



New Leadership on Trade

By Grant Aldonas and Moana Erickson

Diagnosis

Increased economic anxiety, combined with fears of an ongoing global conflict with extremist forces have led many to question the terms of the United States' engagement in the global economy and the world at large. That anxiety finds its political expression in a growing economic populism that openly questions the benefits of a global economy and an instinct to withdraw from world affairs. Recent elections in the United States underscore that point, bringing a stronger populist and isolationist strain to congressional trade politics. Many incoming members of Congress campaigned on distinctly populist platforms, calling for a halt to new trade agreements, the rollback of existing accords like the North American Free Trade Agreement ("NAFTA"), and higher barriers to immigration.

The populist rejoinder to the benefits of participating in an open world economy highlights the perceived flaws in globalization -- higher returns to capital at the expense of labor and highly publicized estimates of the jobs at risk due to outsourcing (as many as 35-40 million workers under the highest of these estimates). The burgeoning U.S. trade deficit has (erroneously) raised concerns about America's competitiveness in international markets. Critics of U.S. trade policy (again, erroneously) link the economic rise of China and India with U.S. job losses in manufacturing and services to assert the need for higher tariffs and other restraints on trade.

The rise of economic populism and the instinct toward isolationism is not limited to the United States. Voters in France and the Netherlands rejected the European Constitution, in part, based on fears of the economic consequences of further European economic integration. The rise of Hugo Chavez, Evo Morales as well as the election of more moderate, center-left governments in Latin America such as Brazil's Lula da Silva is, in part, a reaction to the failure of market-oriented economic reforms undertaken in the 1990s to fulfill the promise of encouraging economic growth and a rising standard of living.

These domestic political trends have already affected the international agenda and progress toward a more open and integrated world economy. Whether it is the failure of the Doha Round of the WTO, failed attempts to create a Free Trade Agreement of the Americas or delays in concluding free trade agreements with trading partners globally, international trade talks have stalled. Where trade talks are proceeding, such as efforts to construct an East Asian trade arrangement, the express design is to afford preferences to trade within the bloc at the expense of players outside the region. The network of free trade agreements currently under negotiations (upwards of 100 worldwide) will create a new generation of trade barriers in the form of conflicting rules of origin, regional standards, and disputes over their relationship to and conflict with the World Trade Organization, which will still provide the basic framework for an open world trading system.



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All of this reflects a single basic fact – while the economic logic of expanding trade is compelling, the politics of trade are extraordinarily difficult in every country. The inability to garner political support in the United States, Europe, and Japan, much less in the developing world, highlights the reluctance to welcome further liberalization in the face of the difficulties of adjusting to new economic conditions and rising public discontent. Left unaddressed, the concerns that led to that rising public discontent will undermine support for the United States’ participation in the global economy and, in the process, undermine the United States’ ability to shape its own economic future and offer global leadership on trade.

Specific Policy Recommendations

a. **Stimulate a Broader Dialogue on Globalization Domestically and Internationally:**

The United States must stimulate a broader dialogue on globalization, both domestically and internationally. The focus of that dialogue should be how best to capture the benefits of globalization while reducing their human cost. There has been no serious effort at either a national or international level to bring business, labor, and agricultural interests together with policymakers, legislators, and academic experts to examine either the U.S. role in the world economy or a global response to the crisis of confidence in the international system’s ability to grapple with the challenges we face. The President, together with Congressional leaders, should take the initiative in launching a national dialogue focusing on how to shape an economy that captures the benefits of globalization while reducing the human costs of adjusting to the demands of competing in a global marketplace. A bipartisan dialogue focused on developing a vision of America’s role in the global economy that embraces the needs and potential contributions of business and labor, farmers and manufacturers, academia and civil society is essential to our ability to move forward as a nation on the critical economic issue of our times – globalization.

The President, with Congress’ express backing, should use the next meeting of the U.N. General Assembly and the fall meetings of the World Bank and International Monetary Fund to launch a similar discussion at an international level. An international high-level commission could be formed with persons such as Larry Summers, Robert Rubin, Ben Bernanke, Harvey Rosen, Edward Lazear, Alan Greenspan, Paul Volcker, John Taylor, Carla Hills, Rodrigo Rato, Peter Sutherland, Luis Derbez (Mexico), Mario Monti (Italy), David Emerson (Canada), Jin Renqing, (China), Jiechi Yang (China), Eduardo Garza-Aldape Sojo (Mexico), Akira Amari (Japan), Michael Glos (Germany), John Hutton (UK), Tony Blair (UK), O-kyu Kwon (South Korea), Min-soon Song (South Korea), Herve Novelli (France), Christine Lagarde (France), Morgan Ing-san Hwang (Taiwan), Lin Chuan (Taiwan), Maria Van Der Hoeven (Netherlands), Palaniappan Chidambaram (India), Kamal Nath (India), Eliyahu Yishai (Israel) to broaden this dialogue on globalization with representatives from the trade, finance and commerce arenas who are also major trading partners of the United States.

b. **Enhance the Competitiveness of the American Worker:** The U.S. job market has been and will continue to change due to globalization, but the changes wrought to our



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participation in the global economy are insignificant compared to the normal churning in labor markets due to purely domestic economic conditions (e.g., interest rate changes; tax cuts favoring one industry over another) and those due to technological change. Changes in computing, telecommunications, and transportation technology have conquered geographic barriers to increase both domestic economic activity and international trade. America's firms, workers, and farmers will remain competitive only if they are exposed to and adopt the latest trends in technology, consumer preference, business organization, and production – that requires a continuing active engagement in the global economy. The same holds true of our ability to attract or retain investment by globally-engaged firms (regardless of whether they are owned by U.S. or foreign investors) that inject those benefits into our economy. Most of the effort to attract new investment takes place at the state level and focuses on tax abatement and other commitments to lower operating expenses. We tend to ignore, however, the importance that globally-engaged firms attach to a highly educated and well-trained workforce.

What has been largely missing from the U.S. policy agenda has been an initiative that focuses on enhancing the competitiveness of American workers, as well as the recurring efforts to increase the competitiveness of American firms. An innovative approach to education, training, retraining and adjustment, health care, and retirement policies must be developed to enhance the ability of American workers to participate actively in creating a brighter economic future for themselves. We must, at a minimum, update the worker adjustment programs that have not fundamentally changed since the introduction of Trade Adjustment Assistance in the 1960s. A new adjustment assistance program is needed that would ease economic dislocations and the loss of health benefits resulting from displacement in the manufacturing and service sectors, as well as provide broader options for workers' re-entry into the job market.

In light of growing competition U.S. workers face from abroad, innovative policies are needed to identify empirically-based programs that can promote and facilitate individual entrepreneurship and the development of intellectual capital, thereby strengthening America's competitive standing. The government must invest in critical needs that market forces will not adequately meet – such as education, infrastructure, and research and development in advanced technologies. As an immediate initiative that the next administration could launch in its first 100 days, we recommend three concrete actions be taken:

- 1.** Expand the quality and accessibility of education and training, by strengthening science, technology and research and development programs at the primary, secondary, and tertiary levels. Efforts by schools to improve math and science education would be enhanced if supplemented by government spending and public-private efforts to give students first-hand exposure to scientists and engineers in the field. If U.S. companies are to remain competitive, they must be able to hire leading scientists and mathematicians from our own colleges and universities, and these



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students must first obtain a solid foundation at the primary, secondary and tertiary levels. Specifically, a tax credit should be enacted for companies that make their in-house training available through public schools and community colleges. Congress should also allow individuals to deduct from their gross income for tax purposes the full cost of education and training expenses, even when directed at preparation for an entirely new career. Finally, Congress should allow companies a credit against income taxes for the marginal increase in expenses they might incur in extending their internal education and training facilities to workers outside the company or to students in local community colleges.

2. Investment in research and development has long been the bedrock of American innovation. We recommend allocating 10% of the budgets (e.g. make the R&D tax credit permanent) of federal research agencies to discretionary funding focused on high-risk, innovative research. Providing sustained funding to national technology challenges in areas that will ensure enhanced U.S. economic leadership, including nanotechnology, biotechnology, telecommunications, and energy technologies is essential in today's global economy. Asia now spends as much on nanotechnology as does the United States, and foreign-owned companies and foreign-born inventors now account for nearly half of all U.S. patents. Countries that have historically been technological followers are now becoming leaders. Technology R&D in cutting edge fields remains critical to the economic competitiveness of the United States and its workers.

3. The United States government has an essential role in creating the conditions for growth in which all Americans can participate including investment and tax restructuring to incentivize the American worker to obtain necessary, competitive skills training. Other policy issues to enhance the competitiveness of the American worker include reducing the cost of health care costs and, thereby, improving health-care coverage; reforming unemployment insurance, job training programs and trade adjustment assistance to cushion the economic shocks of job dislocation; increasing retirement security, and reducing government regulation to strengthen entrepreneurship and innovation. The productive potential of the U.S. economy lies within its people, and specifically within the ability of America's youth to succeed in an international, knowledge-based economy. The aforementioned policy areas would also help to address income inequalities which have deepened around the globe in recent years. Returns to capital continue to grow, while real wages remain stagnant. Globalization adds to the pressures that already exist within the U.S. economy that have exacerbated income and wealth inequalities. In sum, the United States must strengthen its comparative advantage in value-added, innovative industries, which empower the American worker at the bottom of the pyramid to engage in competitive training to take on new higher-skilled jobs.



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- c. **Engage the private sector to play a key role in enhancing the United States' role in trade and economic issues:** The U.S. private sector can create a broader “market” for U.S. values abroad and enhance the United States' role in economic issues at the bottom of the socio-economic hierarchy through education and training programs, NGO outreach, the altruistic activities of churches, charities and foundations, and cultural and educational exchange programs. Such actors help to define the atmosphere in which the private sector operates internationally at a level below that of trade agreements, international conventions or rules on international labor standards. They also help to promote ethical private sector conduct, and can exert a positive influence on the attitudes of foreign governments – a development that sustains healthy economic conditions in which the private sector can create wealth and value both at home and abroad.

Today, multinational corporations are driving the emergence of new industries and technologies through cross-border financial flows and expanded global value chains. These MNC's are supporting innovative business models that expand public-private partnerships with the potential to address challenges that have heretofore been in the realm of the public sector, e.g. poverty alleviation, environmental concerns, and humanitarian relief. If the private sector can integrate and deliver value to those at the bottom of the pyramid, then political unrest, violence and economic populism will not be as acute even as economic integration of global markets continues to deepen. One example would be the broad expansion of telecommunications as a means of delivering financial services to the poor which would widen and modify the base rules in ways that would broaden its availability to a larger cross-section of industries. By expanding the technical platform created by U.S. telecommunications and the innovation available from the U.S. financial sector, the U.S. private sector would make a significant contribution toward expanding the availability of credit to liberate the poor from the limitations of their domestic banking environs.

The actions of key private sector actors and individuals also play a critical role in influencing the perception of the United States around the world. Accordingly, they can make a major contribution toward restoring America's moral and political leadership. Many of these private sector actors operate on their own initiative. Corporations, in particular, act according to the rules of international trade as established in international negotiations among governments. Increasingly, they also impose voluntary standards on their behavior and adopt a variety of corporate social responsibility norms. Often, this is in order to head off more intrusive regulation by governments. American and other multinational corporations are increasingly discovering that ethical conduct benefits the bottom line. Equally, American international corporations are generally regarded as likely to behave more ethically than their European and Asian competitors, not least because of the greater pressures American companies face from shareholders and other interest groups at home.



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- d. Harmonization of tariff relief for the least developed countries:** The United States, European Union, Japan and other developed countries should harmonize tariff relief and liberalize trade preferences across a range of goods and services with the goal of achieving a single set of rules that assures the greatest degree of market access for those countries. The United States should encourage large emerging markets like China, India, Brazil, Russia, and South Africa, to participate in the negotiation and to adopt tariff preference programs for the least developed economies on similarly harmonized terms. The eventual target should be to reach zero tariffs, applied on an MFN basis, to imports from the least developed countries anywhere in the world. The certainty and scale this initiative would afford the least developed countries would exceed the benefits available to them under any foreseeable scenario evolving in the so-called “development round” launched in Doha under WTO auspices. It would also have the effect of drawing the global trading system back together in support of trade liberalization that works for those at the bottom of the economic pyramid.
- e. Launch negotiations to eliminate barriers to trade and investment in goods, services and technology that contribute to energy efficiency:** The United States should launch negotiations to eliminate barriers to trade and investment in goods, services and technology that contribute to energy efficiency and emissions reductions. A common criticism leveled at the world trading system and America’s leadership role in that system is its inability to affect or shape outcomes that help address other global challenges. The United States could offer real leadership in correcting that impression by building a coalition within the WTO to launch an initiative to eliminate all barriers to trade and investment that currently inhibit the ability of markets to contribute to solutions to climate change.

Message & Marketing

- a. Emphasize the value of human freedom, open markets, transparency and the rule of law in U.S. foreign policy:** China, India, Brazil, and the main body of other developing nations, are playing an increasing role in the world economy and its governing institutions, and their influence can only grow greater in the years ahead. These countries are often less committed than the United States to the principles on which the current international economic and financial system is based – values of democracy, economic freedom, open markets, transparency and accountability in both the private and public sector, and the rule and enforcement of law. Currently, India and China are manufacturing and service-producing global leaders, with Russia and Brazil as their main suppliers of raw materials and energy. These four countries are at the center of their respective regions and are projected to reach the rank of top 10 economies by 2040. If the United States wishes to maintain its global preeminence both politically and economically, it must, (in alliance with Europe), act to stabilize these values into the international system before its influence diminishes too far. The maintenance of such values will enable the U.S. private sector to practice ethical and responsible behaviors that distinguish it from some of its competitors, and cast the United States in a favorable



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light internationally. Economies around the world will continue to become more integrated, but differing standards and regulations will compete to become the global norms.

- b. Ease the burden on U.S. workers most affected by globalization:** The concerns that have led to rising public discontent over globalization will undermine support for the United States' participation in the global economy if the burden on U.S. workers is not alleviated through tax and investment policies. Current data and analysis illustrates that the gains from globalization are disproportionately concentrated at the upper end of income distribution chain with earnings among the middle class falling. The middle class continues to be disproportionately affected by globalization. Politicians should support tax and investment policies that do not exacerbate wealth distributions and which only benefit existing, advantaged classes.
- c. Reinforce the multilateral trading system:** The United States has an opportunity to demonstrate stronger leadership in advocating for more open global trade by making significant concessions to salvage the Doha Round, reinforcing and advocating a multilateral trading system and respect for its rules, and by combating the current backlash against globalization around the world. This initiative need not be politically unpopular if it is linked to a broader strategy for the United States and its workers to succeed in the global economy. That said, the United States will have little chance to promote open markets and greater international prosperity if its credibility as a leader is undermined by protectionism and economic nationalism at home. Not only should the U.S. government take a firmer stance against these trends, it should also seek to proactively set an international example of how to cope and ease the burden of those workers most adversely affected by globalization. For example, the United States could assert its leadership in the multilateral trading system through an ITA-style agreement (tariff-cutting mechanism) which would eliminate all barriers to trade in goods, services, technology and investment and products and/or production processes that contribute to energy efficiency or a reduction in carbon dioxide emissions. The goal of such an ITA-style agreement would be to transform this initial agreement to one that furthers bipartisan trade as a means of exporting American values and smart power, as well as goods and services.
- d. Strengthen the role of international institutions in global governance:** There has been a move away from reliance on international institutions in the area of global economic governance, due to their democratic remoteness and heavy bureaucratic processes. The founding set of institutions following World War II – the IMF, World Bank, GATT and their successors – the OECD, IEA, WTO and G8, must adapt to changes brought about by globalization including the role of the private sector in development, the importance of energy supply flows, large financial and trade imbalances, and capital markets and investment infrastructure. These international institutions must mobilize their empirical knowledge-base and exercise their powers and



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responsibilities as delegated to them by their respective member states. This contributes to the United States' restoring its leadership on trade and economic issues by enforcing rule-based behavior, and by making it more difficult for member states to retract from international consensus and institutional frameworks in which they themselves have chosen to participate. A pragmatic approach to reform in the arena of global governance and international institutions is to strengthen and expand the G8 as a forum for renewed negotiation and decision-making. The G8 could be a catalyst for change by inviting more countries such as China, India, Brazil, Mexico and South Africa to join the summit-level forum to begin to collaborate on global issues such as energy security, global poverty, terrorism and multilateral trading systems.