



CENTER FOR NATIONAL POLICY

**TRADE POLICY: FORGING A NEW CONSENSUS
A SERIES OF DISCUSSION PAPERS**

**CHALLENGES OF THE
NEW GLOBAL TRADING SYSTEM**

by
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About the Paper

This is one of a series of papers addressing U.S. trade policy from a political perspective.

It became evident during the 1990s that what once was a broad national consensus supporting U.S. efforts to liberalize world trade had eroded. In its place, an increasingly contentious and, to an extent, increasingly partisan debate emerged.

These papers look at this significant change, explore some of the factors associated with it, and consider policy implications for the future. The views expressed are solely those of the authors.

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Scher received his Bachelor of Arts degree from American University in 1983 and his Juris Doctor from American University's Washington College of Law in 1987.





Challenges of the New Global Trading System

By Peter L. Scher

American policymakers today are confronted with significant contradictions when it comes to international trade. On the one hand, the evidence that liberalized trade has brought significant benefits is clear. Americans now have vast choices among internationally produced goods and services, at better prices than ever before. International competition has stimulated major productivity gains, and new foreign markets have given momentum to technological innovation and capital investment.

At the same time, however, international trade has become a magnet for opposition from a broad spectrum of forces. Some of this opposition is organized under the umbrella of the "anti-globalization" movement, but much comes from more traditional and more mainstream Americans of varying interests. These include manufacturing and agricultural sector producers that have been sheltered thus far from the tariff reduction process, sectors and industries that perceive themselves to have been damaged by practices of U.S. trading partners, and of course, workers and their representatives who have either felt left out as the economy has grown, or, even worse, those whose jobs have been lost as a result of liberalization of the trading system.

The opposition comes at the end of a long string of negotiating achievements. Since the beginning of the modern world trading system in 1948, successive rounds of trade negotiations have eliminated almost all quotas and reduced the average global tariff from 40% in 1940 to 4% today. Trade has expanded fifteen fold, the world economy has grown six fold and per capita income worldwide has nearly tripled. Since 1960, worldwide tariffs have fallen by nearly ninety percent, while global trade has grown by a remarkable one thousand five hundred percent

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This massive increase in the flow of goods and services across international borders has been associated with strong growth in the world's economy. While some debate the direction or causality, it is indisputable that the second half of the 20th century witnessed both historic trade liberalization and phenomenal global growth. In particular, the economic

growth of the late 1990s, which represented the greatest expansion the United States had seen in a generation, was preceded by the adoption of two of the largest trade agreements in the history of the world, the North American Free Trade Agreement (NAFTA) (approved by Congress in 1993 and implemented in 1994) and the Uruguay Round Agreement which, among other things, established the WTO (approved by Congress in 1994 and implemented in 1995).

Economic statistics can often seem abstract. The human side of international trade is a lot more tangible. More important than worldwide growth and change in goods and services, in and of itself, has been the achievement of global gains in human well-being that have paralleled the growth in trade. Since the 1950s, world life expectancy has increased by twenty years, infant mortality has dropped by two-thirds, and famine has receded from all but the most remote, war-torn or misgoverned corners of the globe.

The clear role of an open trading system in contributing to efficiency, choice and growth in national economies led to the creation of the World Trade Organization in 1995. It was apparent to leaders in most countries around the world that the process of global trade had become central to the functioning of national economies. This dictated the development of a new international body to oversee the process, set rules, and adjudicate disputes. The WTO will continue to evolve over time to take account of different interests as well as the evolution of the world economy, but its establishment nonetheless represents the culmination of many decades of work to promote greater openness in international economic relations.

The achievements of the trade negotiating process over the past half century might at first make the current controversy over

its future in this century hard to understand. And yet, the opposition is real. Further progress today faces a significant array of obstacles, many of which were evident during the 2002 Congressional debate over granting new negotiating authority to the President, as well as the earlier Congressional debates over the approval of NAFTA and the Uruguay Round agreements.

If one considers how Congress reflects general popular support for trade, it is obvious that positive momentum has ground almost to a complete halt, dropping precipitously over the past fifteen years in particular.

It is worth noting, for example, that when Congress in 1988 reauthorized fast track negotiating authority for President Reagan, the United States House of Representatives voted 376 to 45 in favor of the new authority. Less than one month later, the United States Senate voted by 85 to 11 in support of the resolution. This represented 89% of the U.S. Congress approving efforts to expand trade.

Five years later, when President Clinton submitted the North American Free Trade Agreement (NAFTA) to the Congress for approval, the vote in the House of Representatives was 234 to 200. In the Senate, the vote was 61-38. This vote reflected 55% approval.

In the summer of 2002, when the Congress was voting to grant trade negotiating authority to President Bush, after failing on at least three occasions to approve new authority for President Clinton, the vote in the House of Representatives was 215 to 212, and in the Senate was 64 to 34 -- down to 53% of support in the U.S. Congress.

What exactly is going on here? There is no single answer to Congress' growing resistance to and the country's growing

ambivalence over further trade liberalization; a number of different factors have contributed, and must be addressed.

NEW COMPLEXITIES OF THE INTERNATIONAL TRADING SYSTEM

One of the greatest challenges facing the trading system, and as a result, affecting the effort to build broader and deeper support for that system, is its increasing complexity.

Traditionally, United States trade policy has had two missions: to reduce foreign barriers to American goods, and to ensure that foreign exporters more or less played fair with us. For years, our focus was on tariffs, principally tariff reductions. While the issues were politically difficult, we were essentially dealing with a narrow set of issues surrounding the importing and exporting of goods.

Over time, the issues dealt with in trade negotiations have become much more complex. We have come to recognize that because the world economy has become so broadly integrated, the domestic policies of our trading partners, and our own, can have significant impacts on the global trading system. We are no longer simply looking at trade between nations. Today, policy makers and negotiators are grappling with how countries' domestic policies and laws affect the global economy. Therefore, many of the fields taken up in the trade arena were outside its reach just a few years ago – intellectual property, electronic commerce, privacy, investment, food safety regulations, and of course, labor and environmental standards.

The past decade's debate in the United States over the inclusion of labor and environmental provisions in trade agreements represents a clear illustration of the new complexities of the global economy – and the challenges we face in developing a consensus

in the United States for further trade liberalization. In many respects the inability of the Congress and the President to come to terms with whether and how these issues should be addressed stalled a good part of the trade policy debate for nearly a decade.

While it has taken almost ten years, we seem finally to have come to a consensus that labor and environment issues can be directly relevant to the competitiveness of our companies and workers and to the global trading system, and therefore do have a place in trade agreements. The disagreement now is not *if* these provisions should be included, but *how*.

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A number organizations and policy makers argued for a long time that labor and environmental issues were sovereign, domestic concerns of our trading partners and, therefore, have no place in trade agreements. This opposition was not sustainable for a number of reasons.

First, our trade policies have historically recognized the relationship between labor and the environment and international commerce. A number of trade statutes and legislation have included labor and environment provisions,

including the Generalized System of Preferences (GSP), the African Growth and Opportunity Act, the Caribbean Basin Initiative, China PNTR, and even the “fast track” trade negotiating legislation of 1988.

Second, the reality of our trade policy has in fact focused on so-called domestic issues – whether domestic enforcement of intellectual property rights, or domestic enforcement of food safety standards. Our trade policy has long recognized that the domestic policies of our trading partners can often impact the competitive position of our companies. When China failed to enforce adequate intellectual property protection and permitted the piracy of American books, movies and CD’s, it became a very relevant trade issue, with wide support from Congress for tough action. When Europe blocks the importation of U.S. produced beef or food products made with genetically modified organisms, based on domestic environment or food safety standards, that too becomes a significant trade issue.

In fact, as a clear illustration of the evolution of the trading system, the trade relationship between the United States and the European Union, the largest and deepest trading relationship in the world, has become dominated by disputes over domestic regulation, whether it be food safety regulations, tax laws, regulations of noise pollution by U.S. produced aircraft, privacy regulations, or regulations addressing the environmental impacts of the production of computers and semiconductors.

Congress now appears to have accepted the idea that the way a country treats its domestic regulations, including labor and environmental standards, and its failure to enforce its own standards, can have a direct impact on the competitive position of U.S. companies and U.S. workers. Moreover, there has been a recognition that countries competing

with us in the global market place should not be permitted to use their environmental laws as a basis for blocking imports of U.S. or other foreign products, nor should they be permitted to lower their standards or fail to enforce their own laws as a way to gain a competitive advantage.

While it has taken us nearly a decade to reach agreement on the implications of labor and environmental issues in the global economy, Congress remains divided over exactly how this should be addressed. Many believe that whatever labor and environmental commitments are made in trade agreements should be treated and enforced like all other commitments. Specifically, if sanctions are permitted to enforce trade violations, such as infringement of intellectual property, then sanctions should be utilized for enforcement of labor and environmental commitments. Others believe that sanctions should not be used to enforce labor or environmental commitments.

The free trade agreement between the United States and Jordan offers one example of how to strike a reasonable balance in addressing relevant labor and environmental issues without infringing on the sovereign rights of either country. The U.S.-Jordan FTA recognizes the right of each country to establish its own level of domestic protection, and further establishes that each country will strive to ensure that its laws provide for high levels of labor and environmental protection. The obligation of each country is to enforce its own laws and prevent the relaxation of domestic laws in order to gain a competitive economic advantage. Enforcement, through sanctions or other means, is available if there is a pattern of non-compliance by either country.

Despite the progress of the last decade in developing a greater consensus on these issues, however, Congress likely will continue this debate about the extent to which labor and

environment and other so-called domestic issues should be included in trade agreements and, in particular, the appropriate enforcement mechanism for such provisions. As the United States Trade Representative works to complete and Congress begins to consider free trade agreements with various countries, including Chile, Singapore, Australia and the nations of Central America, the difficulty in building a broader consensus on the complex challenges of the new trading system, including labor and the environment among them, will be apparent and must be addressed.

TRADE DISLOCATION

A second obstacle we face in building broader support for further trade liberalization is the failure of policy makers to come to grips with the basic reality that there are winners and losers in international trade. When we create more open competition, there will be those sectors and industries that are unable to compete. Though the overall benefits can be great, there will be some job loss and dislocation. We have too often failed to be honest about these negative consequences of trade, and we have failed to provide significant relief to those who are impacted.

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Both sides tend to inflate the benefits and downsides of trade beyond recognition. The rhetoric on each side ratchets ever higher based on the tone of the other. During the NAFTA debate in 1993, we heard some of the proponents talk about NAFTA as the solution

to every economic, social and environmental problem. On the other side of the debate, we heard scare-mongering talk of a “giant sucking sound” pulling millions of jobs out of the United States and down to Mexico. As in most things, the truth is at neither extreme. NAFTA has been a success for the United States and its workers. Exports have increased, jobs have been created, and environmental programs that would not have existed without NAFTA have been put into place. At the same time, there has been increased competition for some U.S. industries and that competition has caused some job loss and dislocation.

Dr. Supachai Panitchpakdi, the new Director General of the World Trade Organization, published an article in the International Herald Tribune titled “*Open Markets, but look after the Losers of Globalization.*” In this article, Dr. Supachai stated, “...every government has the responsibility to implement programs that ensure that those not yet prepared for greater competition are looked after. Failure to take such action would only erode public support in the WTO and the global trading system.”

In Brazil, the landslide election of President elect Luiz Inacio Lula da Silva was a result, in part, of the view that millions of Brazilians have been left out of the economic progress that the country realized under the economic policies of President Cardoso – policies that included a strong commitment to the principles of free and open trade.

The point is that we need to deal honestly with the realities of the global trading system. Many of those who see the benefits of trade as overwhelmingly positive tend to assume that dislocation is more or less an inconvenience when balanced against the benefits of competition. It is as if they assume that fifty year-old farmers from North Dakota can pick up, sell their farms, and become HMO

administrators in Arizona. In fact, adjustment can be very difficult, particularly for the farmers and workers whose livelihoods are directly affected. Policymakers have not done an adequate job of addressing this and we will continue to face high obstacles to trade liberalization until they do.

This issue played out during the debate in the Congress over Trade Promotion Authority. Many of the leading proponents of new trade authority knew that critical to Congressional approval of this authority was an expansion of Trade Adjustment Assistance, or TAA. TAA was a program created in the early 1960s by a President and Congress who recognized the tremendous benefits trade liberalization would have for the country, but who also saw that with increased competition, some workers would inevitably lose out.

That means more difficult choices. This, in turn, means less ability to find creative trade-offs. And it means less time to set aside the difficult issues for another day.

Throughout the 1970s, 1980s and 1990s, as trade expanded, the commitment to those whose jobs were lost or transferred was often not there. Funding was inadequate, benefits were reduced, and inadequate resources were devoted to retraining and healthcare needs. In 2002, Congress reauthorized and expanded TAA, thus paving the way for renewal of negotiating authority for the President.

The clear lesson – the political reality – is that we will no longer get one without the other. Nor should we. For the United States as

a whole trade creates far more winners than losers. But we won't get more trade without honesty about the downside – and a meaningful means to address it. The American people deserve to have confidence that their leaders understand not only the benefits of free trade, but the downside consequences as well.

TOUGHER CHOICES

Another difficulty we face in advancing the trade agenda is that we have far less to offer, and the remaining political choices become more and more difficult with every passing year. The United States already has one of the most open markets in the world. In the past, we had the luxury of being able to push difficult items aside to be dealt with at some future date. This is particularly true in the area of agriculture, which will be central to the next round of world trade talks.

It is important to remember that prior to the completion of the Uruguay Round in 1993, there were no multilateral rules for dealing with agricultural trade, and even when agriculture was brought under the rules of the world trading system, there were many areas and many issues left off the table.

Now, as we get closer to actually dealing with many of these issues we have put off for so long, other countries are demanding a lot more and the United States has a lot less to give. That means more difficult choices. This, in turn means less ability to find creative trade-offs. And it means less time to set aside the difficult issues for another day. Many of the most protected industries in the United States recognize that while they have been successful in maintaining their protections for quite some time, the day of judgment may be coming soon, and they are fighting harder and harder to put that off as long as possible.

We will certainly see this played out in the Doha negotiations when talk turns to trade remedies, some of the more sensitive agricultural industries (sugar, dairy and citrus), and, of course, textiles. The challenge for our political leadership is that we will not achieve greater market access for our farmers, our service industries or manufacturing sector without addressing our own sheltered and politically sensitive industries. We will face some very difficult choices.

IS THE WORLD PREPARED TO MOVE?

The United States' trading partners must also be ready to make their own tough choices. When the United States has attempted to lead by example, we have often looked back only to see key players failing to follow.

Again, agriculture is a good example. When the U.S. Congress passed and President Clinton signed a new farm bill in 1995, the United States took a significant step towards a more market-oriented, less trade-distorting agricultural policy. A key premise of that decision was that the Uruguay Round had committed the countries of the world to move towards more open markets in agricultural trade.

Those negotiations were slated to begin in 1999. Europe was talking a great deal about expanding the Union to the east and instituting major reforms in the Common Agricultural Policy. The Cairns Group countries were actively promoting a more liberal set of world agricultural rules. When the WTO Ministerial in Seattle failed to launch those negotiations and U.S. policymakers saw key players in the European Union reject even modest reforms of the CAP, the attitude of many in the U.S. Congress as well as the agriculture community was that the United States should not unilaterally disarm.

The farm bill approved by the Congress and signed by the President in 2002 was one way of insisting that, until the rest of the world is prepared to move with us towards a more market-oriented policy, the United States will continue to support its farmers.

It is worthwhile to note that even with the recent expansion of farm supports, the United States is still within its WTO obligations and provides about one-third the level of support that Europe provides to its farmers. Moreover, while the United States has offered an aggressive proposal in the new Doha Round of world trade talks to reduce farm supports and eliminate all export subsidies, the European Union appears to have delayed fundamental reform of its agricultural programs for the near term and Japan has proposed to step back from the agricultural commitments it made in the Uruguay Round.

The lesson of all of this is that while the United States will continue to demonstrate leadership and a willingness to advance the broader interests of the world trading system, we will not unilaterally disarm from global economic competition. When the rest of the world is prepared to move, we will move with them, but until that time, we will exercise all our rights to defend our interests.

CONCLUSION

Success in this new world of trade negotiations will require sophistication, agility and honesty. We will have more success and less frustration if we are cognizant of the political constraints faced by our trading partners.

Developing countries, for example, are still faced with numerous market opening and reform obligations agreed to in 1994 during the Uruguay Round negotiations. While many developing countries lack the infrastructure and

capacity to fulfill many of these past obligations, we now are attempting to negotiate a whole new set of obligations as part of the Doha agenda. How realistic this may be, how capable these countries are in taking all of this on, remains a significant question in the global trading system. We should be wary of entering into trade agreements that impose obligations our trading partners are unlikely or unable to meet.

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While these issues are deliberated and other countries work to find their own way in the world trading system, the United States

must remain vigorous in pursuing its own economic and strategic interests through bilateral, regional and multilateral trade agreements.

As American policymakers and negotiators attempt to navigate this difficult terrain, they have a particular burden to demonstrate to the American people, first and foremost, the clear economic benefits of the trade agreements which we will enter – in particular, how these agreements address the real and often complex barriers our companies face in the marketplace. At the same time, trade negotiators and policy makers must set forth the potential risks and downsides to a particular agreement – what steps are we prepared to take to assist the workers and communities hurt by trade? It is only through this kind of open and balanced dialogue that the American people will regain confidence in our approach to the global trading system.