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ON FREE TRADE AND THE POST-AMERICAN WORLD

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Although *The Post-American World* was written before the 2008 crisis, Zakaria has since argued in a preface to the paperback edition that American profligacy would not have been possible without Chinese savings and holdings of US Treasury bills, both of which he claims in support of his thesis about the “rise of the rest.”¹

In the new preface, Zakaria offers further clues about where he believes Chinese – and global – trade policy could be headed. He observes that, although China is now being asked to finance both its own fiscal expansion and that of the United States, China does – as Stiglitz had observed – have a fallback plan, namely the stimulation of Chinese domestic consumption.² In 2009, my colleague Wang Jiangyu and I suggested that this fallback plan could increase China’s clout in trade negotiations because stimulating domestic consumption increases the significance of the Chinese domestic market, while at the same time reducing China’s export reliance.³

At heart, Zakaria’s theory is about how America must now learn to share economic power with the rest of the world.⁴ In this, his thesis tracks the consequences of European reconstruction in decades past, the subsequent rise of Germany and Japan, and that of the emerging BRIC (Brazil, Russia, India, China) economies, among others. Notwithstanding these developments, the General Agreement on Tariffs and Trade (GATT) had been a bicycle built for two, with the United States and the United Kingdom accounting for half of world trade in roughly equal proportions in 1947. Today, the US share has dropped to 16 percent.⁵ Finally, Zakaria emphasizes the continued importance of ensuring the vitality of the American economic worldview.⁶

The trends that Zakaria point to are not new. Indeed, amongst the small group of technical and diplomatic experts in the GATT/WTO and trade scholars (the “Gattologists”) whose professional preoccupation has been with global trade

negotiations, the decline of American power had been keenly observed and felt even before the demise of the Cold War. This chapter discusses the insights of the trade specialist against the legacy of American free trade. We need to assess where America stood after World War II, where it is today following a series of significant changes in the distribution of power within the GATT/WTO, and America's responses. Taking a trade policy perspective is useful because the "rise of the rest" is, first of all, an economic phenomenon; second, it was the GATT/WTO which first showed these signs of change; and, finally, it is in the GATT/WTO that we can already see and therefore assess America's reactions.

The decline of an American notion

America's most important intellectual contribution to free trade was the notion of world-wide most favored nation (MFN) treatment.⁷ During the interwar period, protectionism took the form of the US Smoot–Hawley Tariff. Originally designed to shield American farmers, this led to unprecedentedly high tariffs. Other nations retaliated in kind and global trade shrank. But with Roosevelt in the White House, the Reciprocal Trade Agreements Act of 1934 was passed and Secretary of State Cordell Hull threw himself into the task of bilateral negotiations with America's trading partners.⁸ The bilateral treaties he negotiated included an unconditional MFN clause.⁹ Hull then made this new standard of automatic non-discrimination the linchpin of another, larger idea – that of a world-wide organization to oversee the post-war global trading order. The idea behind the GATT was that, although world-wide tariffs would be brought down in successive "rounds" of negotiation, a multilateral MFN rule would "accelerate" the effect of such tariff reductions. Unconditional MFN treatment meant that a promise of lower tariffs made by GATT contracting party A to party B would become an automatic concession to all GATT contracting parties.¹⁰

By 1957, however, the European Economic Community (EEC) had been created. EEC countries were allowed to discriminate against nations that were not members of that customs union. America could not resist because of Cold War imperatives. EEC concessions to other EEC countries and to their former European colonies were tolerated despite doubts about their legality. At the same time, developing countries which did not benefit from European preferences complained of ensuing European discrimination. They sought and were also granted preferences by the United States in 1947 when the Johnson administration introduced the Generalized System of Preferences in order to avoid American isolation.¹¹ Viewing the loose way in which European discriminatory preferences had been accepted as lawful under the GATT, other regions too began to enter into their own preferential agreements – the Latin-American Free Trade Area was one such example.

Yet these developments did not threaten the GATT as much as America's own treaty behavior by concluding the Canada–US Free Trade Agreement (FTA) in 1989 under Reagan, and the North American Free Trade Agreement (NAFTA)

in 1994 during the Clinton administration. Others, such as the Association of Southeast Asian (ASEAN) nations, believed that they were witnessing the emergence of European and North American trade blocs, and reacted in similar fashion.¹² Under the Bush administration, Robert Zoellick went on to articulate America's policy of "competitive liberalization" – FTAs had become a favored alternative to WTO negotiations.¹³ The result is that, today, America's emulators in Asia threaten to draw a line across the Pacific, discriminate against America and others, and – together with the EU and NAFTA – create a world consisting of three trade blocs.¹⁴

The rise of the rest

Although global attention has mainly been drawn to China's 2001 WTO admission, China too has since launched its own FTA program, which is now shaping the formation of an East Asian trading bloc following the conclusion of the China–ASEAN FTA. At the same time, it has resisted European and American calls for "greater leadership" at the WTO. This is partly due to the onerous terms for China's WTO admission, which have taken their toll and dampened China's enthusiasm for the round.¹⁵

Its disappointment coincides with wider developing country disappointment with the WTO, especially in countries such as Brazil and India. The breakdown of trade talks at Cancun in 2003 indicated a new trend following the earlier failure to launch a new round in Seattle in 1999. Commentators attributed Cancun's failure to the emergence of the G20 developing country grouping (with Brazil, India, China, Argentina, and South Africa at its core) and the "radicalization" and "politicization" of the developing country members of the WTO. Again, in July 2008, trade talks collapsed over India's and the G33's¹⁶ insistence on a special safeguards mechanism to protect developing countries from import surges. In particular, India and the United States disagreed over the threshold required to trigger these special safeguards while attempts to blame China for siding with India were swiftly rebuffed.¹⁷

At a time when the global balance of economic power is shifting to Asia,¹⁸ the popular impression is that India alone or China's intransigence is each sufficient to thwart America's ability to deliver greater global trade liberalization, just as America lost its dominance over the GATT in the 1960s and 1970s. Zakaria says that America should now learn to act as an "honest broker," "engaging all the great powers" within such a "unipolar–multipolar" context ("one superpower, many powers").¹⁹ Yet the signs are that America itself will continue to pursue FTAs as an alternative to the WTO, at least in the medium term. Even if what America wants is simply to provide the threat of a credible alternative in order to get global talks moving, plan B (falling back on FTAs) now threatens to replace plan A (making the WTO work).²⁰ Speaking in 2009, Hillary Clinton explained that the United States remains "committed to the Doha Round, but

if that is not successful . . . then we want to work on a bilateral basis.”²¹ This is competitive liberalization at work, but is America exerting the kind of leadership Zakaria has in mind by turning its back on the WTO? In the meantime, others have followed suit. Where the Clinton administration once cited Europe as the reason for NAFTA,²² ASEAN then went on to cite NAFTA as the reason for having an ASEAN Free Trade Area,²³ whereas China, Korea, and Japan have chosen to emulate America and NAFTA by engaging in their own expansive FTA programs. In Australia, where the Howard administration had previously feared jeopardizing its trade relations with East Asian partners by entering into an FTA with the Bush administration, Canberra has been trying to play a leading role in Asia-Pacific trade regionalism.²⁴ In Brasilia, trade chief Celso Amorim recently confirmed that the “major players” are now insufficiently engaged in the Geneva talks thereby making a Brazil–EU deal more urgent.²⁵

Competitive liberalization means that MFN treatment is fast becoming the exception in the post-American world trading order.

A different future?

America has not always turned its back on the multilateral system when faced with the rise of the rest. The 1950s saw Japan’s GATT admission and the creation of the EEC. By the Kennedy Round (1964–1967), the United States was no longer the GATT’s sole driving force.²⁶ American notions of capitalism and the effectiveness of American trade law and policy abroad had come under threat. European-style welfare capitalism and the Japanese model of a corporate state were equally opposed to the American notion of limited state intervention barring market failure, and these differences became an increasing source of global trade friction.²⁷ By the early 1970s, Congress had started putting pressure on the executive branch in the form of Section 301 legislation, requiring the president to ensure that America gets a “fair” deal by attacking foreign trade barriers. Reagan used Section 301 against Japan in the semiconductor and later in the Motorola and procurement disputes in the 1980s and 1990s.²⁸ In response, Europe, Japan, and the developing countries turned to the WTO from the mid-1990s onwards and brought, or threatened to bring, their disputes with America to compulsory WTO litigation.²⁹ The Japanese scholar Keisuke Iida documents Japan’s success in finally curbing America’s Section 301 actions by simply invoking the threat of litigation during the auto dispute and Kodak–Fuji dispute of the 1990s.³⁰

America is now trying to off-set its declining influence in the WTO by negotiating bilateral deals with like-minded nations, but competitive liberalization too has its risks. A considerable part of that liberalization is occurring in tandem with Factory Asia’s new network of FTAs. Asia’s rising nations are liberalizing on their own where only a few decades ago many still had to be persuaded of the virtues of American-style free markets.³¹ America’s inclusion in such FTA networks is not yet given. Its exclusion would mean that its influence could

decline both in and outside the WTO. Similarly, its inability to realize a Free Trade Area of the Americas could mean that Brazil and the other Mercosur nations will turn to Europe.

Yet there are hopeful signs. The 2008 crisis witnessed a new form of multilateral cooperation in the form of the G20 Summit.³² The Obama administration has embraced the idea of a Trans-Pacific Partnership (TPP) which could avoid America being cut-off from East Asia.³³ The world has changed, again, since the days of US–Japan trade tensions in the 1980s and the transatlantic trade war of the 1990s. Protectionist pressures from import-competing producers are giving way to global supply chain manufacturing and production fragmentation, most notably in sectors like the electronics industry.³⁴ This means that American multinationals have a common interest with their European and global counterparts in pushing for greater trade liberalization, leading to the suggestion that future liberalization may become easier not harder.

America does however need to revitalize the WTO,³⁵ just as a fresh vision is required by the emergence of new supply-side concerns – related in part to the industrial rise of the rest – where the emphasis in the future will not be on blocking imports but on ensuring the supply of raw materials, food and energy from emerging economies as demonstrated by the recent dispute over Chinese export restrictions,³⁶ and the current resumption of the 2007–2008 food price crisis.³⁷ At the moment, there is still an opportunity to creatively engage other WTO members in shaping such a revitalized organization and ensuring America's legacy in global free trade.

Notes

- 1 Fareed Zakaria, *The Post-American World*, New York: W.W. Norton, 2009, pp. xix–xx.
- 2 Zakaria, op. cit., p. xxi.
- 3 C.L. Lim and Jiangyu Wang, "China and the Doha Development Agenda," *Journal of World Trade*, 44, 2010, p. 1309.
- 4 Others question whether American economic power is declining in relation to China; Joseph S. Nye, "A Turn for the Worse," *SCMP*, March 13, 2010.
- 5 Joost Pauwelyn, "New Trade Politics for the 21st Century," *Journal of International Economics*, 11, 2008, pp. 559, 562.
- 6 Pauwelyn, op. cit., pp. xxiii–iv.
- 7 The idea of MFN treatment in trade agreements has had a far longer history, and the unconditional form was originally favored by countries such as Great Britain whereas US treaties adopted unconditional MFN treatment only from 1923 onwards; *Most-Favoured-Nation Treatment*, UNCTAD Series on Issues in International Investment Agreements, New York: UN, 1999, 13; A. McNair, *Law of Treaties*, Oxford: Clarendon, 1961, pp. 274–8.
- 8 Kenneth Dam, *Cordell Hull, the Reciprocal Trade Agreement Act and the WTO*, John M. Olin Law & Economy Working Paper No. 228, Chicago Working Paper Series, October 2004.
- 9 Before 1923, non-discriminatory treatment of an American trade treaty partner was not automatic but was usually made conditional on reciprocal concessions.
- 10 Dam, op. cit.

- 11 Note, "United States Preferences: The Proposed System," *Journal of World Trade*, 8, 1974, p. 216.
- 12 See further, C.L. Lim, "A Mega Jumbo-Jet: South-East Asia's Experiments with Trade and Investment Liberalization," in *The New International Architecture in Trade & Investment*, Singapore: APEC, 2007, p. 115.
- 13 Robert Zoellick, "Our Credo: Free Trade and Competition," *Wall Street Journal*, 10 July 2003; C. Fred Bergsten, "A Competitive Approach to Free Trade," *Financial Times*, December 4, 2002.
- 14 Fred Bergsten, "Plan B for World Trade: Go Regional," *Financial Times*, August 16, 2006. See further, C.L. Lim "Who's Afraid of Asian Trade Regionalism, and Why?," in R. Buckley, R. Hu and D. Arner, eds., *East Asian Economic Integration: Law, Trade and Finance*, Cheltenham: Edward Elgar, 2011 (in press).
- 15 Lim and Wang, op. cit.
- 16 A developing country grouping of import sensitive nations.
- 17 "China's Top Official: Don't Abandon the Doha Round," *Business Week*, September 15, 2008.
- 18 "East or Famine: The Balance of Economic Power," *The Economist*, February 27, 2010, p. 71.
- 19 Zakaria, op. cit., pp. 233, pp. 241–2.
- 20 Sungjoon Cho, "'Plan B' is Always Inferior to 'Plan A'," *Financial Times*, London, August 22, 2006.
- 21 Quoted in "Time for Parallel and Alternative Paths," *Bridges*, 13, 3, July–August 2009, 1, at 2.
- 22 Speech by President William Jefferson Clinton, White House Press Release, 14 September 1993.
- 23 Rudolfo Severino, *Southeast Asia in Search of an ASEAN Community*, Singapore: ISEAS, 2006, p. 223.
- 24 Ann Capling, *All the Way with the USA*, Sydney: University of New South Wales, 2005, pp. 40–6.
- 25 "Time for Parallel and Alternative Paths," op. cit.
- 26 Raj Bhala, *International Trade Law*, 3rd edn, Newark, NJ: LexisNexis, 2008, p. 21. Hudec traced the decline of US dominance to the 1970s and the Tokyo Round negotiations instead; Robert Hudec, *Developing Countries in the GATT Legal System*, London: Gower, 1987, p. 72.
- 27 Sylvia Ostry, *The Post-Cold War Trading System*, Chicago: University of Chicago, 1997.
- 28 Keisuke Iida, *Legalization and Japan*, London: Cameron May, 2006, p. 50.
- 29 Karl F. Falkenberg, "The European Union's Position in the Uruguay Round Negotiations," in Stratos V. Konstadinidis, ed., *The Legal Regulation of the European Community's External Relations after the Completion of the Internal Market*, Aldershot: Dartmouth, 1996, p. 63, at pp. 64–5; Iida, op. cit., p. 50.
- 30 Iida, op. cit., pp. 67–130.
- 31 *The Economist*, "The Noodle Bowl," September 5, 2009; *Time Magazine*, "Bloc Party," September 21, 2009.
- 32 Simon Evenett, "Towards a Meaningful Trade Policy Agenda for the G20 in 2010," *ARTNET*, Policy Brief No. 24, February 2010.
- 33 At the time of writing, the TPP talks involve Singapore, New Zealand, Chile, Brunei, Australia, Vietnam, Peru, the United States, and Malaysia. Japan and Canada are currently contemplating their participation in the TPP.
- 34 See, for example, Gijsbert van Liemt, *Subcontracting in Electronics, Sectoral Activities Programme*, Working Paper No. 249, Geneva: ILO, 2007.
- 35 Pauwelyn, op. cit., pp. 567–8. One might ask if conclusion of the Doha round might amount to "too little, too late", as opposed to the view that multilateralism and regionalism ebb and flow, and that periods of increased regionalism are inversely

correlated to the rise and fall of progress in tariff and trade liberalization at the multilateral level. Whatever the answer to this, it seems that, to survive, the WTO must nonetheless conclude the Doha Round as a basic necessity. For a first rate, accessible account of the Doha Round, see Paul Blustein, *Misadventures of the Most Favoured Nations*, New York: PublicAffairs, 2009.

- 36 WT/DS394/395/1, June 25, 2009 (Consultations). The European Communities is currently proposing a new "WTO Agreement on Export Taxes" which could have a bearing on the issue of energy exports/shortages and the food price crisis by seeking to eliminate developed country export taxes, and regulate developing country export taxes as these tend to affect commodity prices; TN/MA/W/11/Add.6, April 27, 2006; "DDA: Third Submission by the EC on Market Access for Non-Agricultural Products," European Commission, Ref. 143/03 REV. 2, March 31, 2003.
- 37 Vivienne Walt, "The World's Growing Food-Price Crisis," *Time Magazine*, February 27, 2008; Gregory Meyer, Javier Blas, and Jack Farchy, "World Closer to Food Price Shock," *Financial Times*, January 13, 2011.