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BEYOND NAFTA: CLINTON'S TRADING CHOICES

by Jagdish Bhagwati

Although the debate over the North American Free Trade Agreement (NAFTA) will be loud and distracting, its passage seems assured, albeit with some tougher environmental and labor standards. It is time, then, for President Bill Clinton to plan his next, critical step on trade. He must now decide whether to continue with a free trade area (FTA) approach, be it global or confined to the Americas, or to throw his weight exclusively behind a multilateral approach based on the General Agreement on Tariffs and Trade (GATT). Unfortunately, the president seems to be headed down the least attractive of those paths: the embrace of more regional FTAs in the Americas alone.

The president and U.S. Trade Representative (USTR) Mickey Kantor have occasionally remarked, without making a formal policy statement, that they would carry the NAFTA process southward. In a policy statement on March 30, 1993, Larry Summers, the Treasury Department's assistant secretary for international affairs, supported the trade component of the broader Enterprise for the Americas Initiative, which was launched in 1990. After Mexico, then, the Clinton administration is likely to embrace Chile and thus, wittingly or unwittingly, the regional FTA approach—without seriously examining the other options.

Inertia, however, is not a sound basis for policy. Analysis of the choices at hand and an appreciation of the history of such choices are essential if the administration is to make such a momentous decision with vision and wisdom. Indeed, history is most enlightening on this

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question. When GATT was crafted at the end of World War II, the United States was wedded to the cause of open, multilateral trade. It resolutely fought the British, who favored discrimination in defense of Imperial Preference. Because of U.S. efforts, non-discrimination became a central principle of GATT: If trade barriers were lowered for one trading partner, they had to be lowered for all trading partners. Virtually the only exception to that rule is found under Article 24 of GATT, which allows a group of countries to dismantle all trade barriers only among themselves.

That was the door through which the European Community (EC) passed in 1957, with U.S. approval. Though Americans were not at the time interested in Article 24 for themselves, the EC effort led to an outpouring of short-lived FTAs in the developing countries, with the 1960 Latin American Free Trade Association being the most prominent. But the time was not yet ripe for their success. Few developing countries were willing to adopt a regime under which free trade, not planning, would regulate economic activity.

In the 1960s, the use of Article 24 by the United States emerged as a real possibility in a manner that has immediate relevance today. Several influential economists, politicians, and intellectuals in Great Britain and North America came up with the proposal for a NAFTA. But NAFTA then stood for the North *Atlantic* Free Trade Area, which was nonregional at its inception and meant to push outward to the Pacific for new members—with the United States right in the middle of it all. The economist Harry Johnson and Senator Jacob Javits (R-New York) were among the first NAFTA proponents.

The 1960s NAFTA initiative, much like the early 1980s turn to FTAs by the United States, was essentially prompted by the fear that the GATT-based multilateral-negotiations route to lowering trade barriers worldwide had run its course. FTAs, open to new members on a non-regional basis, seemed to offer an alternative, indeed the only, route to free trade everywhere. Thus, at the time, there was a widespread feeling that the Kennedy Round would turn out to be the last opportunity under GATT to lower trade barriers. NAFTA proponents also viewed

the EC as an inward-looking customs union that would resist efforts to liberalize world trade under GATT. At the same time, Atlanticists in Britain and the United States preferred to see Britain link its destiny with the United States rather than with the EC. As British efforts to join the EC met with French president Charles de Gaulle's continuing *non*, others felt that Britain might well have no option but to turn to other initiatives.

It is now time for America to return to GATT as the best means to liberalize world trade.

De Gaulle's opposition to British entry was, of course, driven wholly by the fear that Britain would act as the Americans' Trojan horse within the EC, bringing in the interests and influence of the United States and undermining the French policy of independence from U.S. hegemony. British prime minister Harold Wilson recalled a 1965 cartoon from the *Observer* where a diminutive Wilson says, in short, "I even wake up tired!", to which a towering de Gaulle, a stethoscope in his ear, responds: "Hm. It's all those late night telephone calls to Washington. What you need is an independent policy on Vietnam." Indeed, de Gaulle made no secret of his suspicions about the British. Thus, immediately before his resounding November 1967 rejection of British membership in the EC, de Gaulle had queried Wilson on precisely that issue. As Wilson put it: "The whole situation would be very different if France were genuinely convinced that Britain really was disengaging from the U.S. in all major matters such as defense policy and in areas such as Asia, the Middle East, Africa and Europe."

As it happened, it was precisely the flip side of de Gaulle's concerns that made the American government eager, for political reasons, that Britain join the EC and hence unenthusiastic about the NAFTA proposal. Britain would help moderate, it argued, Gaullist anti-Americanism. In fact, American leaders were also wary of a NAFTA on economic grounds because they were in no mood to give up on multilateralism and

GATT. Both Secretary of State John Foster Dulles and Secretary of the Treasury Douglas Dillon had supported the European Community on political grounds. In 1950, the U.S. House of Representatives had amended the Economic Cooperation Act to include among its objectives the “economic unification of Europe” as part of the effort needed to restore Western Europe to prosperity, strengthening it against the Soviet menace. Both Dulles and Dillon opposed a Europe-wide free trade area, as distinct from the then six-member EC. Thus, any FTA that focused on free trade alone, as the first NAFTA was designed to do, the American government found unacceptable. It saw America’s interests in multilateralism and non-discrimination, as typified by GATT: A trading regime embodying those principles would provide a predictable and orderly framework for trade among all countries and hence benefit the United States in turn. By contrast, the North Atlantic initiative, despite its ultimate objective of free trade worldwide, would have entailed preferences and discrimination at the outset.

The 1960s NAFTA initiative then came to naught: The U.S. government refused to play. But the conjunction of factors encouraging a U.S. policy shift to FTAs had returned in the early 1980s and, this time, the United States changed its mind and its course. Faced with European refusal to start multilateral trade negotiations in 1982, and with growing protectionism at home that required countervailing moves to expand trade, the Reagan administration initiated the talks culminating in the Canada-U.S. Free Trade Agreement now turning a decade later into NAFTA, the North *American* Free Trade Agreement, with Mexico.

The new NAFTA is clearly a regional FTA, and extending it to South America would undoubtedly stamp it as regionalism par excellence. Yet, it is noteworthy that, as with the aborted 1960s NAFTA initiative, the policy shift to Article 24-blessed FTAs by the United States in the 1980s was not conceived as being narrowly regional in scope. When the U.S.-Canadian agreement was first negotiated, its supporters could be roughly divided into two camps, both of them anti-regionalist.

The first group, the GATT optimists, thought that the U.S.-Canadian agreement would push the EC and the developing countries into a new GATT round. Without the United States, all would realize, GATT would have little future and world trade would revert to the law of the jungle, which would be most painful to the weak. The strategy worked, and the American embrace of Article 24 through the Canada-U.S. FTA did indeed prompt countries to come to the table with the GATT Uruguay Round of multilateral trade negotiations. When completed, the Uruguay Round will radically transform GATT, implementing many of the reforms for which the United States has been fighting over the last decade. According to that school of thought, the turn to FTAs was a tactical move designed to jumpstart the GATT multilateral negotiations. Having succeeded in doing so, it is now time for America to return to its original commitment to GATT as the best means to liberalize world trade.

Inertia is not a sound basis for policy.

A second group, the GATT pessimists, also favored the Canada-U.S. FTA. But much like the earlier proponents of the North Atlantic initiative, they saw FTAs as part of a global strategy that sought to build FTAs that were open-ended, not regionally exclusive. Ambassador William Brock, the USTR in the early years of the Reagan administration, offered FTAs even to members of the Association of Southeast Asian Nations. He would have no doubt offered them to the moon if only he could have found life there and a government with whom to negotiate.

The GATT pessimists thought of the GATT process of trade negotiations as less effective and rapid than the FTA approach to worldwide trade liberalization. But that is a hasty and ill-considered view. A comparison of the two processes of trade liberalization is surprising. It turns out that the problems that plague the one also afflict the other. As the economists Bernard Hoekman and Michael Leidy have pointed out, the holes (areas left out) and the loopholes (areas where the disciplines of free trade are

avoided) are practically identical in either case. As for slowness, consider the European Community: The process began in 1957, with the Treaty of Rome pledge to eliminate trade barriers as required by GATT Article 24. As of 1993, it still has not succeeded—not exactly a record of alacrity. The NAFTA talks, which aim to bring together only three countries, have taken nearly a decade, while the Uruguay Round, with 112 countries participating, has so far taken only seven years.

Nonetheless, the nonregional FTA approach embraced by Brock became the U.S. trade policy in the early 1980s, downgrading the option of sticking to multilateralism despite its revival at the Uruguay Round. Yet, down the road, that policy turned into the narrow regional FTA option that is the least attractive of those available. Some of the blame lies with the U.S. Treasury Department, which was able to capture the FTA idea for its own purposes, offering preferential trade to South America in lieu of debt relief. When the South Americans responded positively, the State Department muscled in, turning the trade initiative into a foreign policy initiative and making it an integral part of the Enterprise for the Americas Initiative. That program harked back to President John Kennedy's Alliance for Progress, except that the latter did not include an offer of regional FTAs because the United States was correctly devoted to multilateralism at the time.

The effect of that narrower vision has been to encourage the notion that the United States is interested in trade regionalism no matter how strong its professed commitment to multilateralism. Since the United States also recognizes its vital trade interests in the rapidly expanding markets of the Far East, it has found itself in an awkward position. George Bush's secretary of state, James Baker, was trying to convince the Asian countries not to form their own Japan-centered FTA even as he worked on the NAFTA and its exclusive extension to the south—an incoherent position that argues that what is good for me is not good for you.

Many have even tried to convince themselves that an Asian trade bloc is unlikely because the Asian countries will not soon forget Japan's wartime cruelties—conveniently forgetting that

other countries have learned to live with and profit from Germany despite the unparalleled crimes of the Holocaust. The profit motive can help numb the grey cells of memory.

Indeed, few would have thought that anti-Yanqui sentiments would so quickly evaporate from the Mexican scene, allowing President Carlos Salinas de Gortari's splendid team to hitch Mexico's economic destiny to America's. Salinas turned on its head Porfirio Diaz's famous dictum: "Poor Mexico, so far from God and so near the United States."

But if the United States pushes FTAs only southward, it will certainly invite a defensive, if not retaliatory, bloc in Asia. Divisions will be sharpened and the world economy fragmented into four blocs: an expanded EC, a NAFTA extended to the Americas, a Japan-centered Asian bloc, and a marginalized group of developing countries, many with low incomes and only just turning to export-oriented strategies. We should not favor that scenario.

If the United States continues to pursue FTAs, the least it can do is to return to the Brock agenda, to the vision of the 1960s North Atlantic initiative. That would mean developing a new strategy of openness before adding any new members, especially from South America.

Such a policy would have to be unambiguously stated and diplomatically credible. Negotiations to add one or more non-hemispheric countries before adding hemispheric ones would help. Then again, if U.S. domestic politics drives America farther south, well beyond the Rio Grande, Canada could be explicitly encouraged to seek out new NAFTA members from the British Commonwealth, countries to which Canada surely has stronger economic and historical links. Indeed, instead of playing the complaisant junior partner in NAFTA, Canada could itself play a leadership role; prime ministers like Lester Pearson and Pierre Trudeau did not shy away from the world stage.

But all that is more readily urged than undertaken. Clayton Yeutter, the former USTR who negotiated the U.S.-Canadian agreement, has candidly described the enormous difficulties of such talks. Then again, the politics of pushing the next agreement through Congress could be quite a challenge. Imagine what would happen

if the Congress were considering an FTA with India—or with Japan.

Yet many analysts seem drawn to FTA blocs, to a power-political conception of trade that sees the world as a jigsaw puzzle. Some call for a U.S.-Japanese Pacific free trade area, with the two economic superpowers bringing along their respective regions to provide a counterweight to the enlarging EC. In turn, taking a cue from Margaret Thatcher—the irrepressible Atlanticist—and from the Japanophobes, columnist Charles Krauthammer recently argued that the three NAFTA countries should free up trade with the EC instead. “A transatlantic free-trade zone would signal Japan that if it had thoughts of creating a rival Asian bloc or did not modify its predatory drive for market dominance, it might find itself shut out of the new world economic order,” he wrote in *Time*. And thus each of us will act out our own fantasies, seeking allies against imagined adversaries, lining up our preferred blocs against the others, and vying for political attention and action.

The more deeply one thinks about the issue, and about the basic choice between multilateralism and FTAs as ways of bringing down trade barriers worldwide, the more disenchanted one is likely to be about the latter. Even the popular notion that the two processes and policies can coexist—the “GATT-plus” proposition—and even be benignly symbiotic, is too simplistic. Lobbying support and political energies can readily be diverted to preferential trading arrangements such as FTAs, where privileged access to markets is obtained at the expense of outside competitors (such as the EC and Japan in NAFTA). That deprives the multilateral system of the support it needs to survive, let alone be conducive to further trade liberalization.

The wisest option for the Clinton administration, therefore, is to move NAFTA with Mexico through Congress, conclude the Uruguay Round, and then focus exclusively on the multilateral trading regime of GATT. Will the administration rise to that challenge or, in choosing the least attractive option of regional FTAs, continue the sorry spectacle of thoughtless trading choices?