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To Expand Commerce And Grow The Economy, Trade Freely With Europe

By: Doug Bandow – January 7th, 2012

Recessions bring out the worst in people. The search for economic scapegoats almost always turns to trade. People want to pull up the drawbridge to imports, further reducing growth around the world.

Americans have benefited greatly from the increasingly globalized economy. Yet trade growth, which fueled years of global economic expansion, has slowed. David Smick, publisher of *The International Economy*, warned of the potential crack-up of "the globalization model of the past thirty years."

Protectionist pressures are growing. Robert Merry of the *National Interest*worried: "History tells us that such beggar-thy-neighbor initiatives can lead to currency wars, trade wars and increasingly tense relations among nations intent on preserving their edge in world trade."

That is a losing game for all concerned. Washington needs to raze, not raise, trade barriers. In fact, the U.S. would benefit from unilateral free trade. Government should simply get out of the way, allowing Americans to purchase the best products at the best prices wherever they are made. Unfortunately, that's a political nonstarter.

The next best approach is global trade liberalization. Various negotiations through GATT and more recently the World Trade Organization have greatly liberalized the international marketplace. But the WTO's Doha round, launched in 2001, has stalled. Only the formal funeral has yet to be held.

With these two avenues closed, regional and bilateral free trade agreements are the best vehicles to liberalize commerce. Such accords expand trade, though at a risk of balkanizing the globe. Nor are these treaties political slam-dunks. The Bush administration negotiated agreements with Panama, a small nation with little impact on the American market; Colombia, a nation ravaged by the U.S.-led drug war; and South Korea, a military ally which now trades more with China than with America. Nevertheless, congressional opposition was strong and President Barack Obama renegotiated all three, limiting their benefits, before supporting their ratification.

Still, the administration now appears committed to expanding export markets. Washington is pushing a Trans-Pacific Partnership to encompass the Asia-

Pacific and the Americas. However, Washington wants to exclude China, and the new Japanese government, beholden to domestic protectionist interests, remains skeptical. The obstacles to agreement are many, and an accord lacking the region's biggest two economies would be of limited value.

Europe may provide a better opportunity. The continent constitutes the largest economic unit on earth, bigger even than America. Moreover, residents in both the U.S. and European Union are, on average, significantly richer than those in China, giving them more spendable cash available to purchase imports.

Reducing trade barriers would benefit both sides. Total transatlantic trade and investment in 2009 ran $4.4 trillion. The U.S. and EU then accounted for roughly three-quarters of the globe's financial markets, half of the globe's GDP, and nearly one-third of the globe's trade. With annual trade running about one trillion dollars, even a small boost would be significant. Argued Brian Beary of Europolitics: "The case transatlanticists can make is that in addition to Europe and the U.S. being more aligned politically and economically than any other part of the world, an EU-US FTA will provide the biggest bang for their respective buck."

The Obama administration has talked about the "Transatlantic Partnership," which deals as much if not more with geopolitics than economics. But Secretary of State Hillary Clinton admitted that "the U.S. remains one of only a handful of WTO members not to move beyond most favored nation status with the EU. We need to do better."

The U.S. and EU created the Transatlantic Economic Council in 2007 to promote increased commercial cooperation. However, not much has been achieved. It is time to negotiate a transatlantic Free Trade Agreement.

In fact, the EU, though a bureaucratic monster at home, has been pushing free trade agreements abroad. The EU implemented one with South Korea, recently concluded one with Singapore, is negotiating another with Canada, and has begun talks with Tokyo over a free trade pact.

EU Trade Commissioner Karel De Gucht observed that "There is now, for the first time in years, a serious drive towards an EU-U.S. free-trade agreement." Moreover, with the United Kingdom currently presiding over the G-8, made up of the world's wealthiest nations, British Prime Minister David Cameron said an agreement would be one of his objectives this year: "perhaps the single biggest prize of all would be the beginning of negotiations on an EU-U.S. trade agreement."

The November 2011 U.S.-EU summit led to creation of a High Level Working Group on Jobs and Growth, which released a preliminary report last June. (The final report is expected later in January.) The committee declared: "a comprehensive agreement that addresses a broad range of bilateral trade and investment policies as well as issues of common concern with respect to third countries would, if achievable, provide the most significant benefit of the various options we have considered. A comprehensive agreement could include ambitious reciprocal market opening in goods, services, and investment, and address the challenges of modernizing trade rules and enhancing the compatibility of regulatory regimes."

The potential gains from a transatlantic accord are large. Wrote Daniel Hamilton of the Center for Transatlantic Relations at Johns Hopkins University, "The benefits could be substantial in terms of creating jobs, boosting innovation, improving our competitiveness, and ensuring long-term growth and prosperity."

Estimates of the positive impact vary. For instance, the Center for International Political Economy predicted a 15 percent rise in exports for both sides. Sweden's Board of Trade forecast 20 percent annually. (Those would mean an extra $150 to $200 billion.) The U.S. Chamber of Commerce figured that an agreement would boost the combined U.S. and European GDP by $180 billion. Whatever the exact benefits, they are worth pursuing.

In theory, negotiating an agreement should be easy. ECORYS reported that the EU and U.S. already "are very open towards each other in terms of investments and trade, which is exemplified by the relative absence of transatlantic tariff barriers." The basic principle should be: reduce trade barriers. However, doing so would be tougher in practice. Trade rules are more politics than economics. Thus, "free trade agreements" really should be called "freer trade agreements." Even while generally reducing the burden on commerce, FTAs typically transform rather than eliminate regulation. The resulting special interest fights for advantage are vicious.

The Working Group proposed a comprehensive agenda. All tariffs should be eliminated, "with the shared objective of achieving a substantial elimination of tariffs upon entry into force and a phasing out of all but the most sensitive tariffs in a short time frame." With duties now averaging only about five to seven percent, cutting tariffs is the easiest task before negotiators.

One possibility would be to start with a simple accord zeroing out all duties. In a paper for the German Marshall Fund, Fredrik Erixon and Lisa Brandt estimated "the dynamic welfare gains" of this step alone "to be $58-86 billion for the EU and $59-$82 billion for the U.S." Other estimates of the benefits for America run up to about $150 billion. Erixon and Brandt observed: "you have to start somewhere, and it is considerably easier to negotiate tariffs than [non-tariff barriers] and service and investment regulations."

The Working Group also targeted services, the regulation of which is complicated by history, culture, and local practice. The committee advocated binding "the existing autonomous level of liberalization of both parties at the highest level of liberalization captured in existing FTAs, while seeking to achieve new market access through efforts to address remaining long-standing market access barriers, recognizing the sensitive nature of certain sectors." Also desirable are transparency and due process with regard to licensing, which often is used as a form of domestic as well as international protectionism.

Erixon and Brandt cited this as another area which could be settled separately. They argued that while there are important differences between American and European approaches to some issues, "a bilateral transatlantic deal in services makes sense because the EU and the U.S. represent a big portion of trade and production of tradable services in world." Freeing this market would create a de facto global agreement which other countries might be willing to join.

A 2009 report by the consulting firm ECORYS Nederland BV estimated that an agreement slashing non-tariff barriers alone would increase exports by 6.1 percent for the U.S. and 2.1 percent for the EU. This would add an annual GDP increase of .3

percent and .7 percent, respectively, to the U.S. and EU. In turn, that would generate a .4 percent annual wage increase and yield $8,300 per average American household through 2018.

Moreover, the Working Group proposed rewriting regulation "to progressively move to a more integrated transatlantic marketplace, while respecting fully the right of each side to regulate in a manner than ensures the protection of health, safety, and the environment." Explained ECORYS, non-tariff measures "continue to hinder the emergence of a truly free transatlantic market and constitute important impediments to greater transatlantic trade and investment flows." These differences are rooted in "geography, language, preferences, culture or history," as well as policy.

These transatlantic divisions may be greatest. Richard Blackden of London's*Daily Telegraph* warned: "differing standards between the EU and the U.S. over genetically modified food, the chemicals used to prepare poultry and packaging on medicines will be among the sore sticking points in any negotiations. America's agriculture industry, for example, believes that many of the EU's food safety standards, which restrict imports of U.S. meat, are little more than an excuse for protectionism." Of course, the U.S. is no economic virgin, imposing, for instance, air and maritime regulations which frustrate the Europeans. Nevertheless, progress is possible. ECORYS predicted that an ambitious liberalization program could cut non-tariff barriers in half.

Other issues include further investment liberalization, government procurement access, intellectual property procedures, and general trade rules. The Working Group concluded: "comprehensive transatlantic trade and investment agreement, if achievable, is the option that has the greatest potential for supporting jobs and promoting growth and competitiveness across the Atlantic."

Overall, the agenda is sound. However, my Cato Institute colleague Simon Lester warned of the danger of littering an accord with exemptions, exceptions, set-asides, and other restrictions. For instance, he pointed to the fact that the Working Group spoke about limiting tariff reduction for "sensitive products" and deregulation of "certain sectors" in services.

Most important, any agreement must liberalize markets, not cartelize them. Opponents of free trade have fastened on the tactic of "raising" environmental and labor standards, which in practice increase costs, limit opportunities, and restrict competition. Lester pointed out that labor unions hope to manipulate any U.S.-EU agreement to their advantage. Reported *Inside U.S. Trade*, these groups "believe a potential U.S.-EU trade agreement could provide an opportunity to raise some U.S. labor standards to a level prevailing in EU member states." That is, special interests want to use the cause of "free trade" to win political privileges that they are unable to attain through the normal democratic process.

A transatlantic FTA would promote trade freedom around the world. The Working Group expressed the hope that an agreement "could promote a forward-looking agenda for multilateral trade liberalization." Daniel Hamilton made a similar argument, that any accord should be used to free international markets. He hoped that "standards negotiated by the U.S. and EU can quickly become the benchmark for global models, reducing the likelihood that others will impose more stringent, protectionist requirements for either products or services." Indeed, binding the U.S. and EU together in a genuinely free trade regime might spur negotiation of a TPP, with or without China, as well as agreements with other rising economic powers, such as India.

Another technique would be to turn the FTA into what Spanish economist Pedro Schwartz called the Open Atlantic Prosperity Area. Rather than restricting membership by geography, the agreement would "be open to all those nations wishing to join on the same principles as its founders." He termed it "a Trade Round from the bottom up; instead of trying to agree to universally applicable rules at the top table I think it more practical to create a club of commercial liberties so attractive that other nations will want to join."

Negotiations on a transatlantic FTA are expected to begin in the spring. Karel De Gucht called it "a game changer if you can manage it." However, any agreement would have to get through Congress on this side of the Atlantic and both the European parliament and the European Council, made up of national governments, on the other side. The political sell wouldn't necessarily be easy.

Countries around the world are desperate to get their economies moving again. The best stimulus program would be to free the international marketplace. Turning America and Europe into a massive free trade zone would be a good start.