
The US is painting itself into a corner on 21st century trade policy

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America's best chance at getting better access to the world's fastest growing economies is on the table – it is called the Doha Round. The US should push hard for a conclusion as the alternatives are much worse. The US faces great domestic and foreign problems in pursuing the regionalism alternative. In particular, US faith in the Trans-Pacific Partnership seems to be based on unclear thinking about political constraints at home and political reactions abroad.

The Obama Administration is getting ready to paint itself into a corner on 21st century trade policy. The key event is the 29 April 2011 meeting of the Doha Round's steering committee that will decide the Round's fate.¹

The basic issues are simple. Obama feels that he cannot win the domestic political battle against US protectionists without fulsome support of US export interests. Such support, he believes, would require much larger tariff cuts by emerging economies – especially China, India, and Brazil. As these nations say they cannot offer greater cuts, Doha is deadlocked.

All indications are that the US is pushing for a suspension of the Round, or some similar tactic. The goal, it seems, is to shield the Obama Administration from pressures to make any compromises this year or next.

¹ The steering committee is known as the Trade Negotiating Committee; all members are on it and it is chaired by the WTO Director-General Pascal Lamy.

Woolly and wishful thinking in Washington

Washington's thinking on this seems incomplete.

- Obama's stalling makes perfect sense from a short-term domestic political perspective.

US exporters of manufactured goods, service, and agriculture are not pushing for Doha. They reaped handsome harvests from emerging markets' unilateral tariff cuts this century but view this as history. They focus only on the new market access and they are unimpressed.

- The unclear thinking concerns medium-run alternatives for US trade policy.

The most critical point turns on the timing of what happens next.

If the 2011 deadlock is for real, no deal is possible before 2020

There is still a glimmer of hope that the Doha deadlock is tactical – brinksmanship rather than an unbridgeable gap. But if it the deadlock is real and Doha cannot be done in 2011, then no deal is likely until the end of the decade.

This not-before-2020 is a bold conclusion, but consider the logic.

As Claude Barfield argues in his essay, US labour unions oppose trade liberalisation, offshoring, and globalisation. Labour unionists are the “foot soldiers of Democratic election armies”, so Obama will not risk further alienating them during the election year. Nothing will be done in 2012.

Many view 2013 as the next window but let's think that through. The US political scene is likely to be much worse in 2013 – scared by divisive debates over spending and taxes driven by extreme positions taken on the size and role of government. In this poisonous climate, Obama will find it harder to compromise on multilateral trade liberalisation.

The obvious way to break the deadlock starting in 2013 will be to give China something to bargain for. The big US concessions in this Round are on agriculture. These interest Brazil but China and India will only find it politically optimal to cut their tariffs further if Chinese and Indian export interests are offered prizes that make them willing to push their governments into signing the deal.

The predicament is the delay this agenda-expansion would entail. History tells us that it takes years to negotiate a new agenda, and then years to complete the actual bargaining.

In short, if the US and Chinese are unwilling to break the deadlock in 2011, no deal is likely before 2020.

Can't Obama follow the regional route?

If Obama allows Doha to fail, it is surely in part because he believes the US can pursue its trade ambitions via the regionalism route. But let's think that through. Apart from agriculture, US exporters face fairly low barriers when exporting to other developed nations but not when it comes to the world's fastest growing markets – especially Brazil, India and China.

Given US domestic politics – which makes FTAs with low-wage nations difficult for the US to ratify – and domestic politics in large emerging economies – which makes NAFTA-style FTAs with the US difficult to sign, the bilateral route seems very unlikely to work out well for the US.

This is not speculation, it is a fact. The pairing of US domestic politics and Asian domestic politics, American is already seriously behind its main industrial rivals when it comes to bilateral agreements in Asia. Allowing Doha to die will not change the structural impediments that are hindering US FTAs with Asians, but not those of the Europeans and the Japanese.

The two big US domestic problems are agriculture and labour unions. The US is a major food exporter, so it insists that its FTA partners remove their food tariffs. Many East Asian nations are allergic to food liberalisation, so signing FTAs with the US is a difficult deal (witness the Korea US FTA). Europeans and Japanese, by contrast, are quite happy to leave aside all sensitive agriculture goods. US trade unions' opposition to trade agreements with low-wage nations is the second problem (witness the many years it took to ratify the Colombia US FTA).

But Obama has a plan to fix all this – it is called the Trans-Pacific Partnership (TPP) agreement. Let's think that through.

What happens if labour unions view TPP as an offshoring agreement?

The Obama Administration's big hope is the TPP. The US is negotiating the TPP with 8 other nations. It already has FTAs with the 4 bigger ones, so there will be no new market access from them and precious little from the other four. This makes it clear that TPP is not mainly about preferential tariffs – it is about providing 21st century rules for 21st century trade.

When supply chains internationalised, trade became more complex, revolving around a “trade-investment-service nexus” (Baldwin 2011). Firms invested in production stages internationally to lower production costs and linked the facilities via trade and infrastructure services (telecoms, express mail, air cargo, internet, etc.). The Obama Administration hopes that TPP will set the rules that 21st century commerce needs. As USTR Ron Kirk put it: “the agreement will create a potential platform for economic integration across the Asia-Pacific region.”

As commendable as this may be from the US business perspective, US trade unions may view TPP as making the world safe for American outsourcing. The fact that two of the current TPP members have labour rights issues on par with Colombia will create even more problems.

One would have to be quite the optimist to think Obama can rapidly implement TPP and then expand it to include other low-wage Asian nations. But US opposition is not the only threat to Obama's hopes for the TPP.

Suspicion of US motives among potential Asia-Pacific members

A key assumption behind US hopes is that TPP will create a domino effect. Although TPP starts small, the US wish is that it draws in all the fast-growing Asia-Pacific economies. The biggest wish of all is that India and China will eventually have to join this agreement dominated by American rules. There are two serious flaws in this thinking:

- First, applying the domino theory of regionalism to this situation is problematic given the lack of preferential market access mentioned above.

Empirical evidence in the World Bank's forthcoming Handbook on Regionalism and the WTO's forthcoming World Trade Report confirm the lack of trade diversion from "deep" FTAs. The basic economics is simple. Many of TPP's rules would make it easier for all nations to run the trade-investment-services nexus in, say, Vietnam. National reforms on investment rights, intellectual property rights, FDI-linked capital flows, and infrastructure services do not come with rules of origin.

- Second, some Asia-Pacific nations have begun to worry about why the Obama Administration is so interested in the TPP.

Japan is hesitant to join – given the insistence on radical agriculture liberalisation. Korea finds it hard to see what TPP offers beyond the Korea-US FTA and worries about being part of a plot to corner China and India. A TPP without Japan or Korea is not the sort of agreement that will force China and India to grant the US better market access. The large ASEANs may join, but they already have TPP-like agreements with Japan. Without compulsion, India and China will never join. China – and increasingly India –

are at the heart of the trade-investment-services nexus even without a 21st century trade agreements. Their markets are large enough to attract US, Japanese and European FDI without them.

Concluding remarks

The US's best chance at getting better access to the world's fastest growing economies is on the table – it is called the Doha Round.

If the Obama Administration lets the Round slide into a coma, the next multilateral agreement will be closer to 2020 than 2013. If today's deadlock is bona fide – i.e. the US really cannot use systemic arguments to get the current package through Congress – then it will be equally real in 2013. The US will still demand deep, additional tariff cuts from China; China will still see no reason to concede. Think of 2013 as 2011 with much less goodwill internationally and poisonous politics inside the US. Breaking the deadlock will require a broader agenda but that would take years to agree and years to negotiate to fruition.

One reason the Obama Administration seems so blasé about failure of the Round is that it seems to think highly of its Plan B – the Trans-Pacific Partnership. Plan B, however, is based on wishful thinking and a misunderstanding of the nature of 21st century trade agreements.

- 21st century trade agreements create much less political economy “jealousy” and are thus much less “contagious” than the old-fashioned preferential tariff deals that seem to be in the minds of Obama's advisors.

Most of TPP's rules do not come with rules of origin; nations don't have to join TPP to benefit from it (this is what happened with the EU's Single Market Programme).

- Other Asia-Pacific nations have begun to suspect US motives when it comes to the TPP.

If TPP doesn't finish in 2011, US domestic problems will hinder TPP progress in 2012. By 2013, there may be other TPP-like arrangements in place – in addition to the deep bilaterals already signed by Japan and the EU. For this reason, a little delay now could completely ruin the TPP's domino effect. China won't join and Japan and Korea are hesitant. A TPP without Japan, Korea, and China misses the heart of Factory Asia. This is certainly not the sort of agreement that will force China and India to grant the US better market access than they are now offering in the Doha Round.

This is the corner in which the US may find itself in 2013. Completion of a multilateral Round may be years away, and the US's bilateral and regional options will be difficult to pursue for domestic and international reasons.

In the meantime, the US will continue to play catch up in the FTA game. The EU will continue to sign FTA with large Asian nations. It is likely to conclude one with Canada and it is considering an FTA with Japan like the one Switzerland has already signed.

At that point, the US's wishful thinking may be wishing it had made the compromises necessary to complete the Doha Round in 2011.

About the author

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