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On a Restart of Economic Multilateralism

By Jörn Kleinert

Abstract

With the election of Donald Trump as the 47th President of the United States, voters have chosen "America First," thereby burying multilateralism as we knew it. Following the end of globalization around 2010, the world has slowly divided into several blocs. These blocs emphasize their differences and competition with one another more than the opportunities to reap benefits from trade and other forms of cooperation. However, a global economy that encompasses some four billion people in an economic system based on the division of labor requires a multilateral order. The "Keynesian" institutions established after World War II functioned well for a time but then proved unsuited to a world undergoing drastic change following the end of colonialism and the Cold War.

The multilateral trading system established after World War II was based on the benefits of trade. The multilateral system was extremely successful. It helped millions of people escape from extreme poverty. While it led to higher average incomes, income distribution increasingly became a problem—both between countries and within them. During the era of globalization, the distributions of income and wealth shifted significantly to the detriment of the poorest members of society.

It is difficult to reduce inequalities within society. Although many attempts have been made, few have been successful. In the U.S., presidential candidate Trump promised tariffs as a corrective measure. Protectionism has become a tool of power politics for the country with the largest market and the world's reserve currency. In bilateral negotiations, all other countries are to be forced to grant better trade terms to the U.S. Other major players will do the same if

this is the new model of international cooperation. An era of power politics is looming—or has already begun. This comes at the expense of smaller countries.

The United Nations-based order was remarkably flexible. In recent decades, however, it has become more difficult to achieve a convergence of interests. The system was undermined by its own success, by the very dynamics it fostered: dynamics characterized by varying rates of growth across different regions of the world. The old order cannot be restored. Attempts to halt structural change will prove counterproductive both domestically and in international relations.

As an alternative, President Trump proposes a system of international relations based on "deals." This is certainly better than trade wars and much better than military conflicts. There is untapped potential here, but we lack a framework that would enable us to reap the benefits of a transformed multilateralism. A new multilateralism is necessary, but it is not yet in sight—not even as a draft.

Only the Canadian Prime Minister seems to have a vision of what a new multilateral order might look like. His efforts to invite the "middle powers" to engage in open cooperation—in order to counterbalance the major powers—are currently the only counterforce to the division of the world into their respective spheres of influence. For him, the European Union serves as both an anchor and a model. The EU is a confederation of sovereign states with negotiated and balanced institutions. It is open to other partners for cooperation in specific areas and has a value system that aligns with that of the Canadian government. The EU operates on the basis of rules which foster international cooperation.

The success of the postwar order lay in its being anchored by international rules that were institutionalized through international treaties and organizations—in the economic sphere, for example, the GATT, the IMF, and the World Bank. The multilateral organizations and the GATT, which replaced the International Trade Organization, were the result of years of scholarly preparation and coordination between the United States and the United Kingdom. They sought to create a sustainable postwar order and avoid a disaster like the one that followed World War I. This struggle to establish effective institutions is linked above all to the work of John Maynard

Keynes and Harry Dexter White. The result of their efforts was an open trading system supported by a system of fixed exchange rates. Their work laid the scientific foundation for the field of macroeconomics in open economies.

This system suffered its first major blow when U.S. President Nixon abandoned the U.S. dollar's peg to gold in 1971. What followed was a decade of macroeconomic turbulence without fixed exchange rates. The failures to achieve stability were attributed to misguided government interventions, not to the changed economic conditions. "The market" was supposed to provide the solution. Deregulation and privatization significantly expanded the scope in which market-based solutions were applied. The difference from the previous order is striking: the institutional order was increasingly replaced by a "spontaneous order" of the markets. The old institutions merely accompanied the market-based solutions.

During the era of globalization in the 1990s and early 2000s, the call for government intervention waned. National institutions were seen as ineffective or even a hindrance to international competition. Tony Blair's remark from 2005 remains memorable: "I hear people say we have to stop and debate globalization. You might as well debate whether autumn should follow summer." It is hard to imagine a greater departure from the original idea of combining national stabilization policies with an open international order. Markets determined the fortunes of regions and entire countries. Policymakers no longer claimed the right to intervene in a regulatory capacity. They could rightly point out that globalization had a dynamic effect, generated new sources of growth, and integrated many new countries into the international division of labor, thereby showing some of them a path out of extreme poverty. From the perspective of people, especially in OECD countries, however, these were very abstract achievements.

For many of them, only the problems remained. The promise of upward mobility made by the previous generation became increasingly difficult to fulfill. Industries were overwhelmed by global competition, causing the affected regions to fall into decline. The unequal distribution of income and wealth grew considerably. Public infrastructure was neglected due to cost pressures. Individual adaptation was presented as the only possible response to these disruptions to social life. For many people, this seemed unappealing, yet no alternatives were offered. It

was not until after the financial crisis of 2007–2010 that alternatives were articulated: "Take control back" became the Brexiteers' successful slogan.

The financial crisis of 2007–2010, however, was merely a particularly severe example of a series of financial crises that have repeatedly plagued parts of the global economy since the end of the Bretton Woods system. Keynes' efforts to establish a postwar economic order were motivated by his desire to prevent a financial crisis in the highly indebted and economically weak European countries. The international institutional framework helped achieve this: Until 1971, financial crises were very rare. That changed significantly after the collapse of the Bretton Woods system and the liberalization and deregulation activities in the financial sector in the 1980s. It began with the debt crisis in Latin America in the early 1980s, followed by the devaluation of the dollar after 1985, the S&L crisis around 1990, the Scandinavian banking crisis in 1992, the EMS crisis in 1992 and 1995, the Tequila crisis in Mexico in 1994, the Asian financial crisis in 1997, the Russian crisis of 1998, the Brazilian crisis of 1999, the Argentine crisis of 2000, the Turkish crisis of 2001, the financial crisis of 2007–2010, the Greek crisis of 2010, and the euro crisis. Leaven and Valencia (2008) identified 124 banking crises, 208 currency crises, and 63 sovereign debt crises between 1970 and 2008. At least to date, no stable spontaneous order has emerged.

Rodrik (2011) argues that, out of the set "democracy, sovereignty, and globalization," only two elements can ever be fulfilled at the same time. It is not possible to achieve all three simultaneously. I would agree with him if he were willing to curb globalization and give priority to democracy and sovereignty. Curbing globalization refers primarily to unhindered global financial flows. This would lead to a Bretton Woods-style framework, with or without a system of fixed exchange rates, but with restrictions and controls on international capital movements. In 2009, in the wake of the global financial crisis, things seemed to be moving in this direction. But as early as the second half of the same year, the idea was shelved. Politicians lacked the courage to act. Tony Blair's conviction was still shared by too many.

We need more rules in international economic relations once again. Even though it is currently impossible to predict whether the efforts to achieve this will be successful, it is important to preserve the existing rule-based structures and build upon them as the core of a new order. It

may be that the only way to transform a system that was no longer functioning was to partially dismantle it. Whether or not something constructive emerges from the current situation also depends on the proposals we put forward for establishing a new order.

Literature:

Leaven, L. und F. Valencia (2008). Systemic Bank Crisis: A New Database. International Monetary Fund, Working Paper WP 08/224.

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These thoughts are drawn from the author's new book in the book series "New School of Multilateralism," titled "On a Restart of Economic Multilateralism," Nomos, to be published in November 2026.



Jörn Kleinert *is a professor of international economics with over 20 years' experience in the field. His theoretical work focuses on general equilibrium models with heterogeneous agents, while his empirical work involves large micro data sets. Recently, his research focus has turned to the emergence and development of institutions in general, and markets in particular. Having studied and worked in Kiel and Tübingen, Germany, he joined the University of Graz in 2010.*

The photo shows the author and the editor and founder of the New School of Multilateralism at the book presentation at University of Graz.

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