>7</sup> implications are troubling.

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<sup>7</sup> The Melian Dialogue refers to an exchange reported by Thucydides in his *History of the Peloponnesian Wars* between the major power of the era (Athens) and the small city state of Melos during which the Athenians chillingly declared ‘the strong do what they can and the weak suffer what they must.’ Following the ‘dialogue’ the state of Melos was extinguished.

## Avoiding the 'traps'

14 Recently, during a presentation to the New Zealand Foreign Affairs, Defence and Trade Committee (FADTC)<sup>8</sup> two reference points were identified that can help illuminate New Zealand's trade policy agenda alongside that of other countries that similarly rely on a predictable rules-based trading system for their prosperity.

15 The first is the risk posed by what is known as the "Thucydides Trap". This phrase refers to the situation when a rising power causes fear in an established power which escalates towards war (whether kinetic or otherwise, such as a trade war). The concept was developed by Harvard Professor Graham Allison drawing on Athenian General Thucydides' seminal History of the Peloponnesian War which analysed the epic struggle between the two most powerful Greek city states at the time – Athens, a rising power and Sparta, the established one.<sup>9</sup> The parallels with our current time are plain to see, and have even been remarked upon by Chinese President Xi Jinping who said: "We all need to work together to avoid the Thucydides trap – destructive tensions between an emerging power and established ones".<sup>10</sup>

16 What can small states like New Zealand do when faced by these risks and what lessons can we draw from the Peloponnesian War? What is clear is that we can't sit complacently aside. If we look at small states' interests through a "Thucydian prism" we can learn from those smaller Greek city states that had to navigate those turbulent times. Some were successful, while others such as the Island state of Melos were destroyed. The policies pursued by the survivors and those which preserved the peace for long periods have common characteristics. These include how they aligned themselves to help create and sustain regional structures and instruments as a way of maximising their influence, and defending their interests. APEC, the CPTPP and indeed RCEP can be seen in this light, as one of the ways in which New Zealand is investing in such processes as a way of protecting itself from suffering collateral damage in turbulent and changing times.

17 The second reference point is the "Kindleberger Trap". This is the situation described by Charles Kindleberger one of the architects of the Marshall Plan, who argued that the disastrous decade of the 1930s was enabled by the failure of the US to take on the role of provider of key global public goods after it had replaced Britain as the leading global power.<sup>11</sup> Global public goods include things like freedom of the high seas, financial stability and global trade rules. It has been suggested that this is the new "trap" being confronted internationally i.e. whether the major powers will support and invest in global public goods or create new ones to sustain the rules-based system. Against this risk coalitions of smaller countries may need to step in to

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<sup>8</sup> Available at: [https://www.parliament.nz/en/pb/sc/submissions-and-advice/document/52SCFD\\_ADV\\_78569\\_1971/ministry-of-foreign-affairs-defence-and-trade-initial](https://www.parliament.nz/en/pb/sc/submissions-and-advice/document/52SCFD_ADV_78569_1971/ministry-of-foreign-affairs-defence-and-trade-initial) (accessed on 28 March 2019)

<sup>9</sup> Allison, Graham. (2017) *Destined for War: America, China and the Thucydides's Trap*, Houghton Mifflin Harcourt.

<sup>10</sup> NPQ Volume 31 #2 Spring 2014 "Can China avoid the Thucydides' Trap".

<sup>11</sup> Nye, Joseph S. (2017) The Kindleberger Trap, *Project Syndicate*, 9 January.

sustain these global public goods that we all depend on. Again, both the CPTPP and RCEP are good examples of a coalition of like-minded countries coming together on the basis of “open plurilateralism”, in a bid to support and sustain trade rules. Other such bodies include the OECD, the Commonwealth and APEC, among others.

#### What does this mean for New Zealand?

18 Our priorities need to be numerous and across a range of fronts. Effectively implementing CPTPP is key to ensure the maximum benefit to our exporters and through them as a feedback loop into the New Zealand economy. We also need to work to conclude the Pacific Alliance negotiations; push for the conclusion of or at least a significant breakthrough in the mega-plurilateral Regional Comprehensive Economic Partnership (RCEP - which crucially includes India). Alongside this we need to continue and intensify our negotiations with the European Union and be prepared to take full advantage of emerging opportunities such as with the UK and Mercosur, as well as through non-traditional trade policy forums like the Commonwealth – a new and important focus for our work.

19 We should also work with others to swiftly expand the membership of existing agreements. In particular, CPTPP represents an opportunity to extend its high quality rules by encouraging the membership of economies as diverse, but important as Korea and the UK. In this way, the agreement offers a way of supporting regional and international public goods in support of the rules based system. Alongside this, we will need to work to ‘upgrade’ - with an eye to relevant sensitivities on both sides - existing agreements with Singapore, China and ASEAN.

20 It is against this background, that an elaborated framework for pursuing New Zealand's trade policy can be identified comprising the following six elements:

- ***Defence of the 'rules-based system'***. This remains *the* priority. It will require a re-doubling of our current efforts to protect and sustain the existing system;
- ***Embed New Zealand in the emerging regional economic architecture***. Implementing CPTPP; working to conclude the Pacific Alliance and conclude or get a significant breakthrough in the RCEP negotiations. Intensifying the negotiations for an FTA with the EU is also now a matter of urgency. We also need to pursue other opportunities as they emerge, including for instance, a possible negotiation with the UK;
- ***Supporting regional and global public goods*** which can sustain and support the rules-based system by building coalitions of like-minded countries such as through the Cairns' Group, the coalition supporting our work on fossil fuel and fisheries subsidy reform, those working with us on the Trade for All Agenda as well as engaging more actively in existing institutions like APEC, OECD and non-traditional trade policy forums like the Commonwealth; and
- ***Open-plurilateralism*** – advancing this concept as an active

deliberate and structured process of engagement, including with CPTPP partners in particular, to accelerate the consideration of new members as soon as possible.

- ***Economic diplomacy*** – to actively work with other New Zealand agencies on-shore and off-shore to help our exporters through the provision of bespoke advice and a range of practical web-based tools that help access new and existing markets (Non-Tariff Barrier portal; Tariff finder service; Exporter hotline and so on)
- ***Develop the Trade for All agenda.*** As you will have seen from recent announcements, the Government is embarking on a process to ask New Zealanders what they want from trade policy in general and trade agreements more generally. The aim is to seek New Zealanders views on how our trade policy can contribute to delivering sustainable and inclusive economic development for the benefit of all.

### New Zealand-India Relations: Broadening our shared Horizons

21 India is recognised as one of the ‘rising powers’ in Asia through sheer scale at 1.3 billion people, its growing economic clout and its increasingly outward-looking foreign policy. Unfortunately, there are few indications that India intends to open its borders to trade. An export-led growth model is not currently favoured by India. More broadly, India’s approach to WTO negotiations has been challenging depending on the issues under discussion and it has been rather more defensive than one might expect of such a global player, including across both our bilateral negotiations – now nearly a decade old – and those well underway in RCEP.

22 In many ways, this defensiveness is hard to understand. To say that India’s potential is vast is an understatement. Across a range of indicators the latent capabilities and capacities are clear. At the same time, however, there are serious challenges related to poverty, development, demography, the environment and of course growth.

23 Nevertheless, as one of the re-emerging major players in international trade and indeed in the global order itself, there is a role for Indian leadership. In this regard, Prime Minister Modi’s stated commitment and thoughtful elaboration of why a rules-based order matters is both welcome and significant, not least for the way it captures the opportunities, challenges and complexities confronting us all globally.<sup>12</sup> India’s actions to support and reinforce that commitment will be valued and indeed can play a crucial catalytical role in the way forward.

24 The various strategic frameworks in place to think through India’s role in the world make for interesting reading. Part of that strategic thinking appears to be

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<sup>12</sup> See in particular Prime Minister Modi’s statement at the Shangri-La Dialogue last year available here: :

[https://www.mea.gov.in/Speeches-](https://www.mea.gov.in/Speeches-Statements.htm?dtl/29943/Prime+Ministers+Keynote+Address+at+Shangri+La+Dialogue+June+01+2018)

[Statements.htm?dtl/29943/Prime+Ministers+Keynote+Address+at+Shangri+La+Dialogue+June+01+2018](https://www.mea.gov.in/Speeches-Statements.htm?dtl/29943/Prime+Ministers+Keynote+Address+at+Shangri+La+Dialogue+June+01+2018) (accessed on 29 March 2019)

driven by a focus on trade deficits with a recent Indian Parliamentary Report, for instance, drawing attention to the existence of such a deficit between India and ASEAN members.<sup>13</sup> Setting aside whether these supposed trade deficits are even being measured accurately by anyone (ie are we sufficiently accounting for services trade and investment flows) – it is difficult to understand why there is such a focus. After all, given the powerful role India could be playing both as a rules-setter, but also as a supporter of rules that can drive its own domestic growth, there is a real opportunity here in the Asia-Pacific generally and in RCEP in particular.

25 For its part, New Zealand would welcome India playing a greater role in the region, conscious of course that with leadership comes responsibility, including for the rules-based system that fosters and sustains both India's economic development, but also that of other international actors, not least the more than 100 small states, of which of course New Zealand is one. We would also welcome constructive engagement by India in Geneva on WTO reform and modernisation, where we of course also strongly support India's ambition for meaningful and lasting agricultural reform, not least but not only, by developed countries

26 In bilateral terms, India is already a significant trading partner for New Zealand and is New Zealand's 11<sup>th</sup> largest two-way trading partner. Two-way trade in goods and services was NZ\$2.98 billion in the year to December 2018. India is also New Zealand's sixth largest services market, with New Zealand's services exports to India valued at NZ\$1.31 billion in 2018, fuelled by strong tourism and education sectors. There is, however, still considerable unfulfilled potential, particularly in bilateral goods trade – much of which is unfortunately 'chilled' by high tariffs (up to 150 percent in some cases)<sup>14</sup> and other barriers. Not surprisingly perhaps, New Zealand's goods exports to India grew modestly after the Global Financial Crisis and have declined since 2011 to a plateau of about NZ\$600-700 million per annum. Interestingly, services export flows are growing much faster than in goods, with their value in 2018 at \$1.3 billion, compared to \$712 million in goods exports.

27 Like India, New Zealand is focused on the diversification of our trade relationships without confusing dependence with interdependence. Our trading relationship, for instance, needs to be understood as one where we manage our bilateral economic interdependence within the architecture of the WTO and our bilateral FTA and plurilateral FTA negotiations. We regard these instruments not simply as commercial opportunities (though clearly they are that as well), but as a way to mutually reinforce the plurality of interests we have in ensuring India's integration into the Asia-Pacific and its continued support for and engagement on global trade rules and disciplines. Regional economic integration is proceeding

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<sup>13</sup> See in particular: <https://worldview.stratfor.com/article/asian-free-trade-proposal-broad-scope-narrow-focus> (accessed on 28 March 2019)

<sup>14</sup> It is worth also acknowledging the role that coal has played in the bilateral trade and the effect of global prices and domestic developments in New Zealand which may have lowered the overall trade flow at particular moments in time.

apace, and it would be very unfortunate for New Zealand, not least for India's leadership in the region if India's defensiveness meant it was unable to find a way into these processes in the near future.

28 In the meantime, the New Zealand business community is engaged on India, and interested in advice and information on business and exporting opportunities. This will always be welcome, and the role of the New Zealand India Trade Alliance is appreciated in this regard.

### Conclusion

29 The year ahead is shaping up to be an intensive and busy one, driven in no small measure by the now existential threats that confront the existing trade policy order, but also the usual challenges New Zealand faces as a trade-dependent small (and distant) economy. In purely process terms and unlike many others (eg the EU and ASEAN member states or members of the Pacific Alliance or Mercosur), we do not have regular and close points of trade policy engagement with key counterparts internationally beyond the usual forums like the WTO, APEC and the OECD. Combined with our expectation that we should be 'in the room' to shape outcomes on issues that touch on our national interests, this all means New Zealand has to work particularly hard and be particularly present simply to keep up with developments. Even greater effort than usual will therefore be needed to ensure that we are contributing not just on process but also in substance, ie to be creative, constructive, interesting and interested as well.

30 It is against this backdrop of a changing world trade order that our relationship with India is positioned. The risk of a fragmentation of international rules simply underlines the need for major players like India to exercise leadership and with that leadership comes a responsibility to sustain and support a transparent, certain and fair international rules-based system. RCEP is one important avenue for such engagement, but the bilateral track is another which can complement and support the RCEP outcome.

31 And finally, as we navigate the end of the Golden Weather for trade policy and prepare for more turbulent times, it is worth bearing in mind the distinction Aristotle made between three types of knowledge "*episteme*" (theoretical knowledge); "*techne*" (technical knowledge) and "*phronesis*" (practical wisdom). For Aristotle, these three forms of knowledge were at the heart of *eudaimonia* – the state of ethical and political wellbeing where, above all, one does what is worth doing and what is right. We have traditionally been able to deploy all three of these forms of knowledge in support of our trade policy, but in 2019, perhaps more than in most years, it will be our application of *phronesis* in particular that will best help us manage the inclement weather ahead.