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The Strategic Setting: An American Assessment

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Trading arrangements in the APEC region are now in considerable ferment. APEC's commitment to open regionalism at Bogor in 1994, NAFTA's launch that year, AFTA's start in 1993, the Uruguay Round's conclusion in 1994 and the WTO's creation in 1995 ushered in a brief period of relatively stable trading arrangements. During the four years that followed Bogor, only two FTAs – Chile-Mexico and Canada-Chile (both of them by-products of Chile's exclusion from NAFTA on political grounds) – were negotiated in the entire APEC region. Regionalism seemed to be at bay in the Asia Pacific, even as it was flourishing elsewhere.¹

The Asian financial crisis of 1997-1998 and the Seattle WTO debacle a year later did much to ignite the current ferment. Since January 1999, at least 25 sub-regional FTAs have been mooted among APEC countries.² Most significant, three major APEC countries that previously eschewed sub-regional FTAs – the U.S. (NAFTA apart), Japan, and South Korea – are now actively exploring them. The U.S. is the principal cheerleader for a Free Trade Area of the Americas (FTAA) agreement, it is negotiating bilateral FTAs with Chile and Singapore, and it is contemplating bilaterals with Australia, New Zealand and perhaps South Korea.³ Japan and South Korea are studying a bilateral FTA, which South Korea suggests broadening to include China. Japan will probably conclude a bilateral FTA with Singapore this year, it is studying a plurilateral FTA with the ASEAN countries, and it is also looking at bilateral FTAs with Canada, Chile, and Mexico.⁴ For its part, China has also suggested a plurilateral FTA with the ASEAN countries, some believe that a China-Japan FTA is conceivable in the medium term, and a free trade area encompassing all of East and Southeast Asia region is another scenario that receives increasing discussion.

In Washington trade policy circles there is again talk of Paul Krugman's three-bloc world, in which the EU, a western hemisphere FTAA, and a fused East Asia would

¹ In a useful compilation of regional trade agreements, Scollay and Gilbert note that an average of 11 new agreements were notified annually to the GATT/WTO between 1992-1998. 'By 2000, the WTO counted a total of 172 Regional Trade Agreements currently in force, and a further 68 under negotiation.' R. Scollay and J.P. Gilbert, *New Regional Trading Arrangements in the Asia Pacific?* Washington: Institute for International Economics, 2001, p. 5.

² *Ibid.*, p. 3.

³ Senator Max Baucus (D-Montana), the newly installed Chairman of the pivotal Senate Finance Committee, and Representative Jim Leach (R-Iowa) have lodged bills in Congress that would grant the Bush administration trade promotion authority to negotiate FTAs with these three countries.

⁴ *Financial Times*, 7 June, 2001.

face each other in mutually discriminatory trading constellations.⁵ Though most observers regard Krugman's vision as alarmist or, at least, as a long way off, Fred Bergsten's alternative depiction of a 'multipolarized' world trade regime seems quite realistic.⁶

The ferment in APEC trading arrangements is accompanied by much ferment in APEC political regimes. The slow-motion Indonesian train wreck, which could eventually be of Soviet magnitude, is the most dramatic case. In the Philippines there are disquieting earmarks of the Indonesian trajectory in the form of Joseph Estrada's election to the presidency, his ejection by the military, and resurgent Islamic secessionist forces in the southern islands. In Thailand, the election purchased by Thaksin, ongoing investigations into his financial wheeling and dealing, and Thaksin's high-handed actions in economic matters form a cloud that may contain another of Thailand's many military coups. Malaysia approaches a difficult transition from Mahathir's long rule coupled with renewed communal tensions and much economic uncertainty. All three post-totalitarian regimes in the region – China, North Korea, Vietnam – face uncertain but surely divisive transitions to more garden variety forms of authoritarian rule, for which nationalism will be the main political mobilizing device. The less said about political (in)stability in Myanmar, Cambodia and Laos, the better. Political paralysis shows no sign of easing in Japan, it has a renewed grip on the United States, and the possibility that paralysis will take hold in both Mexico and South Korea is real. It's no wonder that the oligarchy in control of Singapore is looking for life rafts in the form of bilateral FTAs with just about any countries willing to negotiate them.

These brief observations are, of course, a pastiche of developments in the APEC region. But they highlight some of the complexities that the Bush administration confronts in formulating its trade strategy

The Emerging Zoellick-Bush Trade Strategy

The Bush administration has yet to state its trade strategy explicitly. This is because of the political priority it has given to the just-enacted tax cut, and because the administration finds itself embattled on a number of other fronts – energy policy, the national missile defense system, the electricity crisis in California and some other states, etc. The defection of Senator James Jeffords (I-Vermont) from Republican ranks in the Senate and that chamber's consequent takeover by the Democrats have hammered home the administration's exceptional political weakness. Indeed, it is not hard to find well-informed observers in Washington who believe that, though the administration has been in office a scant 150 days, it has already seen its best days. It is quite possible that the

⁵ P. Krugman, 'Is Bilateralism Bad?' In *International Trade and Trade Policy*, eds. E. Helpman, A. Razin. Cambridge, MA: MIT Press, 1991.

⁶ F. Bergsten, 'America's Two-Front Economic Conflict.' *Foreign Affairs*, March/April 2001, pp. 16-27.

Bush administration's trade strategy will amount to no more than a few limited initiatives for which congressional support can be stitched together.

Nevertheless, press statements by USTR Robert Zoellick and reports of discussions that Zoellick has had with officials from relevant countries suggest that the administration would *like* to implement an ambitious three-pronged trade strategy:

1. Pursue vigorously the FTA of the Americas, as proclaimed at the hemispheric summits in Miami and Québec and as strongly endorsed by President Bush, who has much personal enthusiasm for this initiative. Trade specialists in Washington believe that the FTAA negotiations could be completed by January 2005, though the agreement would not be implemented in any full way until, say, 2020. Negotiations that are going forward with Chile for a bilateral FTA will probably be concluded this year, and the Chileans have mounted an aggressive lobbying effort with Congress to adopt this agreement. Some Washington observers regard the Chile-US FTA as a way of 'goosing' Brazil to be more disposed to the FTAA by signaling that the U.S. intends to negotiate bilateral or plurilateral FTAs in Latin America with or without the Brazilians.
2. Enter into cross-regional FTAs (CRFTAs) with countries in the Western Pacific, as in the current US negotiations with Singapore. Australia and New Zealand, but perhaps also South Korea, are prime candidates. As was the case with the Clinton Administration's Jordan-US trade agreement, one or more of these CRFTAs might be achieved without trade promotion authority being granted by Congress. Their aims would be to breathe new life into APEC, thereby helping to jump-start a WTO round, and to indicate that the U.S. wants to avoid the APEC region splintering into opposing trade blocs, one in the Americas and the other in East and Southeast Asia. As regards rejuvenating APEC, it is significant that George Bush's good friend and ally, President Vicente Fox of Mexico, will be the next APEC chairman.
3. Work to launch a world trade round at the Doha WTO ministerial meetings in November. This has been pledged publicly by Zoellick and is taken seriously in Washington, though expectations for robust results anytime soon are certainly modest. A key question is the extent to which Congress will festoon the necessary trade promotion authority with provisions for ensuring labor rights, safeguarding the environment, and maintaining US anti-dumping and other protectionist laws and measures.

The order in which I list these prongs of the nascent Zoellick-Bush trade strategy is deliberate. Although Zoellick and other administration leaders insist publicly that their top priority is the WTO round, in reality the administration is more invested in achieving the FTAA and in offsetting its effects with a set of CRFTAs in the APEC region. The FTAA receives such a high priority because of the strength of the Washington view that US strategic interests lie first and foremost in its own hemispheric region. Australians may not comprehend fully enough just how far economic, demographic, cultural, and also political integration has proceeded in the Americas. In North American political and

business circles NAFTA is regarded more or less uniformly as an astonishing success.⁷ There is a widespread belief that this success can be duplicated throughout the hemisphere, and there are strong political constituencies in the U.S. for doing so. At the same time, Latin America's formidable problems are seen as real and proximate threats to America's well being. In most Latin American countries democratic regimes are still precarious and are under strong populist pressures. Drug trafficking into the U.S. is highly organized and impervious to border controls. There are high levels of corruption nearly everywhere. Most pressing of all is the large and constantly increasing flow of Latinos into the U.S. as a result of glaring social inequalities at home that can only be reduced through sustained economic growth. Though no one regards the proposed FTAA as a panacea, the NAFTA track record with Mexico and the need to find ways of moderating Latin America's problems impel the Bush administration to go forward on the FTAA front more vigorously than on any other.⁸

In my view, the prospects for an Australia-US Free Trade Agreement should be assessed primarily in terms of the mooted FTAA because the two ventures are likely to be quite interrelated. If the FTAA goes forward, then an Australia-US FTA will be an important corollary to it that is aimed at spurring wider APEC liberalization. If the FTAA is abortive, bilateral FTAs with Australia and other APEC countries, in both Latin America and the Western Pacific, will be second-best alternatives for the U.S. and its NAFTA partners. As Zoellick put it two weeks ago when in China for the APEC ministerial meetings, 'If other countries are unwilling to move forward, we will take care of our own economic interests, whether with bilateral agreements, regional agreements or other steps.'⁹

Much probably turns, then, on how the FTAA initiative unfolds. Most immediately, this is a question of whether the Bush administration will obtain trade promotion authority (TPA) from Congress this year. Washington trade observers are split down the middle over this, half cautiously optimistic, the other half quite pessimistic. It is generally agreed that the Senate is more disposed to grant TPA than the House and that this probably remains the case even after the Democratic takeover of the Senate. In the House, the minority Democratic leadership is uniformly opposed to granting TPA or, at least, to doing so without attaching so many safeguard provisions that US negotiating capacity would be crippled. To gain House approval of a serviceable TPA, the Administration needs between 35 and 50 Democrat votes. These will have to come, in the main, from Democrats representing districts that contain large numbers of Caribbean and Latino voters, for whom the FTAA is an enticing prospect. In the Senate, states with powerful agricultural interests are represented in gross disproportion to their small populations, and there are not a few Senators from textile-producing southern states - the new Chairman of the important Commerce Committee, Fritz Hollings (D-South Carolina), being the most flamboyant example. Obtaining TPA without provisions or at

⁷ To give just one indicator of NAFTA's success, *annual* direct US investments in Mexico, which is now the US's second largest trading partner (after Canada), increased from \$4.9bn in 1994 to \$8.9bn in 2000. *Financial Times*, 23 May, 2001.

⁸ A forceful statement of this policy priority is made by Henry Kissinger in his new book, *Does America Need A Foreign Policy?* New York, Simon & Schuster, 2001.

⁹ *New York Times*, 7 June, 2001.

least understandings that prevent large amounts of agricultural and textile trade liberalization will be a hard sell indeed.¹⁰

One can slice and dice the coming political maneuvers over TPA in many ways. For example, it is in the administration's short-term political interest to carry the TPA fight to the Democrats in both chambers, thereby enflaming and exposing the Democratic Party's deep divisions over trade liberalization. On the other hand, the administration may decide that, having lost control of the Senate, and having angered Democrats in both chambers by ramming its massive tax cut through without even holding congressional hearings, the risk of a TPA defeat is too great. Thus, a deal involving concessions by the Administration on high-priority Democratic issues in exchange for support on TPA may be the better way to proceed. Or again, both sides may decide tacitly that the TPA issue is too fraught in this narrowly divided Congress and that action on it must await the results of next year's elections.

The Bush administration enjoys one significant advantage over the Clinton administration, which is that it is not beholden to trade union protectionist pressures to anything like the same extent. But, offsetting this advantage, the administration is greatly beholden to industry pressures, as is evident in its decision this month to initiate a case before the US International Trade Commission aimed at curbing steel imports. Moreover, the administration's 'in your face' calls for more or less unlimited supply-side energy measures and its decision to walk away from the Kyoto Accord have antagonized environmental lobbies greatly. The administration has likewise antagonized millions of electricity-starved Californians (and New Yorkers) by its steadfast resistance to capping electricity prices and its apparent readiness to watch 30 million Californians and others 'sweat in the dark' this North American summer. These are reasons why the newly empowered Senate Democrats may well decide that sabotaging the administration through endless but politically profitable hearings, leading to policy stalemates, is the best course to take. In which case, TPA is unlikely to be obtained this fall and the window for trade liberalizing initiatives will be slammed shut by Christmas.

Prospects for an Australia-US FTA in the Near Term

Let me employ the window metaphor to take a closer look at prospects for an Australia-US Free Trade Agreement in the near term. If TPA is necessary for negotiating an agreement that Congress won't later pick apart, it does seem that a rather narrow window of opportunity will exist during the next several months. This is because TPA is most unlikely to be granted during the 2002 congressional election year or during the 2004 presidential horse race that will be off and running almost immediately afterwards. No American politician wants to deal with trade liberalization during an election campaign. By roughly the same token, it seems to me that the will to push the Americans to undertake FTA negotiations will diminish if this year's Australian federal elections produce a change in government in Canberra. At the least, an ALP government would have to settle in and deal with significant internal divisions about the desirability of an

¹⁰ To illustrate, Senator Baucus, representing agriculture-rich Montana, is up for re-election in November 2002. The last time he faced an important Senate trade vote in advance of his re-election campaign, in 1994, he voted against the Uruguay Round's adoption.

Australia-US FTA before it became highly active in Washington. By that time, the American election cycle would be in full swing.

Conversely, if the Americans agree to launch negotiations between now and Australia's federal election, it seems to me that the election's outcome will not greatly impede the start of actual negotiations early next year. I must, of course, defer to the many at this conference who are better able to assess Australia's disposition toward an Australia-US FTA under an ALP government (and whether such a government is likely in the first place). But I suspect that if American agreement to negotiate is secured in the next few months, whichever government is in place in Canberra early next year will go ahead with the FTA negotiations.

But maybe my thesis about a narrow window of opportunity is too pessimistic. It is worth asking what might happen if Congress refuses or cripples TPA. Negotiation of an Australia-US FTA, and probably of a parallel one between New Zealand and the U.S., could still get underway early next year and be approved legislatively by Congress during the brief interregnum that will follow next year's congressional elections and the 2004 presidential race's start. This might not be the optimal way to proceed, but the current US negotiations of trade agreements with Chile and Singapore suggest that it could be feasible.

The gains that the U.S. and Australia can realize from a FTA are great enough to warrant resorting to this second route if it becomes the only one open. These gains, as well as the costs they involve, will be the subject of detailed discussions later in this conference. If I just tick off the most obvious gains, one is the creation of a high-quality FTA that will show what should be done with other APEC countries, with the FTAA, and with the WTO round itself. The demonstration effect of large agricultural exporters and competitors like Australia and the U.S. making significant mutual concessions in agriculture would be especially significant. Second and similarly, there is the chance to show, as CUSTA and NAFTA demonstrated between Canada and the U.S., how liberalizing trade can enhance investment and technology flows among capital intensive and industrially advanced countries. A third major gain would be the deepening of existing Australian-American security arrangements and foreign policy cooperation in the politically unstable Western Pacific region.

What would some of the main costs be? From the US side, Australia would have to be given significantly greater – though it is politically unrealistic to expect fully open – access to US agricultural markets, probably equivalent to the access that Mexico gained through NAFTA. The Bush administration would clearly pay a political price for this. In addition, although there is little enthusiasm among Republicans in Washington for including labor and environmental standards in any trade agreement, doing so is by now probably unavoidable politically. Fortunately, Australian laws and practices should make this quite easy, even if there might be some abrasions. From the Australian side, costs would include accepting much less than optimal access to US agricultural markets, having to live with continued US farm subsidies, and having to make unpalatable intellectual property, local content, and foreign ownership adjustments at home. But while certainly significant, these costs would pale by comparison with gaining preferential access to the world's largest, most globally oriented, and most technologically advanced economy.

There is another reason for thinking that the legislative route to an Australia-US FTA may be the one to take. This is the possibility that even if the Bush administration obtains broad TPA from Congress this autumn, negotiating an Australia-US FTA risks getting lost in a jumble of other trade initiatives and policy struggles in Washington. As indicated, the grant of TPA will be focused on negotiating the FTAA and also on the WTO round, so that most of the Bush administration's negotiating capacities will be devoted to these projects. For the duration of this narrowly divided Congress, moreover, the administration will be embroiled in a great many other domestic and foreign policy disputes and struggles.

In Washington's trade and policy whirlpool, an Australia-US FTA is essentially a peripheral matter. There is no large constituency in the US political arena to promote and protect Australia's interests. Although there is every reason to believe that people in the White House, as well as top officials in the State and Defense Departments, the intelligence community and USTR, are disposed toward an Australia-US FTA, there is no reason to expect them to devote much political capital to push it. On Capitol Hill there is also broad good will toward Australia, but there are a great many more politically potent fish to fry. Equally important, among the numerous Washington think tanks that do so much to generate ground swells for policy initiatives, there is no phalanx of experts who concentrate on Australia. With very few exceptions, think-tank Washington is indifferent to an Australia-US FTA.¹¹ It is left to the Australian Government's emissaries, the score or so of large corporations with significant operations in Australia, a few journalists, and a smattering of academics collaborating with each other across the Pacific to create the policy discourse that an initiative of this kind needs.

Conclusions

Australia's welcome offer to negotiate a Free Trade Agreement with the United States is fast approaching a decision point in Washington. Both countries clearly stand to gain from the proposed FTA, and in a less cluttered policy and political world this self-evident fact would be enough to see it through to fruition. In the real world, however, the mooted Australia-US agreement is entwined with larger and politically more difficult Bush administration undertakings, the most important of them being the proposal for a Free Trade Area of the Americas. Prospects for the Australia-US FTA depend to a considerable degree on how this FTAA initiative goes. The Australia-US FTA may be either a corollary to the FTAA or a second-best alternative to it. In the latter case, Australia and the U.S. probably have no alternative but to negotiate an agreement that can gain congressional approval legislatively, without the up-or-down vote to which trade promotion authority would lead.

My best guess is that the Bush administration is too weak politically to deliver on any broad trade liberalizing initiatives in the current, and probably also the next,

¹¹ To my knowledge, the only American-based study of how to enhance trade relations between Australia and the U.S. was the one done by my Center at Texas eight years ago; see R.G. Cushing, J. Higley, M. Sutton, T. Tompkins, and S. Weintraub, *The Challenge of NAFTA: North America, Australia, New Zealand, and the World Trade Regime*. Edward A. Clark Center for Australian Studies, Univ. of Texas at Austin, 1993.

Congress. This means that a legislatively approved FTA between Australia and the U.S. is the most likely prospect. We will learn its probability during the next three to four months.