USTR Lighthizer introduces the Trump trade doctrine

Shanker Singham looks at President Trump's trade policy, and what the Administration means by 'free and fair' trade

Trade played a significant role in the recent G7 discussions, and based on what happened after the last G7 meeting where the US famously withdrew the usual paragraph committing G7 members to 'no new protectionism', there was much speculation about what the US would say, especially since a new US Trade Representative is now in place. The key words in this G7 was the reference by US officials including USTR Robert F Lighthizer to 'free and fair' trade.

During the campaign, and since taking office, President Trump has made a number of statements that suggest that Trump trade policy will be highly protectionist. He announced the withdrawal of the US from the Trans Pacific Partnership (TPP), and also signalled his intent to pull the US out of, or to substantially renegotiate the North American Free Trade Agreement (NAFTA).

On the other hand, early rhetoric on China has not been matched by protectionist actions, and indeed a recent deal the administration did with China purported to fix many of the trade barriers that have plagued the US-China relationship for many years (notably in financial services generally, and credit card market access in particular). What is the Trump trade policy, and what precisely is meant by 'free and fair' trade.

Free and fair trade

Fair trade is a term that has been used extensively since the 1999 WTO trade ministerial. Indeed the rise in the use of the word also coincided with the decline in the overall free trade consensus. The approach generally taken is that trade cannot be fair unless the key inputs to the cost of production are the same in the two trading nations. Hence, the desire by some to artificially increase the costs of labour and environmental protection for developing countries in trade agreements with developed countries.

The problem with this approach is that not all countries should have identical labour costs and indeed low cost labour is one of the key comparative advantages of some developing nations (in some cases the only way they can rise up the development ladder). The challenge is to isolate out those differences that are truly unfair and take steps to change those things that are bad for trade, and bad for domestic consumers where the distortions occur.

That new USTR, Robert F Lighthizer used the G7 to try to explain what he meant by fair trade, and to identify those practices that adversely affect trade in ways that damage international trade (his particular concern being producers in the US). While this might not be a concern to the Trump trade policy, it bears pointing out that consumers in the markets where the distortions occur and global consumers occur also suffer when markets are distorted in anti-competitive ways. In his speech, we see the beginnings of a Trump doctrine on trade based more on reciprocity and the totality of a country's trade barriers, not just those at the border.

The Trump trade policy is still emerging. It is vital that what emerges moves the world forwards towards freer trade and more competitive markets, lifting people out of poverty and creating wealth

Breakdown of the free trade consensus

For Lighthizer and other members of the Trump team such as Commerce Secretary Wilbur Ross[1] and President Trump himself, fair trade means that what happens inside a nation's borders does have an impact on trade and must be dealt with as part of a comprehensive trade agreement. If we do nothing about economic distortions inside borders, then we merely import them into our own economies with devastating, and yes, unfair results for our own producers. It is important to note that this is not protectionism in the classical sense.

Indeed, it is the logical application of free trade and free markets to the US *and* to the countries that it does business with. What the US wants to see is a systematic reduction of the domestic distortions that damage trade while at the same time driving down border barriers between nations. It is crystal-clear that countries that refuse to lower their internal distortions will not benefit from US tariff reduction or US trade agreements. For now, the US administration believes it can achieve its goal most effectively through bilateral deals.

However, the Administration may come to realize that agreements with like-minded countries (ones that agree that distortions are bad) could also yield benefits, and should not be ignored. Supply chain efficiencies can only realistically be achieved by larger groupings. The Administration will have a first taste of what these possibilities are in the NAFTA renegotiation process as they seek to add provisions on state-owned enterprises, and stronger disciplines on competition policy into the agreement.

Selling free trade: an old paradigm

In the past, free trade has been sold by its proponents in the following way. Free trade is good because it makes your clothes, food and other essentials cheaper. There are winners and losers. Tough. Protectionism has been sold equally simplistically. Free trade is bad because it will mean you will lose your job. We will protect you from free trade with tariff protection that will keep cheap imports out.

Both of these statements are false. Free trade is not really free if one country is artificially lowering the costs of its producers (be they state-owned or not) so that they can outcompete a domestic producer. Keeping cheap imports out merely increases price and pushes people into poverty as the price for basic goods goes above the market price. Instead, politicians must come up with a more nuanced view of trade, at a time when behind the border barriers, regulatory and other economic distortions are the most pernicious barriers in international trade.

This is the view that the Trump team are reaching towards, and it supports our own work in this area.[2]

The new paradigm: free trade and free and competitive markets

In the papers referred to we argue that economic distortions that lessen competition (which we describe as Anti-Competitive Market Distortions or ACMDs) need to be dealt with both offensively in trade agreements in order to discipline countries not to introduce them, and to lower the ones they have, and also defensively by imposing a tariff based on the scale of the distortion if in fact it can be shown that an ACMD exists and that it has affected trade and damaged a particular industry.

We identify the types of practices that could be regarded as ACMDs. For example, rules that artificially increase the costs of certain producers by setting unnecessarily high capital adequacy requirements for banks, or providing regulatory protection for certain processes for producing products can substantially lessen competition, and lead to consumer welfare losses. In addition, by giving producers in the home market an artificial edge they can prevent exporters competing fairly, or can allow those producers an artificial benefit in reaching the other market. Both cases damage producers and consumers alike (albeit in different markets).

We also set out an offensive and defensive mechanism. Offensively, we can include disciplines on competition, and also on domestic regulation such as those found in the Reference Paper on Competition Safeguards in the WTO (part of the Basic Telecommunications Agreement), or by building on the state aids provisions of European Union law.

Defensively, we argue that the US can build on existing trade laws, such as section 337 to exclude or tarifficate ACMDs, as a species of unfair competition (which that statute specifically applies to, in addition to violations of intellectual property). As we have noted in our paper, *Trade Tools for the 21st Century*:

> *Section 337 condemns as illegal imports (1) that violate US intellectual property (IP) rights related to a US industry (including patents, copyrights, trademarks, and certain designs), or (2) that involve 'unfair methods of competition and unfair acts' that cause harm to a US industry.*
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> *The US International Trade Commission (USITC), an independent federal agency, is required to investigate allegations of Section 337 violations and to direct the exclusion of the articles concerned when a violation is found, unless it deems that specified public policy conditions counsel against exclusion. The USITC may also issue 'cease and desist' orders in lieu of exclusion orders. The US president may disapprove ('for policy reasons') a USITC Section 337 exclusion or cease and desist order within 60 days of receiving it from the USITC, but in practice, this right has very seldom been exercised.*[3]

In practice, this provision has been very sparingly used in the case of acts of unfair competition, but more so in cases of intellectual property violations. However, the Trump administration may find in Section 337 a mechanism which could be focussed on acts of unfair competition, and might be the basis for actions that they may wish to take to correct for unfair trade.

A coalition of the willing

Countries like India, Brazil and China have long argued that international trade liberalization stops at the border. Indeed, they have resisted any attempt to reduce behind the border barriers, and successfully fought off major initiatives such as the Singapore issues on trade and competition, and trade and investment, and the Free Trade Area of the Americas ('FTAA'). These countries will generally not be supportive of the new US trade policy.

While the above countries are unlikely to support the Trump initiative, there are many countries who recognize that the goal of pursuing trade liberalization and markets whose organizing principle is competition is an extremely important one both systemically for the trading system itself, and for their national economic objectives. Unsurprisingly these countries are those that generally have open trading systems and competitive and undistorted markets.

This would include countries like Australia, New Zealand, Singapore, the UK (out of the EU), the NAFTA group, and possibly the Pacific Alliance countries of Chile, Peru and Colombia. This would not be an insignificant grouping, representing at least half of world trade. The critical thing would be to ensure that this is a high standards agreement and the level of ambition for liberalization and competition is not diminished in any way. One lesson from the TPP negotiation is that if agricultural subsidizers are brought in too early into the agreement, the level of ambition will be diminished.

What is at stake?

Adoption of this type of mechanism would go a long way in fixing the perceived unfairness in international trade which is being picked up by producers in developed markets and the people they employ. Many of these people are the ones who sense that the economic game is rigged against them, and who voted for an anti-establishment candidate. The alternative to the mechanism we propose is not a return to the status quo, but rather a full embrace of protectionism with all the damage it will inflict on people – a perfect case of the medicine being worse than the disease.

It is clearly important, and in the interests of all trading nations and their people that we find a mechanism to help us deal with the very real distortions that have an impact on the supply chain, and on trade flows. Failure to do so will unleash the forces of protectionism which will destroy the huge economic gains which were made after the second world war with the GATT system.

The Trump trade policy is still emerging. It is vital that what emerges moves the world forwards towards freer trade and more competitive markets, lifting people out of poverty and creating wealth. It is equally vital that what emerges is not the protectionism which destroys wealth from economies and pushes people into poverty. ■

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Endnotes
1. Donald Trump will make trade fair again, Wilbur Ross, Financial Times, 4 April, 2017
2. In particular, see
http://www.li.com/activities/publications/trade-tools-for-the-21st-century and
http://www.li.com/activities/publications/introduction-to-anti-competitive-market-distortions-and-the-distortions-index
3. Trade Tools for the 21st Century, Shanker A Singham and A Molly Kiniry, Legatum Institute, October, 2016