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US Strategies of Institutional Adaptation in the Face of Hegemonic Decline

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Abstract

How do shifts in the global distribution of power affect the US' preferences for institutionalized cooperation? This article explains why and when the power shift creates incentives for the US to move cooperation out of universal multilateral institutions, such as the WTO, and into exclusive multilateral institutions where it seeks to create a leading consensus among a select group of 'like-minded' states. An agreement reached within the sub-group imposes costs on those excluded from the deal. This increases the hegemon's power bargaining leverage *vis-à-vis* outsiders who can join the new agreement as price-takers. In this scenario, the hegemon's institutional response to the challenge of rising powers is a strategy of divide and conquer; that is, *strategic cooptation* based on inducements followed by *power bargaining* based on coercion. The double move, however, puts the hegemon in the position of challenging the institutional status quo with potentially negative consequences for the original institutional order. A case study of negotiations over a new trade in services agreement (TiSA) shows this strategy of divide and conquer at work as the US tries to first achieve a deal without emerging economies, notably China, that can later be imposed on them.

Policy Implications

- US global partners should recognize that the US' commitment to inclusive multilateral institutions is likely to decline because of broader shifts in the distribution of power which increase the domestic and international costs of its commitments, and not merely for reasons idiosyncratic to a given administration.
- The US will be increasingly prone to pursue global policy cooperation with like-minded states within exclusive multilateral settings, making future global institutions likely to be more issue- and actor-specific.
- US policymakers should return to negotiating a rules-based framework for trade in services rather than pursue one-off bilateral deals with China.
- The WTO should attempt to integrate minilateral trade negotiations into its framework early on in order to avoid undermining its policy-making and legitimacy-granting authority.

The United States government explicitly recognizes the ongoing global power shift as one of its main foreign policy challenges. Despite polarized views on most issues, both parties and all recent administrations have worried that the growing influence of countries such as China, India, and Russia within and outside of international institutions has the potential to re-shape the global order to the detriment of US interests (see, e.g. White House, 2015, 2017). Liberal institutionalists have argued that a hegemonic actor, such as the US, should respond by defending and expanding the multilateral order by integrating rising powers into international organizations and multilateral commitments on a more equal basis. The theoretical expectation has been that rising powers dissatisfied with the institutional status quo could disrupt the order and that the US can best lock-in its leadership by accommodating them with 'new, expanded, and shared international governance arrangements' (Ikenberry, 2005, p. 136; see also Brooks and Wohlforth, 2009; Brooks et al., 2013; Ikenberry, 2018a, 2018b). There is, however, little empirical evidence that the US is responding to

rising powers by deepening existing multilateral institutions. Instead we see the US challenging rather than expanding the multilateral institutional order that was created under its leadership. President Trump's overtly confrontational approach may be unprecedented, but the US' ambivalence towards the multilateral institutional order is not new and appears to come to the fore most forcefully when the US perceives a decline in its relative power (Skidmore, 2011). Over the last two decades, the US has stood in the way of reform at traditional international organizations (IOs), such as the United Nations Security Council and the IMF, and it is reluctant to join new ones, such as when it refused to join China's multilateral initiative to create the Asian Infrastructure Investment Bank (AIIB). Instead of a doubling down on multilateral institutionalism, the global power shift has been accompanied by an ongoing pattern of failed institutional reform combined with institutional fragmentation (Morse and Keohane, 2014).

This article asks, how does the power shift affect the US' preferences for institutionalized cooperation? It develops an

argument to explain how shifts in the global distribution of power affect the institutional preferences of the US, as a hegemonic actor, and thereby the prospects for cooperation within multilateral institutions. As Kruck and Zangl argue in the Introduction to this special issue, '[s]hifts in the global distribution of power put the global order and its underpinning international institutions under adjustment pressure'. While many power transition theories assume that established powers will be under pressure to accommodate the demands of rising powers in order to defend the status quo, those pressures might instead create incentives for powerful established actors to pursue alternative institutional settings that ultimately undermine the status quo. The changing distribution of power has given rising powers greater leverage within international institutions, but the ensuing cooperation problems have meant that outcomes have been unattainable. Negotiations over institutional or policy adjustments, for example over UNSC reform or trade policy reform within the WTO, have been extensive, have had few results, and are generally stuck in deadlock (Hale et al., 2013). Building on these observations, this article argues that circumventing the institutional leverage of rising powers is itself a strategy of institutional adaptation. The global power shift is one significant, albeit not the only, explanation for a move towards exclusive multilateralism.

My argument is that the power shift creates incentives for the US to move international cooperation out of inclusive multilateral institutions and to pursue its interests instead within a more selective, exclusive institutional setting where it seeks to create a leading consensus among a select group of 'like-minded' states. As rising powers with preferences that diverge from the interests of the hegemon become more important for achieving cooperative outcomes, collective action and distributional problems intensify. The hegemon's relative power decline, meanwhile, decreases its ability to deploy side-payments and inducements to overcome preference divergence and impose its own preferred outcomes on the group. The power shift increases the likelihood that the benefits of cooperation in an inclusive multilateral setting are outweighed by the costs of achieving alignment with the hegemon's own preferences, providing the hegemon with incentives to pursue exclusive multilateralism. When like-minded actors are available and the hegemon has sufficient 'convening power' to mobilize them, it will attempt to achieve agreement on its preferred policies among this sub-group of states. The hegemon uses exclusive multilateralism to change existing institutional conditions by creating an outside option for itself. An agreement reached within the sub-group imposes costs on those states affected by the issue but excluded from the deal. This increases the hegemon's power bargaining leverage *vis-à-vis* outsiders who can join the new agreement as price-takers, thereby circumventing the collective action and distributional problems of more inclusive multilateral negotiations. In this scenario, the hegemon's institutional response to the challenge of rising powers takes the form of a strategy of divide and conquer by using *strategic cooptation* based on inducements (Kruck and Zangl, this issue; see also Fioretos,

this issue) followed by *power bargaining* based on coercion (Kruck and Zangl, this issue). The double move, however, puts the hegemon in the position of challenging the institutional status quo with potentially negative consequences for the original institutional order.

I develop this argument in four steps. Section 1 presents a conceptualization of the global power shift (the explanatory variable) and the hegemon's choice of multilateral settings (the outcome variable). Section 2 discusses the conditions under which a hegemon will choose to use or defect from inclusive multilateral institutions, while Section 3 discusses the conditions under which a hegemon will choose to pursue the double strategy of strategic cooptation (via exclusive multilateralism) and power bargaining (via imposing *fait accompli* agreements). Two important features of current US hegemony, its relative decline and its continued significance, work together to explain institutional choices. The shift in power to actors with divergent preferences makes it more difficult for the US to reach consensus on its preferred outcomes and also increases the costs to the US of using its resources to overcome disagreement, while also eroding domestic support for a re-investment in multilateralism. But the US still has significant power that it can deploy to mobilize a select set of actors to join an exclusive multilateral institution, thereby creating outside options that can exert pressure on the rest. Section 4 then applies the argument to the case of negotiations over trade in services. Trade in services is an increasingly important component of global trade and national GDP, and the existing multilateral regime within the WTO is in dire need of an upgrade. Yet, the global power shift has impeded any progress towards a new regime within the WTO. Instead, the US has moved negotiations for a Trade in Services Agreement (TiSA) outside of the WTO and into a more homogeneous group that excludes major emerging economies with high stakes in the trade in services regime, such as China, Brazil, and India. Its intention, however, would be to impose this narrowly negotiated agreement on the broader WTO membership. China, meanwhile, has not been a passive bystander, but has attempted to deploy its own institutional strategies in response. The outcome of these dynamics is both economically significant and significant for the evolving architecture of global cooperation.

Global power shifts and the hegemon's dilemma

US hegemony, which we can define simply as its leadership role in managing the global order and getting other states to pursue common goals, is rooted in its predominant power; as its power predominance declines in relative terms, so does its ability to exert leadership. Even though there have been measurable changes in the distribution of power across the world over the past few decades, how we interpret 'relative decline' remains controversial given that the US maintains material superiority across most measures. On the one hand, America's share of world gross domestic product (per cent world GDP, PPP) has been declining over the past 25 years from about 23 per cent to under 15 per cent

today, with projections of continued decline.¹ China's share of world GDP, meanwhile, has grown over the past 25 years from about 4 per cent to over 19 per cent today.² Poverty is falling in some emerging economies, such as China and India, and a middle class appears to be growing. But by most other measures of GDP the US remains well ahead of China, the largest of the emerging economies. The US has a much higher level of per capita income and a much higher standard of living. The US also remains ahead on indicators of future economic potential, such as measures of technological innovation and research and economic competitiveness.³ Moreover, the US maintains substantial structural power that is not undone by the rise of several emerging economies. In terms of military power, the US outspends all other states by a large margin and is among the biggest spenders as a per cent of GDP.⁴ It also has a unique ability to project power to every part of the globe and is the main provider of security for a number of countries, even if China has a large standing army and has increased its military spending over the last few years. Ultimately, the US still has a great deal more power than other states in the system and will continue to for the foreseeable future.

The uneven rise of the emerging economies and their inability to economically or militarily overtake the US fails, however, to capture the basic insight of the global power shift – namely, rising powers' increasing importance for managing global order. Rather than conceiving of the power shift solely in terms of inter-state comparisons of economic and military resources, the intuition behind the shift is better captured by the changing *global governance significance* of rising powers. By global governance significance I mean the extent to which actors are relevant for international cooperation, specifically for achieving mutual gains or preventing mutual losses on any given issue. The increasing material power of emerging states together with growing interdependence means that states that were previously largely marginalized in international cooperation have become increasingly salient for achieving governance goals on a systemic scale. A greater number of states have a higher probability of contributing to global policy failures or successes, and in this sense power has become more diffuse (Kupchan, 2012; Nye, 2015; Posen, 2009). This is evidenced in policy areas as diverse as the response to the financial crisis, the imposition of sanctions on nuclear proliferators, or reaching agreement on policies to combat climate change. The absolute number of states and the diversity of states have not changed significantly, and their relative power increase may still present no absolute challenge to US power, but the number of states important rather than marginal to the success of international cooperation on a range of issues has expanded.

The changing number of states salient for cooperation on issues of global governance affects the hegemon's institutional strategies because it increases the diversity of interests and values that need to be negotiated. The rising powers have different interests, policy preferences, and values than the US and its traditional G7 partners across a host of issues: they have an interest in policies that promote

economic development, they tend to value social protection over liberalization, they are strongly opposed to most forms of external intervention, and their particular interests also diverge among themselves. At the same time, these actors experience a disconnect between their marginal position in many IGOs, such as the IMF and UNSC, and their salience for and exposure to global policies, leading them to demand institutional reforms – primarily greater voice opportunities – in exchange for their cooperation within institutions. By thinking about the power shift in terms of shifting relevance for achieving cooperative outcomes, we can formulate the declining hegemon's dilemma like this: On the one hand, the hegemon needs rising powers to achieve its interests when they are newly significant for cooperation on an issue; on the other hand, including such heterogeneous interests in decision-making tends to decrease the leverage of the hegemon in achieving its own preferred policy outcomes. From the perspective of the US, the question of how to accommodate rising powers within multilateral institutions becomes a question about the costs and benefits of extending or limiting the group of cooperation partners that have decision-making power.

Multilateralism, which we can define as institutionalized cooperation among three or more states on the basis of generalized rules and principles, has been a core characteristic of the modern international system and is seen by many scholars as the most prominent method of global governance (Ruggie, 1992). We can usefully distinguish between inclusive and exclusive multilateralism. Inclusive multilateralism, based on a principle of universalism, includes all actors affected by an issue. Exclusive multilateralism, also sometimes referred to as minilateralism or plurilateralism, is here defined as cooperation pursued with a limited membership, more specifically a *subset* of all actors affected by the issue at hand, where access to the group is determined by the members. I use the term exclusive multilateralism to highlight the intention to limit a potentially larger group to a smaller set of actors. Thus, I am not interested in cases of regional cooperation that are limited by geographic scope or of cooperation on issues with local or limited externalities.

The question at hand is how the global power shift, as defined above, affects the US' choice of multilateral settings and with what consequences for global multilateralism. In theory, a hegemonic actor like the US has a lot of 'go-it-alone' power, which makes unilateralism an option. Unilateralism presumes that the US can forgo cooperation altogether and achieve its own interests best without relying on others. This may be because the US is able to create private goods – goods from which it can reap all the benefits to the exclusion of others – or because it benefits more from providing a collective good than the cost of paying for it entirely, even while others also benefit from it (Olson, 1965). However, the more interesting set of cases, and those likely to be of growing frequency under conditions of a global power shift, are policy issues with global externalities that concern the provision of global collective goods for which unilateral or bilateral action on their own would be

insufficient (Hooghe et al., 2019). These are collective goods that require cooperation from others – because they require, for example, compliance or specific assets from others – and for which multilateralism can reduce transaction costs of organizing that cooperation and can mitigate distribution and enforcement concerns (Rixen and Rohlfing, 2007; Thompson and Verdier, 2013). This set of cases is of great significance because as the US' relative power declines under conditions of global interdependence, unilateral provision of collective goods should become more costly and the gains to cooperation should increase. Under these conditions, it is in the interest of the US to cooperate to enhance the provision of the collective good and to share the costs that it would otherwise have borne alone. At the same time, multilateralism may become more costly for the same reasons – the US in relative decline faces increasing difficulty imposing its preferences on the group and might have to make greater concessions to arrive at a deal. Given these considerations, I argue that we should expect the US to be most in favor of inclusive multilateralism when it is at the height of its relative power (in an issue area) and to pursue a strategy of divide and conquer when its relative power is declining and preference divergence is increasing.

Inclusive multilateralism and the costs of adapting to rising powers

A core insight of the international institutions and global governance literatures has been that the need for international collective action is driven by externalities that reach across borders and create a demand for the provision of common goods, such as collective security, open trade, or climate governance (Kaul, 2013). The effective provision of collective goods is facilitated by inclusive arrangements that extract commitments from all states (Barrett, 2007). Multilateralism saves on transaction costs and enhances the chances of reaching common agreements by bringing more actors to the table, thus increasing bargaining possibilities and opening more issue linkage opportunities (Koremnos et al., 2001). Liberal institutionalists have emphasized the benefits of inclusive multilateralism for reducing the costs and enhancing the legitimacy of great power leadership in particular (Ikenberry, 2001). At the height of its relative power after WWII, the US used multilateral institutions to secure cooperation from less powerful states who received a voice in decision-making in exchange for accepting rules that largely served US interests. The Cold War provided an incentive for the US to seek cooperation among a large number of states and to use large-scale, rules-based multilateralism to reduced transaction costs, keep states within its orbit of influence, and to incentivize coordination around its own policy preferences.

These benefits of inclusive multilateralism, however, depend on a certain degree of interest overlap and compliance incentives that are not always given. When goals and interests diverge, distributional conflicts increase, achieving consensus on policies becomes more costly, outcomes are delayed and wars of attrition can occur, leading to no

outcomes or lowest-denominator outcomes. During the Cold War and the immediate post-Cold War period, often described as the unipolar moment, the costs to using large-scale multilateralism were relatively low for the US because of a broad alignment of interests between the US and countries in its sphere of influence. Even during this period, however, US support for inclusive multilateralism was contingent; the US expected major allies to defer to American leadership and interests. When goals and interests diverged, the US deployed its hard and soft power resources to enforce convergence around its preferred outcomes. As hegemonic stability theory argues, when a leader expects to reap benefits it is willing to use its power predominance to facilitate cooperation among heterogeneous actors by using side-payments, selective incentives, negative inducements, or rhetorical and moral persuasion to mobilize coalitions, promote compliance, or extract concessions. The US has regularly pursued this strategy within IOs by, for example, using the distribution of foreign aid and other benefits to influence voting within the UN (Carter and Stone, 2015). In short, high levels of power asymmetry can facilitate cooperation within a large group, making it more likely to reach levels of collective action otherwise more likely in a small group (Olson, 1965). Thus, from the perspective of the hegemon, large-scale multilateralism offers significant benefits for achieving collective goods but the benefits have to outweigh the costs of side-payments and inducements required to align others with its own preferences.

Under conditions of a global power shift, however, multilateralism becomes more difficult because preference heterogeneity and distributive concerns intensify collective action problems, while at the same time changes in relative power increase the costs of overcoming these challenges. As a greater number of states with divergent interests becomes salient for cooperation, it becomes more difficult to reach agreement and more costly for the hegemon to enforce consensus around its preferred outcomes because of its reduced leverage and higher transfers needed to overcome preference heterogeneity. With the end of the Cold War, the emergence of newly significant economies, and the relative decline of the US beginning in the early 2000s, the US' ability to dominate inclusive multilateral institutions waned. As formerly marginal states gain in relative power, institutional rules such as consensus-based or one state-one vote majority decision-making rules can now be used more effectively to protect their gains, promote their growth, and – where these are at odds – to hinder US interests. Rising powers might have the ability to frustrate cooperation by holding out their (needed) cooperation to wait for a better deal, while not (yet) having the power to break through deadlock and facilitate achievement of cooperative outcomes. We can see the consequences in what has been described as the 'gridlock' of the international system (Hale et al., 2013). The Doha trade round, climate negotiations, and impasse at the UN can be attributed, in part, to the newfound ability of rising powers to exert leverage in negotiations on behalf of interests that conflict with those of established powers. As one senior US official under Obama

put it: 'It is remarkable how closely coordinated [Brazil, South Africa, India, China] have become in international fora, taking turns to impede US/EU initiatives'. Uncertainty over the national benefits of large-scale multilateralism and fears of losing out to rising powers also erode domestic support for investing in the side-payments and concessions necessary to make global multilateralism work. Overall, the power shift makes it more difficult for the US to determine outcomes in multilateral settings where actors with divergent interests are empowered, it increases the costs of side-payments and concessions that could achieve agreement, and it erodes domestic support for investing those resources.

The challenges of collective action when preference heterogeneity is of increasing salience create incentives for declining but still powerful leaders to reduce the costs of coordination by using institutional designs that manage or minimize preference diversity (Kahler, 1992). In other words, they have incentives to move negotiations over collective goods to clubs with a more limited membership. Within an institution where actors share some degree of common values, goals, and interests, demands for redistribution and the obstacles to collective action should be lower, facilitating policy coordination and consensus. The benefits of scale that are lost by forgoing large-scale multilateralism can potentially be recaptured once a club deal has been reached. When the losses associated with the global power shift are not overcome by the cost-sharing effects, hegemonic actors have incentives to challenge the status quo by forming exclusive clubs that enable a strategy of divide and conquer.

Exclusive multilateralism and the strategy of divide and conquer

The hegemon's frustration with inclusive multilateralism under a global power shift turns it into a challenger of the status quo and creates incentives for it to pursue *exclusive multilateralism* on issues with high preference divergence. Rather than accommodate rising powers within existing arrangements, hegemonic actors pursue counter-institutionalization by creating new clubs with a select set of 'like-minded' actors (Zürn, 2018). This move provides two key benefits: it facilitates cooperation and thus overcomes the deadlock that results from stalled negotiations between rising and established powers, and it provides a mechanism for re-imposing the hegemon's preferences on the original institution. This strategy for coping with rising powers is a mix of *strategic cooptation* that peels off a sub-group from the larger group followed by *power bargaining* to impose the small group solution on others (see Fioretos, this issue). But under what conditions can a hegemon pursue this strategy and how might it work?

Strategic cooptation is an integrative bargaining strategy by which the hegemon 'buys' the support of like-minded states through promises of maximizing joint interests, offering a seat at the bargaining table, and increased likelihood that the hegemon itself will stick to the deal (Kruck and Zangl, this issue; see Fioretos, this issue; Stephen and

Stephen, this issue; Thompson, this issue; Vabulas and Snidal, this issue). Given incentives to move to exclusive multilateralism, two additional conditions must be met before a hegemon can use this strategy. The first condition is the *availability of like-minded states*, a sub-group of those affected by the issue. These are actors who can contribute to the financing or production of the collective good along the preferences of the hegemon and whose contribution is greater than the marginal cost (to the hegemon) of reaching agreement. The second condition is the *ability of the hegemon to mobilize* these actors. Generally speaking, a hegemon, by virtue of its still significant power, should be well-placed to mobilize at least a sub-set of states. In order to coopt, the hegemon needs sufficient 'convening power' in the issue area based on its ideological, market, or military resources to incentivize participation. It can use its agenda-setting and convening power to select the states it wants to cooperate with or to exclude states with which cooperation is likely to be difficult.

The criteria for joining an institutional arrangement can be explicit or implicit, but they will be aimed at promoting a certain degree of interest convergence. Such institutions will arise in a manner that responds to the technical and distributional characteristics of the particular cooperation issue in question and the characteristics of the population of states that might be members. Thus, we should see exclusive multilateral institutions form around *specific issue areas* or around *actor attributes*. Exclusive multilateralism can occur on an ad hoc and informal basis and does not necessarily require the creation of a formal organization. The informal institution can be created within or outside of an already existing formal institutional body. Moreover, because exclusive institutions concentrate power among a sub-set of political actors with closer preferences, it will be less costly to distribute decision-making authority more equally within the group. This, along with the convening power of the hegemon, makes joining such an exclusive institutional arrangement attractive for other states. The US has been able to set up exclusive multilateral arrangements in areas of financial regulation, trade, and security where it could not achieve its priorities through inclusive multilateralism; examples include the Financial Stability Board, the 'Really Good Friends of Services' grouping, and the Proliferation Security Initiative. In these examples, the US, through its market or military power, was able to attract a select group of states to negotiate a cooperative agreement on a specific issue that would not have been possible within the respective multilateral institution because the larger grouping would have included newly powerful veto players.

The hegemon's use of strategic cooptation to pursue exclusive multilateralism has an important additional effect. The hegemon effectively uses strategic cooptation to change existing institutional conditions by creating an 'outside option' for itself, which it can then use to enhance its power bargaining position *vis-à-vis* others (e.g. rising powers with increasing leverage). *Power bargaining* is a distributive strategy that relies on the imposition of costs to promote a

particular position and to undermine opposition (Kruck and Zangl, this issue; see Lipsky, this issue). When the hegemon reaches a deal among a coalition of states, it imposes costs on those states who are excluded but who have preferences over the outcome. Agreement within a sub-set of actors produces a *fait accompli* which can be used as leverage to coerce other actors to accede to the deal on terms they did not negotiate, thereby preserving and projecting hegemonic influence by making non-members price-takers (see also Vabulas and Snidal, this issue). The barriers to re-negotiation by later joining members will be high and the terms of the deal will already have been set. In this way, exclusive multilateralism can be used to circumvent negotiation deadlock in more inclusive institutions and to force an agreement in the interest of the hegemon.

The divide and conquer strategy does not come without risks or potential costs. First, rising powers can be expected to react to this dynamic by trying to mobilize their own institutional strategies. Second, by forcing acceptance of its deal outside of inclusive multilateral institutions, the hegemon risks undermining or challenging those existing institutions. As I discuss below, both outcomes may paradoxically undermine the hegemonic order by fostering institutional fragmentation, weakening the policy-making function of universal multilateral institutions, and de-coupling policy-making from policy-legitimizing institutions.

Case study: Negotiating a trade in services agreement

I use a case study of negotiations over a trade in services agreement to evaluate my argument and to gain insight into how the power shift works as a causal mechanism with respect to explaining institutional strategies. The US has moved its policy coordination efforts out of inclusive multilateral settings and into exclusive multilateral settings on a number of issues, but trade in services represents a particularly important and understudied case given its economic significance and the decades-long attempt to reach agreement within the WTO. Diagnostic pieces of evidence from this detailed within-case analysis allow me to process trace the sequence of events over time and to test the plausibility of the causal argument (Collier, 2011). The case study lends empirical support to the argument that the power shift, via the mechanism of increased salience of actor preference heterogeneity, can serve as an explanation for the US' strategic choice over institutional settings. Moreover, it allows me to highlight the strategic dynamic between the US' moves and rising powers' responses. I consider how the power shift incentivizes the US to pursue exclusive multilateralism among like-minded states in order to facilitate agreement on its preferred trade policies and to enhance its power bargaining leverage *vis-à-vis* the larger WTO setting. I then consider how the relevant rising power, in this case China, reacts with its own strategies of rhetorical coercion, strategic cooptation, and power bargaining. Finally, I address the consequences of this sequence for multilateralism.

The power shift and preference heterogeneity

The liberalization of international trade has been a centerpiece of the post-WWII multilateral institutional order. This regime has largely been concerned with trade in goods, but trade in services represents a growing part of the global economy. 'Services' refers to intangible products such as travel services, professional services (e.g. legal, accounting, human resources), financial services, distribution services (e.g. transportation and logistics), electronic services (including e-commerce and telecommunications), and so on (Fefer, 2017). For many countries, trade in services represents a large and growing component of trade. Trade in services currently accounts for about a fifth of global trade and has been steadily increasing since 2000 as national economies move from manufacturing to service-based economies (WTO, 2019). In the US, services account for about three-quarters of GDP, over 70 per cent of private sector jobs, and over one-third of exports (U.S. International Trade Commission, 2019). Based on the latest available figures, the US is the world's largest exporter and importer of services,⁵ and in contrast to its current account deficit on trade in goods, the US enjoys a large surplus in services trade. Given its competitiveness in the industry, the US has an interest in opening international markets for services and it has been a strong promoter of services trade liberalization. Trade in services are largely regulated through non-tariff 'behind the border' barriers at the national or sub-national level, such as licensing regulations, labor laws, environmental protections, and data protection laws, which increase the costs of trade in services across national borders. A services trade agreement aims to liberalize barriers by, for example, establishing common standards or standards of mutual recognition.

The only currently operative multilateral framework codifying trade in services, the General Agreement on Trade in Services (GATS), was negotiated under the GATT during the Uruguay Round and went into effect for all WTO members in 1995. The GATS covers all services except those not supplied on a commercial or competitive basis (e.g. military defense) and it follows basic principles similar to the GATT, including most-favored-nation treatment (MFN) that disallows trade discrimination between WTO members. The negotiations succeeded in setting up a framework that provides the foundation for all other attempts to liberalize trade in services, but the effects have been modest with most changes happening in a limited number of sectors. Indeed, the Uruguay Round was meant to be a first step in a longer process. The basic principles include a commitment to progressive liberalization and GATS required members to launch new negotiations, which began in 2000 and continued under the Doha Round.

Negotiations were undertaken within the WTO because it provided a large-scale multilateral negotiating forum meant to foster cooperation by including many actors at the same table, enabling issue linkages and side payments, and providing an established process for negotiating, monitoring, and enforcing trade agreements. But these characteristics became liabilities as the economic leverage of major

emerging economies increased over the decade, intensifying the challenges of preference heterogeneity. Between 2005 and 2017, trade in services expanded faster than trade in goods (WTO, 2019). In this period, developing economies' share of global trade in services grew by over 10 percentage points (WTO, 2019).⁶ Among developing countries, China and India are leaders on both exports and imports of services. In Brazil, China, and India, services account for half or more than half of total GDP, while trade in services accounts for about 5.5 per cent of GDP in Brazil and China, and 12 per cent in India.⁷ Moreover, the potential for expansion of trade in services with large emerging economies is great as these countries diversify their economies and transition to services. While many developed economies currently enjoy trade surpluses as net exporters of services to the rest of the world, China, India, and Brazil continue to increase their own services exports and to penetrate foreign markets, especially in the US and EU. Although developing countries were initially not very receptive to GATS (Chadha, 2001), as they grew they became 'active *demandeurs* in WTO and regional negotiations. This is especially true in areas where they enjoy strong comparative advantages, such as in tourism, construction, computer, shipping and a host of labour-based services' (Sauvé, 2004, p. 2).

The growing leverage of certain developing countries, accompanied by interest divergence and distributional concerns, impeded the Doha negotiations on trade in services. WTO countries have conflicting preferences on issues ranging from liberalization of labor mobility, to data protection and privacy concerns, to disciplines on state-owned enterprises (SOEs) meant to reduce the discretion of governments to use state ownership as a tool for trade protectionism. Market asymmetries made developing countries worry that liberalization would open their service markets to service providers from developed countries without improving access to developed markets for developing country services (Hoekman and Mattoo, 2011). The existing GATS includes provisions to protect developing countries, such as Article XIX which provides that 'there shall be appropriate flexibility for individual developing country members, and especially least developed countries, to open fewer sectors, liberalize fewer types of transactions, extend market access in line with their development situation and attach conditions aimed at strengthening their domestic services capacity and competitiveness' (WTO, 1995). While developing countries seek to maintain protections offered by GATS, developed countries, led by the US, view them as outdated and unfair and seek to 'level the playing field'. Ultimately, progress on a new trade in services agreement was impossible within the inclusive multilateral setting given that all WTO members have a de facto veto power.

Exclusive multilateralism as strategic cooptation

Because of the lack of progress in the Doha Round, in 2012 the United States announced its intention to negotiate a plurilateral Trade in Services Agreement (TiSA) outside of the WTO (Fefer, 2017). With the support of Australia, the US

initiated negotiations in April 2013 among a sub-group of WTO members dubbed the 'Really Good Friends of Services' (RGF) group. The RGF began as a select group of 16 like-minded members with similar interests in services liberalization. The group has also been called a 'coalition of the willing' 'as each participant sees a national interest in liberalizing trade in services' (Fefer, 2017, p. 5). Shared trade interests along with the sheer market power of the US in this sector allowed the US to mobilize countries to join the standards-setting deal. The costs of being excluded from any such deal were clear. According to Viviane Reding, an MEP and the European Parliament's rapporteur on the pact, 'If we get these negotiations right, TiSA is an opportunity for Europe to consolidate its position as a world leader in services trade ... We need to be standard-makers today, not to be standard takers tomorrow' (quoted in Mucci, 2016). The RGF has since expanded to include 23 members, including twelve G20 members, and the US has said that it is in principle open to adding other WTO members who are willing to agree to its premises. As Canada has diplomatically put it, the negotiations are open to other WTO states 'provided that they demonstrate an ability and willingness to be constructive and ambitious'.⁸

Notably absent from the negotiations, however, are the large emerging economies who are net importers of services, including Brazil, Russia, India, China, South Africa, and Singapore. In fact, China requested to become part of the group, but the United States has blocked it from joining. In the words of one negotiator interviewed by Politico, 'China is a heavyweight. If it was included in the negotiating process, the U.S. would have to negotiate taking into account very different positions from its own ... The U.S. wants to decide the rules and then have every country that wants to join the TiSA simply follow them' (Mucci, 2016). According to Fefer (2017, p. 15), 'it is unlikely new members will join the TiSA negotiations unless they are willing to accept the provisions agreed to thus far in negotiations'. The US has thus maintained control over composition of interests represented in the group.

The RGF group has met regularly since 2012 under the leadership of the US to discuss a comprehensive agreement on trade in services based upon but going beyond the GATS. The negotiations have been happening in secret, with the first information on the deal coming to light in 2015 when Wikileaks released documents regarding the meetings (Wikileaks, 2015). The EU has subsequently released position papers giving some indication of what the draft framework looks like.⁹ Unlike the hundreds of preferential trade agreements (PTAs) that have burgeoned since the 1990s, the TiSA represents a plurilateral agreement. In practice PTAs are generally not highly discriminatory, in part because their proliferation has essentially increased rather than restricted preferential access to markets (Rocha and Teh, 2011). Plurilateral agreements, in contrast, may be more successful at allowing discrimination because of their exclusive nature. Plurilateral agreements reached in an exclusive multilateral setting, such as the TiSA, are narrower in scope than PTAs and such sector-specific market concessions to only select

members are contrary to the MFN principle at the heart of the WTO (Hoekman, 2015). Indeed, TiSA participants agreed to conduct the negotiations on a non-MFN basis such that the benefits of the commitments would apply only to those who sign the agreement (Fefer, 2017). The RGF thus helps to mitigate points of disagreement that would likely arise within the larger WTO membership and facilitates a services agreement closer to US preferences. The US moved negotiations on trade in services outside of the WTO because it anticipated costly conflicts over issues such as the extent, timing, and scope of liberalization. For example, the agreement appears to not extend those GATS provisions that accommodated the concerns of developing countries regarding protections for their national services and instead promotes the ability of foreign actors to provide services in those countries. State-owned enterprises, which are a key component of state-led economies such as China's, are given fewer protections and are treated like private businesses. And regulations regarding data flow, which is one of the most controversial issues between the EU and the US, would be even more contentious if the negotiations included China. At the same time, the US has tried to minimize any costs that might accrue to it as a result of excluding certain actors from the deal. For instance, the US supports an 'MFN-forward' approach which would require TiSA members to automatically extend to all other TiSA members any benefits that it grants to other countries in future bilateral or regional trade deals (Inside U.S. Trade, 2016).¹⁰

Multilateralizing through power bargaining

Even though the negotiations have taken place outside of the WTO, the Really Good Friends of Services are reportedly debating how the agreement could be further 'multilateralized' by incorporating it into the WTO (Fefer, 2017). According to reporting by Politico, a European Commission source admitted that 'Once the agreement comes into force we are hoping to integrate it into the World Trade Organization, in other words, have its rules accepted by all 162 WTO members and become the benchmark for global trade in services' (Mucci, 2016). Current negotiating members account for 70 per cent of the world's trade in services and a common governance structure among them would give them power bargaining leverage. Through the setting of exclusive multilateralism, the US can present outsiders with a fait accompli, weakening the negotiating position of those outsiders who will need to engage with the TiSA agreement if they wish to move forward on trade in services liberalization. 'It's nearly certain that those countries outside of TiSA will want access to the biggest common service market on the planet', according to a negotiating official (Mucci, 2016). But outsiders, including newly powerful countries such as China, will have to accept entry on the terms already negotiated within the exclusive group, making them price-takers. With a TiSA in hand, the US would have created a tool of power bargaining that puts pressure on excluded WTO

members to adhere to a plan that was not achievable in the broader membership (Hoekman, 2013). This is one reason why plurilateral agreements have been unpopular among many WTO members, especially emerging economies, while exclusive multilateralism has become attractive to the US as a hegemon facing a global power shift (Hoekman, 2015, p. 546).

Strategic dynamics: China responds

The significant hard and soft power resources of the US, along with its privileged position within those multilateral institutions it helped to create, provide it with strategic advantages not readily available to any other power in the system. Nevertheless, the institutional strategies outlined in the framework article – power bargaining, strategic cooptation, rhetorical coercion, and principled persuasion – are in theory also available to other powers, such as China. Indeed, China has a strong interest in the development of global trade rules and did not simply remain passive as the US moved to exclude it from a trade in services agreement. China initially responded to the US moves with rhetorical coercion, followed by attempts at strategic cooptation, and finally power bargaining. China was not successful in these responses in that it has not been included in the TiSA and is likely to become a rule-taker once – and if – the TiSA comes into force. In an interesting twist, however, the current US administration's ambivalence on trade liberalization may open a path for China to influence trade in services rules after all.

On the face of it, China and the US both have an interest in liberalizing their trade in services. The US would benefit from liberalized trade in services with China since the US is a net exporter of services and increased trade with China would improve the US' bilateral trade deficit with China. China, in turn, is transitioning to a services-oriented economy and it has been implementing policies to increase its export of services. China's first preference was to have trade in services negotiations take place within the WTO, where it has a formal negotiating status and institutional influence. Thus, China's initial response to the RGF initiative was to engage in *rhetorical coercion* that pointed to the legitimacy of the WTO as a negotiating forum and the normative importance of inclusive multilateralism. Especially as China's influence within the WTO grew, it became a vocal opponent of negotiations taking place outside of the WTO framework. The Chinese delegation to the WTO made statements 'saying TiSA was going to be the death knell of the multilateral system' (Donnan, 2013). In the WTO General Council it warned that multilateralism is 'in crisis' and echoed the sentiment that 'multilateralism is at a crossroads', calling for a re-commitment and doubling-down by members (WTO, 2012). This was a relatively low-cost option that coincided with the norms of the community and was a position supported by other WTO members. But the US' use of strategic cooptation, based on its material and ideological power, was successful at mobilizing powerful states to negotiate

outside of the WTO. Moreover, China's own soft power on trade norms was not particularly high, civil society attention on the issue was initially low, and the RGF made explicit their intention of inserting the agreement into the WTO system, thereby taking the edge off of the rhetorical pressure.

By 2013, when TiSA negotiations took off, China adopted a different response by actively trying to join the RGF and the TiSA through a version of *strategic cooptation* by which it promised to abide by the negotiated agreement if it were allowed to join. China's Commerce Minister, Gao Hucheng, initially raised the idea of acceding to the talks with the US Trade Representative, Michael Froman (Donnan, 2013). The US, however, rebuffed these advances, concerned that China, given its still relatively high service trade barriers, would water down the agreement, obstruct liberalization, or push for long phase-out periods for barriers. China then turned to Europe and held talks with EU officials in which it offered the EU assurances that it shared the objectives of TiSA and was willing to meet the obligations agreed upon by current participants in exchange for EU support of its application. This strategy culminated with President Xi Jinping's visit with the EU Trade Commissioner in 2014, after which the EU released a statement saying that 'China has reassured the EU' and, as a result, 'the EU will now strongly support China's swift participation in the Trade in Services Agreement (TiSA) negotiation' (European Commission, 2014). While this strategy appeared to work with the Europeans, who see strong material benefits in China's inclusion, the US continues to block China's participation.¹¹ The EU appears more concerned about keeping the US in the deal than in pressuring the US to allow China to join in the negotiations.

With little hope of being included in the TiSA negotiations, China moved away from its initial insistence that multilateralism take place within the WTO and instead pushed harder on promoting regional trade agreements. 2013 marked the first round of negotiations for a Regional Comprehensive Economic Partnership in Asia (RCEP), which currently includes the ten ASEAN member states and five partner states but excludes the US. China's commitment to the RCEP has been interpreted as a kind of counter-institutionalization or *power bargaining* move by which it creates a strong outside option with a view to both creating pressure on other agreements and pursuing its own rule-making. China has been a strong supporter of the RCEP in part because it sees the agreement as a tool to counter US efforts to shut China out of trade agreements such as the Trans-Pacific Partnership (TPP) and the TiSA. The RCEP, which has yet to be signed, would be an opportunity for China to set regional trade rules without the influence of the US and to liberalize its own access to developing markets in the region. The RCEP negotiations began with a commitment to, among other elements, a liberalization of trade in services (ASEAN, 2012), but the current agreement includes limited provisions that only weakly liberalize services compared to other draft agreements (such as TiSA or TPP) and it largely fails to prohibit barriers to e-commerce and cross-border data flows (Terada, 2018). It thus would institutionalize a weak liberalization of trade in services that maintains many protections in place.

Outlook and implications for multilateralism

After many years and multiple rounds of negotiation, TiSA members at a ministerial meeting in Davos affirmed their intent to finalize a deal by 2017. Instead, momentum on the agreement has since stalled as the political climate in the US and Europe moved away from trade liberalization altogether. Although both the EU and the US Trade Representative officially still support TiSA, the current US administration has not made it a priority. The Trump administration, in the meantime, has chosen a more directly confrontational approach towards China, especially on trade. In 2020, in the wake of the US–China trade war in which the US used tariffs to impose costs on China in order to gain concessions from it, the two countries signed the so-called 'Phase-One' deal.¹² In the area of services, the US used the deal to push China to open its financial services sector to US competition and to extract a pledge from China to purchase \$37.9 billion of services, such as cloud computing, financial services, travel and tourism. What the deal does not do, however, is create a rules-based framework for future trade relations.

The TiSA agreement, in contrast, is designed to be a broader framework of trade rules. If signed, it will certainly affect the future of trade in services and have broader institutional consequences. First, it allows the US to achieve its own interests by setting the standard on trade in services and locking in those interests against a likely future shift in market power on services. Second, a TiSA is likely to further weaken the WTO and, with it, inclusive multilateralism. The TiSA takes trade in services negotiations out of WTO control and relocates it to a sub-set of actors, relegating the WTO to the role of providing minimum common standards. The TiSA does not have broad multilateral support from within the WTO, where actors such as Brazil and India have expressed general opposition to pursuing plurilateral agreements (Hoekman, 2013). Whereas the WTO now clearly states that the GATS 'is the first and only set of multilateral rules governing international trade in services',¹³ with the TiSA there would be two general trade in services agreements. Moreover, exclusive trade negotiations, such as TiSA, have pushed China to pursue agreements within its own sphere of influence. Overall, this leaves the WTO's policy-making function undermined (Hoekman, 2013). Third, the US strategy of divide and conquer not only moves policy-making out of inclusive settings but it then attempts to use those inclusive settings to gain broad acceptance for the exclusive agreements. This approach runs the risk of decoupling policy-making from policy-legitimizing institutions. Asking the WTO to provide collective legitimacy for policies decided on by a sub-group is likely to meet resistance and to compromise the WTO's ability to deliver that legitimacy since fair and inclusive participation is one important source of its legitimating authority.

Conclusion

Despite concerns that the Trump administration has been uniquely damaging to the liberal institutional order, the

US' commitment to inclusive multilateral institutions, such as those that characterized the post-WWII order, is likely to decline as a result of structural changes. On those issues where the US' power is still significant but in relative decline, and where rising powers with divergent interests are of increasing significance for achieving cooperation, the US will have incentives to pursue cooperation within exclusive multilateral settings that circumvent the problems of preference heterogeneity. Trump's apparent affinity for 'bilateral deals' is one extreme manifestation of this logic. The power shift need not be the only reason for cases of exclusive multilateralism, but it is an important one.

The hegemon's institutional response to the challenges of rising powers elucidated here, strategic cooptation of the like-minded followed by power bargaining on the rest, is likely to have a number of implications for the shape of the institutional order. First, it offers an explanation for why, in contrast to the arguments of liberal institutionalists, we have not seen the US re-commit to inclusive multilateralism as a strategy for overcoming the challenges associated with a global power shift. The hegemon is unlikely to react to the global power shift by accommodating rising powers with greater decision-making authority within inclusive multilateral institutions as long as preferences are highly divergent. As the anticipated costs of including rising powers increase relative to the benefits, the hegemon will be more likely to drag its feet and pursue other strategies for achieving cooperative outcomes.

Second, my argument offers a theoretical explanation for Morse and Keohane's (2014) empirical observation of 'contested multilateralism', or the fragmentation of the institutional order. Power shifts that increase the salience of preference heterogeneity hinder large-scale cooperative outcomes and become a motor for moving policy making out of inclusive, general purpose multilateral fora and relocating it into sub-groups of actors defined by their actor attributes or their issue-specific interests. This implies that institutionalized cooperation will be more specialized and more targeted. Broad multilateral international organizations, in turn, will lose agenda-setting and negotiating authority. Indeed, frequent use of exclusive multilateralism may even decrease the returns to using multilateral institutions over time, further weakening these.

Third, exclusive multilateralism can lead not just to fragmentation but to a division of labor between policy making and policy-legitimizing institutions. The post-WWII model of international organization was based on a (incomplete) notion of representation and voice that was supposed to not only facilitate cooperation but also create legitimacy for policy outcomes. As exclusive multilateral institutions become venues for policy creation while those policies are then imposed on the "rest" via inclusive organizations, the link between policy making and policy-legitimation is severed.

Finally, and relatedly, the divide and conquer strategy is meant to have strong distributive effects. In particular, it limits the ability of excluded actors to influence global governance, thereby undermining a key tool for enhancing global

justice. The ability to selectively include actors into cooperation agreements will likely have the most negative distributive consequences for the least powerful states, but it should also dampen optimism about the prospects for rising powers to influence global governance outcomes. As long as powerful clubs of common interest proliferate, rising powers will likely find it difficult to gain systematic and structural – as opposed to ad hoc – leverage over global governance.

Notes

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1. IMF data available from: <https://www.imf.org/external/pubs/ft/weo/2016/01/weodata/weorept.aspx?sy=1981&ey=2021&scsm=1&ssd=1&sort=country&ds=.&br=1&pr1.x=75&pr1.y=12&c=111&s=PPPSH&grp=0&a=> [Accessed 30 January 2020]
2. IMF data available from: https://www.imf.org/external/datamapper/PPPSH@WEO/OEMDC/ADVEC/WEO_WORLD [Accessed 30 January 2020]
3. In 2018, the World Economic Forum ranked the US as the most competitive economy. <https://www.weforum.org/agenda/2018/10/most-competitive-economies-global-competitiveness-report-2018/> [Accessed 30 January 2020]
4. Data available from: http://www.sipri.org/research/armaments/milex/milex_database [Accessed 30 January 2020]
5. This ranking considers EU countries separately. Data from the Office of the United States Trade Representative. Available from: <https://ustr.gov/about-us/benefits-trade> [Accessed 30 January 2020]
6. This figure excludes least developed countries (LDCs).
7. World Bank data available from: <https://data.worldbank.org/indicator/BG.GSR.NFSV.GD.ZS> [Accessed 30 January 2020]
8. Global Affairs Canada <https://www.international.gc.ca/trade-agreements-accords-commerciaux/topics-domaines/services/tisa-acas.aspx?lang=eng#c> [Accessed 30 January 2020]
9. Available from: https://ec.europa.eu/search/?query_source=TRADE&QueryText=TISA [Accessed 30 January 2020]
10. Not surprisingly, other members, including the EU, oppose this and are seeking to make it optional.
11. Although, interestingly, the EU's statement in the same breath acknowledges that the US is not likely to agree.
12. Officially known as the "Economic and Trade Agreement Between the Government of the United States of America and the Government of the People's Republic of China," available at: https://ustr.gov/sites/default/files/files/agreements/phase%20one%20agreement/Economic_And_Trade_Agreement_Between_The_United_States_And_China_Text.pdf [Accessed 30 May 2020]
13. Statement available from: https://www.wto.org/english/thewto_e/whatis_e/tif_e/agrm6_e.htm [Accessed 30 January 2020]

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