

FREE TRADE AND THE FUTURE

From CAFTA to NAFTA, it's easy to be pessimistic (or optimistic) about trade

On Jan. 27, 2006, a panel of experts was assembled by *The New Republic* to debate and discuss what lies ahead for free trade. As many markets continue to adjust to the Central American Free Trade Agreement, the World Trade Organization has found itself hobbled by disputes between developed countries and those that are developing. And, as trade continues to grow and business scrambles to cash in on growing overseas markets, what impact does that bear on America's trade balance? The following is an edited transcript:

JEREMY KAHN: At the current moment the future of free trade appears to face equal amounts of promise and peril. In many respects these are great times for free trade. In absolute terms, the flow of goods and services across borders has never been greater, and that's true in both the developed and the developing world.

Trade has helped lift entire nations out of poverty in that it has helped create middle-class jobs that never existed before. It also has transformed the politics of many nations, mostly for the better. But the politics of trade remain highly contentious, and here is where we can see some of the down-sides of trade.

In this country, the bipartisan consensus for free trade that once existed as recently as a decade ago has, if not collapsed, at least been severely strained. This is particularly true within the Democratic Party, where there is now a lot of debate about extending

THE PANEL

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free-trade agreements, which wasn't necessarily true as recently as the mid-'90s. You can see this in the debate at how closely [the Central American Free Trade Agreement] came to not passing, and you also can see it in the fact that there is quite a lot of speculation that the president may not have his fast-track authority on trade agreements renewed when it expires in 2007.

Abroad, trade also is in peril politically in South America. The neo-liberal economic ideas, including free trade, are certainly being questioned as never before. There was quite a revolt at the Summit of the Americas over the United States' push for a free-trade area of the Americas.

[The World Trade Organization] has been hobbled by disputes between the developed

and the developing world over agriculture, among other things, and it also has become a locus for protest against globalization generally, although there is some good news on this front in that these protests seem to be waning over time.

So these are some of the issues that are being faced right now in this trade environment. Let's start with Sean.

SEAN RANDOLPH: My organization, the Bay Area Economic Forum, is supported by employers and local government and universities and others here in the [San Francisco] Bay Area, and we focus on what makes the economy here competitive, looking at big, long-range issues. And international trade — [and] I think globalization in all of its aspects — is certainly one of those. You could probably make a case that after New York, the Bay Area's economy — and here we're talking about San Francisco, Oakland and the East Bay, including San Jose and Silicon Valley — is perhaps the most globalized regional economy in the country when you look at its trade [and] foreign investment patterns.

The interest of Bay Area companies in what happens in global markets is growing. It's not limited to big companies. A lot of small companies are invested and impacted by this. [International agreements] that have a global impact or have an Asian focus are probably going to have a lot more importance at the end of the day to us here than agreements made in other parts of the world.

MODERATOR: Thanks, Sean. Andrew?

ANDREW ROSE: It's really easy to be pessimistic about the future of free trade, but also it's real easy to be optimistic too. The most striking fact that no one disputes is that trade has grown faster than income; trade always grows faster than income. Countries seem to be engaged in more and more trade every year, and there is no reason to doubt that that wouldn't continue. We don't seem to need the WTO or the [General Agreement on Tariffs and Trade] to

engage in multilateral trade liberalization; it just seems to do it on its own. The legal limits on tariff rates are much higher than the actual tariffs applied. We give out “most favored nation” tariff status almost freely to everyone in the world. We don’t have to, we just do, and we’re not unusual.

So you don’t seem to need a multilateral round or a multilateral organization to liberalize a lot of trade. You could say, “O K, so we waste a huge amount of money by giving it to a corrupt group of large agribusiness interests, but who cares? They’re really small in the economy.”

[As for] regional trade agreements, you might say it’s better to have some freer trade than none. And who cares about the mindset? Who cares about the lack of protesters? Trade continues to grow. That’s good for consumers; it’s good for businesses. Trade will continue to grow because countries realize it’s in their own best interest, and act that way.

MODERATOR: Thanks, Andrew. Glynn?

GLYNN WOOD: The Indian government has come through what is truly a revolution since the time that I was first assigned there in the 1960s. At that point, India was very concerned about something called “the brain drain.” They realized that a lot of bright Indians were taking off for the United States and Europe, and this was damaging their economy greatly, and they were on their way to what people called Nehruvian Socialism.

At the same time, Indian business was out-producing the government sectors that were put up in terms of productivity, even under the rather severe controls of the so-called socialistic government. Since 1991, India has liberalized, and they’ve had all the same problems that Jeremy has mentioned, as far as the United States is concerned. The Congress Party can’t help but going back to an occasional Nehruvian slogan. Anti-colonialism still gets an audience from time to time.

No one has anti-English riots anymore because English is being promoted as India’s major asset in the world market as it competes with China for the kinds of investments that might come from abroad.

MODERATOR: Thanks, Glynn. I’m curious,

Sean or Glynn, if you could respond. Andrew sort of posited that, in essence, the WTO doesn’t necessarily matter because trade is going to expand anyway, and liberalization happens best when countries realize it’s in their own interest to lower tariff barriers, and not when they’re forced to by some sort of bilateral or multilateral agreement. So I’m curious what you think. Do you think the WTO really matters? And, Sean, you have two businesses in the Bay Area. Are they particularly concerned about progress from the WTO, or does it not really play into their thinking?

RANDOLPH: Well, there may be more than one answer to that. I’m not sure that businesses, except for maybe a handful here or anywhere, follow the WTO negotiations all that closely. It’s rather broad, and I believe

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for many of them, [the negotiations are] rather abstract, and [are] very drawn out, and may be a little bit more difficult to get their hands around than a bilateral or regional negotiation. Even at that, I don’t believe they’re as invested as they could or probably should be in the process of the negotiations.

Does it matter what happens? Well, I think specific companies are affected in very specific ways depending on their line of business. If they’re in the technology business, the international technology agreement we had a few years ago is very beneficial to them. If you’re an agricultural exporter of certain kinds of products, it’s important to you.

But I believe, in general, [that] there probably isn’t as great a degree of engagement as there should be by businesses at any level. And does it matter? I’m sort of biased in thinking that it does matter. I believe countries have shown again and again that unilateral liberalization works, and it works just fine. And of course Mexico did it, as we’ve heard. Chile did that; they

didn’t wait for anybody else. And those countries that have done that have come out ahead of the rest of the pack. I believe it is in our interest, if we can, to have a uniform set of rules and a more predictable, transparent environment.

MODERATOR: Glynn, what do you think?

WOOD: I’m with Sean on that. It continues to bring up the very serious issues of distortions. Eventually it still comes back to the United States negotiating with China about intellectual rights. Having a template out there, though, to place where we are at a particular time on any rule is not a bad thing, and makes that kind of activity worthwhile.

MODERATOR: Andrew, did you want to respond?

ROSE: Let me just clarify my views. I’m extremely unpopular in certain areas of Geneva as a result of my research on this, but I would be completely in favor of the WTO doing what it’s supposed to do. I’m a big free trader, completely unambiguous, but the WTO was sort of designed to fail in almost all of its functions.

For instance, these rounds require unanimity. Well, that sounds like Corruption City, right? You know, every single player has to buy into a round, and that is not a recipe for success. So it would be great if the WTO were more effective, [but] they just aren’t very effective.

But having said that, there are at least two other things that the WTO does do, to some effect. One is a little bit ambiguous. It serves the same role in international trade as the International Monetary Fund does in macroeconomic policy, which is it’s the focus of anger, and that’s great. So you hate free trade, you blame it on the WTO, you blame it on some bureaucrats who are faceless who are sitting across the ocean. And that’s actually a useful function, right? You don’t blame your own politicians; you blame it on some foreigners, and that is of some value.

The other thing is that the dispute resolution system is working. Now, it doesn’t really affect much trade, but I will say when there is a dispute between countries, having the equivalent of a court of law to go to whose

verdicts are adhered to is important. And that's a big deal for the United States, so we have one for [the North American Free Trade Agreement]. And we have a big dispute with Canada — or rather Canada has a big dispute with the United States — over timber, and the NAFTA tribunal came back and unambiguously said the United States was at fault. [The United States] just said, screw that, and is ignoring it. [The United States doesn't] do that for the WTO, and that is of value for a small number of fractious cases.

MODERATOR: One of the things that came up at one of these other panels that we had when we were talking about the WTO was whether it was designed to fail. One of our other panelists postulated that maybe it was time to get rid of the grand round concept, that the entire idea that trade had to proceed in these great leaps where vast sectors were liberalized altogether was problematic. I was wondering, Andrew, what you think of that idea?

ROSE: I think it's a good idea. My view is that the WTO is, by its very nature, just not going to work, and as more and more countries come in, it's going to be more and more difficult. I believe we should ignore it, and I believe a bunch of countries should ignore it, in the same way that the U.N. General Assembly used to be an important institution and is just not anymore, because you require a large number of people that you don't really care about and who aren't acting appropriately, meaning they're not acting in the interests of their own citizens.

So I personally would be happy if all the rich industrialized countries got together with Brazil, Russia, India and China, and did a small, more focused, more effective trade liberalization. And other countries are happy to buy in. You know, they can do it, but if you want to impoverish your own country by keeping your protectionist barriers up, that's fine, but don't stop progress elsewhere.

So something like that — the equivalent of the Security Council instead of the General Assembly — seems like a good way forward to me.

WOOD: I believe the general rule of "large numbers do not make for great decisions"

certainly is there. It's not just in world trade — it's with almost any other organization that starts out being a very activist organization, and later finds that arriving at the consensus either means that you sort of farm it out to a player or two, or you end up not doing anything.

RANDOLPH: I think it's true that there has been a big change in the negotiating environment since the GATT was first set up. If I remember the numbers right, when the GATT first started there were something like 30 members, and I think now there is something like 148 — maybe it's 150 members now — in the WTO. So that really makes a much more complicated negotiating environment, especially where in the early days the tune was for better, or for worse, being called by a small number of very major economies, and the smaller ones kind of

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weren't along for the ride, but it was a simpler process relatively.

So, yes, with almost 150 countries at the table it's gotten a lot more complicated, not to mention the complexity of some of the issues. We're not just talking about terrorists anymore; we're talking about government procurement and intellectual property and services, and all of that.

But, I believe, at the end of the day the bottom line is probably, well, what works? What's going to produce the most bang for the buck, the most liberalization for the effort? And it's probably the countries that decide not to participate, for whatever reasons, that will benefit the least. They're probably more likely to fall behind those that do step forward to open things up.

MODERATOR: Glynn talked about India, which I think is very interesting. I know there are a lot of technology firms that are doing business with India, and India is emerging as a very important market for trade. Can you comment on what role you think India is going to play in liberalization?

RANDOLPH: I will defer to Glynn on the question of India's role in trade negotiations, but in terms of the Bay Area, it's an interesting question. The amount of trade we do with India right now is very, very small compared to any major economy. However, it's growing very fast, and so if you project current trends over the next five or 10 years, it starts to really show up, I think. I believe the impact, though, is more than just trade — it's more the flow of human capital.

However, since 9/11, for a whole variety of reasons, it's harder to get visas to come here. We've been more discouraging of foreigners coming to study at our universities, and there are more business opportunities for people from China and India in their own countries, and their universities are getting better. And so we're actually seeing people who came here in the '90s — and before — going back to India. They're starting up businesses. And actually, that can be a good thing for us, because when they leave here, they don't often leave altogether. They have roots here, they may have a shop here or an anchor here, and they become essentially bi-national businesspeople, going back and forth. So I think in terms of our global connections and our ability to take advantage of assets in India and vice versa, that's something we're going to benefit from.

WOOD: The notion of roots on both sides is quite important. The students that I helped fill out forms for — not for American government grants, but for Caltech and Chicago and MIT — have grandchildren here now, even if they have gone back to live in a more pleasant place called Bangalore, which often is the case. And it's not always for retirement. Again, some of them are going back and doing start-ups inside India.

MODERATOR: There has been a huge push by U.S. companies to get into China, and there is a tremendous flow of goods from China into the United States, and yet politically it's a highly charged subject because there always is this feeling that we're being unfairly undercut by this sort of very cheap labor, or that the environmental and labor standards in China aren't the same as here, and therefore somehow this trade is unfair. Sean, in this region, what are you seeing companies do vis-à-vis China, and how do they feel about trade with China? Do com-

panies feel like they're getting a good deal out of this transaction, or do they just feel like they have to be there because they're afraid not to be?

RANDOLPH: Oh, I think it's a mix of things, but I think China is the easiest place to talk about when they talk to businesses here. If you have a forum on China, you're [probably] going to have a good turnout. It's something that turns out a crowd because there's really a very heightened level of interest in what's going on because people see the opportunities.

A lot of our major companies, of course, are heavily invested there. They are seeing the opportunity for certain kinds of lower-cost manufacturing where the labor costs are very low and the quality of production is going up. It's quite good now.

ROSE: The issue of China is a really straightforward one, which is, it's always easier to blame foreigners than it is to take the blame yourself for domestic policy failures. And the issue of China has emerged basically because of two completely American-specific issues, which are the fiscal deficit that the Bush tax cuts and the spending increases have created, and the enormous housing bubble.

So American savings has just disappeared, and of course we're sucking in imports. We happen to suck them in from China, and it's always easier to blame the foreigners than it is to sort of say it's our problem, and it is an American-specific problem. The solution is not going to come from China; the solution has to come from increased savings in the United States, either from the public sector or the private sector.

RANDOLPH: It's true. I think for 2005, it's probably going to come in that the U.S. savings rate was zero, and maybe actually slightly negative. What has happened, I believe, is a lot of the trade surplus that other countries — like Taiwan — used to have with us has been diverted to China. A lot of Taiwanese manufacturing and Japanese manufacturing is now being done in China, so it shows up as a Chinese export, whereas, in fact, some of that is displaced exports that would have come from other countries before.

I have never been a huge fan of using exchange rate policy or blaming exchange rate policy on trade imbalances, although it, of course, has an effect. If the Chinese really significantly revalued the currency and did pretty close to what we were asking in terms of the scale of the reevaluation, it wouldn't have a huge effect on the trade balance.

Some companies, of course, would benefit more than others, but at the end of the day, China — even with all of its growth in exports — is not that big a part of our total import picture. As long as we continued to be consumers on the scale that we are, we would still continue to suck in exports at about the same level, if not from China, then from other places.

(Moderator turns to the audience for questions)

Andrew Rose:

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QUESTION: Many of us thought that free trade would lead to legal, social and political liberalization in some of these countries, and I'm hopeful that will happen, but I look at China and Russia, and I'm not sure that is going to happen. I'm wondering if the panelists can address that and whether they believe there is hope.

ROSE: There is very little economic support for that. You sometimes hear that and it just doesn't seem to be backed up by the data. I guess the easiest way to think about it is Latin America. Some areas of Latin America have liberalized a lot more and you don't seem to see a consistent pattern in the respect for human rights, which is measured often, or the democratization. And certainly East Asia was opening up like crazy when they also were staying relatively autocratic states.

Singapore is really open right now, and it's a benevolent dictatorship. Hong Kong is, of course, open to the Chinese.

RANDOLPH: I think if you go to China today,

obviously the government is loath to open up more than marginally, say, at the village level, and they are trying as hard as they can to control what comes through the Internet in certain categories, and they have got their hands into lots of stuff.

But if you just walk around the streets and talk to people, it's a flying economy. And so if you look at it from the standpoint of most Chinese, their income is going way up, their quality of life is going way up, their lifestyle is going way up. I think [there's] hope.

QUESTION: Could I get a comment on how you feel the future will be with CAFTA?

RANDOLPH: At a macro-regional level it doesn't have a whole lot of impact. It may have more political significance in terms of the relationships and the connections between those economies and those countries and the [United States].

We have got a significant number of Central Americans here, in addition to those from Mexico, and for them and some of their businesses, which might be micro-level businesses, [CAFTA] probably makes a difference, but I think on the scale of things, at least in this area, it's pretty small. I suspect if you were in Miami or Texas, maybe it would be a different story.

MODERATOR: I want to thank you all for coming. It's been a very good discussion, and I would like to thank our panelists again.

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