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US can’t afford another decade without new free trade agreements

Clark Packard

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As 2022 winds down, it is worth noting that it has now been 10 years since the United States entered into a free trade agreement (FTA) with new trading partners. Despite claims that the United States is a “hyperglobalist,” the reality is much different. In fact, as Adam Posen of the Peterson Institute for international economics noted in his excellent *Foreign Affairs* essay last year, the United States has been withdrawing from international economic integration for about 20 years. The consequences of a stagnant trade agenda will become more apparent and pronounced as time passes.

In 2012, U.S. FTAs with Korea, Colombia, and Panama, respectively, entered into force. Since that time, new liberalization has become non-existent. Though several mistakes were made along the way, the Obama administration at least tried to pursue an ambitious negotiating agenda. Most notably, it negotiated the Trans-Pacific Partnership (TPP) with a number of Pacific Rim nations, an increasingly vital part of the world both economically and strategically. Once the Trump administration entered into office, it immediately withdrew from the promising pact – an enormous unforced error. After the United States withdrew from TPP, the remaining members consummated the agreement and renamed it the Comprehensive and Progressive Trans-Pacific Partnership (CPTPP).

Meanwhile, the Trump administration’s oversaw a disastrous trade agenda: aside from withdrawing from TPP, it imposed bogus “national security” tariffs on steel and aluminum imported from virtually every country in the world, including longstanding military allies, which raised prices, hurt manufacturing, and alienated trading partners; engaged in a reckless trade war with China, which imposed enormous costs on the economy while failing to discipline the legitimate challenges posed by Beijing’s international economic practices; and rewrote the North American Free Trade Agreement (NAFTA) in a more protectionist direction.

Today, the Biden administration has shown no interest in liberalization. While the U.S. dithers – the United States Trade Representative (USTR) Katherine Tai recently called FTAs a “very 20th century tool,” a stunning admission from the head of the agency tasked with tearing down trade barriers around the globe – the rest of the world clearly is moving on.

Whereas once the United States used its dominant position in the global economy to liberalize trade, create vital institutions and rules like the General Agreement on Tariffs and Trade (GATT) and its successor the World Trade Organization (WTO), it is now clearly retreating from further international economic leadership. Others are filling the void. China, Taiwan, post-Brexit United Kingdom, and Ecuador have all recently applied to join the CPTPP. Likewise, the Beijing-led Regional Comprehensive Economic Partnership (RCEP) has gone into effect. The WTO’s maintains a database of regional trade agreements entered into by various WTO members. Indeed, a cursory glance confirms a massive proliferation of such agreements over the last 20 years.

To be clear, regional free trade agreements are not costless. They promote what economists call “trade diversion”, which occurs when trade is diverted from a more efficient exporter to a less efficient exporter simply by the creation of a preferential (or discriminatory) free trade agreement or customs union –what the famed trade economist Dr. Jagdish Bhagwati called “termites in the trading system.” Still, these agreements are preferable to no liberalization at all.

Over the years, Cato scholars have argued U.S. policymakers should simply unilaterally eliminate trade barriers irrespective of what other countries do. If that is politically impossible, then the U.S. and countries around the world should negotiate multilateral agreements within the WTO system so the basic non-discrimination principle applies between all members.

Since the Doha Round effectively collapsed in 2008–2009, widespread liberalization within the WTO system has been dormant. The WTO system is plagued by a requirement that multilateral liberalization be unanimous, which has proven to a major hurdle.

Another avenue for liberalization is through plurilateral negotiations through the WTO system – that is, agreements with some, but not all, WTO members. As my Cato colleague and former chief judge of the WTO’s Appellate Body, the highest court of world trade, has written , plurilaterals offer the best way forward for liberalization within the WTO system.

There are ongoing plurilateral negotiations over trade in so-called “green goods”—such as wind turbines, solar water heaters, etc.—as well as digital trade. Still, these negotiations have been slow. That leaves free trade agreements, both regional and bilateral, outside of the WTO system as the only active way to cut trade barriers. In the past, U.S. pursuit of regional and bilateral free trade agreements has prompted action within the WTO system. For example, NAFTA helped spur action to complete the Uruguay Round, which converted the GATT into the WTO system.

As Posen noted last year, the U.S. trade-to-GDP ratio has risen more slowly than the global average – increasing from 20%. in 1990 to 30% in 2008—and “[i]t fell at the same rate as the world at large’s during the financial crisis, but it has yet to recover.” Posen argues it’s natural for the U.S. to have a lower trade-to-GDP ratio than much of the world given its large, diverse economy separated by major oceans, but it should be liberalizing at roughly the same rate as the rest of the world, which it is not.

So, what are the long term consequences of an atrophying trade agenda? First, U.S. consumers will pay more for goods and services than they would otherwise. Likewise, despite the pervasive myth, a non-existent trade agenda will lower real wages since increased trade tends to promote specialization and enhance productivity. Over time, it will mean a less innovative and dynamic ecosystem for existing firms who are shielded from foreign competition. Next, U.S. firms will lose access to markets abroad since they will face higher trade—both tariff and non-tariff—barriers and competitors in other parts of the world with more free trade agreements meet those demands.

In less concrete terms but arguably just as important, the U.S. will lose a vital tool of soft power to set standards around the world in emerging areas vital for the 21st century economy. Near-peer competitors like China will surely fill the void.

Finally, the U.S. will forfeit the prestige and respect it earned after World War II when policymakers wisely leveraged America's status as the world's lone super power to create the modern trading system that exists today, which has paid enormous dividends both economically and strategically. Indeed, as Gary Hufbauer and Zhiyao Lu of the Peterson Institute noted in a 2017 study, "the payoff to the United States from trade expansion—stemming from policy liberalization and improved transportation and communications technology—from 1950 to 2016 is roughly 2.1 trillion (measured in 2016 dollars). It further concludes that U.S. GDP per capita and GDP per household accordingly increased by $7,014 and $18,131 respectively (both measured in 2016 dollars."

Still, Hufbauer and Lu note, "liberalization still has a long way to go; the potential gains from future policy liberalization could be as large as $540 billion for the United States by the year 2025," which would translate into an additional increase in GDP per capita of about $1700 and $4,400 in GDP per capita."

Simply put, we cannot afford another decade of a decaying trade agenda.

Clark Packard is a research fellow in the Herbert A. Stiefel Center for Trade Policy Studies.