CHAPTER 6

Liberalizing International Trade

SINCE THE SECOND WORLD WAR the United States has taken the lead in championing liberalized trade and open markets. A series of trade negotiations at a variety of levels has produced a world economy that is far more open, integrated, and efficient than that of the 1950s. For the global economy this has meant an extraordinary expansion of income, not only in the industrialized world but shared by those developing countries that were willing to promote international trade. For producers, trade liberalization has meant access to lower cost supplies and the ability to reap returns on investment over a much larger market. For consumers it has meant wider choices, higher quality, lower prices, and higher real incomes.

In the 1950s almost all trade was in commodities or manufactured goods, transported by sea, and trade barriers consisted of tariffs and quotas. Levels of trade protection were high, and negotiating reductions was relatively easy. Trade negotiations today are severalfold more difficult. Tariffs, which are easily observed and compared, are now much less important. Tighter integration among economies has shifted the emphasis of negotiations to domestic practices that inhibit trade, while new, nontariff trade barriers have been devised to take the place of those reduced through negotiation. Trade in intellectual property, technology-intensive goods, and a wide array of services has changed the product landscape, and trade now takes place among a much wider group of countries. In the 1990s, firms regularly operate subsidiaries in their major overseas markets, blurring the definition of what is a national firm. Their foreign direct investment has both pushed the expansion of trade and, in many industries, been pulled by the necessity to be in close touch with customers, so that rules governing foreign investment now have a direct effect on trade. All of these changes have made the pursuit of effective trade liberalization more challenging.

This Administration, like its predecessors, has responded to these changes by pursuing liberalization and the promotion of exports at a variety of negotiating levels. The American approach has been that of nondiscrimination: negotiated reductions in trade barriers should apply to all trading nations; individual nations should not cut deals that benefit themselves at the expense of others. This principle of U.S. diplomacy goes back to the Nation's early history as a new entrant in the trading world, but it has roots in both fairness and economic efficiency. Nondiscrimination as a goal received powerful support from the disastrous experience of discriminatory trade and payment regimes during the Great Depression. Often called the most-favored-nation (MFN) principle, since each participant receives the same treatment accorded the "most-favored nation," nondiscrimination formed the basis of the postwar trade order.

Even though nations will seek concessions by others in areas of most immediate interest to themselves, nondiscrimination makes trade liberalization a public good—what is produced by one country in negotiation with another is available to all. This gives rise to the coordination problem shared by all public goods, that of getting each party to participate rather than sit back and let others do the liberalizing, free-riding on their efforts. The solution to this dilemma requires commitment on the part of the major trading nations, coupled with ingenuity and the artful use of the fear of exclusion. Thus, while the United States has continued to support multilateral liberalization efforts, it has been forceful in bilateral negotiations as well, and has also pursued liberalization on a regional basis, both as a way of extending market opening and as a way of pressing for greater liberalization in the full multilateral arena.

This Administration has achieved remarkable success at each of these three levels of trade negotiations. After 7 years of negotiating and two missed final deadlines, the Administration brought the most ambitious of postwar multilateral negotiations, the Uruguay Round, to a successful conclusion. At the regional level the Administration brought about the enactment of the North American Free Trade Agreement (NAFTA) with Canada and Mexico, and has reached agreements to move toward free trade in the entire Western Hemisphere and in the Asia-Pacific region. At the bilateral level the Administration has concluded a number of agreements, the most important of them within the Framework for a New Economic Partnership with Japan.

In its first 2 years in office the Administration has achieved more in international trade policy than any other postwar administration. The agreements it has reached and implemented change the landscape of future trade issues. This chapter reviews those agreements and their consequences for the United States and the world trading order, and then explores the issues that will govern future trade relations.

MULTILATERAL INITIATIVES: THE URUGUAY ROUND AND THE WORLD TRADE ORGANIZATION

The Uruguay Round took a full 7 years (1986–93) to complete, and the resulting agreement is by far the most extensive and comprehensive yet concluded under the General Agreement on Tariffs and Trade, or GATT (Table 6–1). It goes beyond all previous GATT agreements in three respects (Box 6–1). First, it deals more directly and extensively with nontariff barriers to trade than any past agreement. Second, it brings several major product sectors under international trade rules for the first time. Finally, the agreement goes a long way toward establishing a single set of trade rules applicable to all member countries, limiting the ability of countries to pick and choose what trade obligations they will accept. The Uruguay Round agreement offers huge benefits for the United States and for the other signatories and will shape the future of multilateral trade negotiations.

TABLE 6–1.—*GATT Negotiating Rounds*

Negotiating round	Dates	Number of participants	Tariff cut achieved (percent)	Comments
Geneva	1947	23	73	
Annecy	1949	13		
Torquay	1951	38		
Geneva	1956	26		
Dillon Round	1960–61	26		
Kennedy Round	1964–67	62	35	Antidumping agreement signed
Tokyo Round	1973–79	99	33	Addressed nontariff as well as tariff barriers; codes (optional) on government procurement, dumping, subsidies, standards, and customs valuation
Uruguay Round	1986–93	125	40	Addressed nontariff as well as tariff barriers; covered new areas of agriculture, services, intellectual property; strengthened dispute settlement

Note.—Tariff cuts achieved are those agreed to by the major industrial countries on industrial products. The tariff cut achieved in the first five negotiations is an estimate. Tariffs fell from an average of about 40 percent at the time of GATT's founding to 7 percent by the beginning of the Tokyo Round.

Source: General Agreement on Tariffs and Trade.

TARIFF AND NONTARIFF MEASURES

Even in the traditional areas of trade negotiation the Uruguay Round marks a significant achievement. The agreement reduces average industrial product tariffs by 34 percent overall, and by 40 percent for industrial countries. Tariffs were eliminated entirely in "zero-for-zero" agreements in several sectors, including pharmaceuticals, steel, construction equipment, medical equipment, and paper. Overall, the Round is estimated to result in a $744 billion cut in world tariffs over the next 10 years. In addition, many countries agreed for the first time to bind (cap) a significant portion of their tariffs, giving up the possibility of future rate increases above the bound levels. The increase in tariff bindings among less devel-

Box 6–1.—Uruguay Round Highlights

Tariffs. The Uruguay Round agreement achieved a 34-percent average reduction of industrial product tariffs. Most of these tariffs are now bound (capped).

Agriculture. The agreement converts quotas and other trade restraints to bound tariffs. It requires cuts in export and domestic subsidies and minimum market access commitments.

Textiles and clothing. The agreement eliminates quotas on textile and clothing imports over a 10-year period.

Services. The agreement extends MFN treatment, national treatment, and other principles to service sectors in which countries make specific market-opening commitments. Specific sectoral commitments were negotiated or are being negotiated.

Intellectual property. Patent, trademark, and copyright protections are recognized as trade obligations and strengthened.

Rules governing trade. So-called voluntary export restraints are forbidden, and country-specific import safeguard measures are allowed only in limited circumstances. Antidumping procedures become subject to limited duration ('sunset') provisions and improved standards of transparency and procedural fairness. Subsidies are divided into categories: those prohibited outright, those subject to countervailing duties if they cause injury to producers in other countries, and those explicitly declared exempt from such duties.

Trade-related investment measures. Measures requiring foreign subsidiaries to achieve a specified minimum level of domestic content in their production or requiring that imports be balanced by equivalent exports, as well as certain other measures, are to be eliminated within 2 years for developed countries, and within 5 years for less developed countries.

"Single undertaking." With the exception of a few sectoral agreements, a single set of trade rules applicable to all signatories is established.

World Trade Organization (WTO). The agreement ends the ambiguous foundation for world trade that the GATT had provided, regularizing and creating a legal basis for previous GATT practice. The WTO provides a single umbrella for trade agreements in goods, services, intellectual property, and other areas.

Dispute settlement. Disputes involving all WTO matters are subject to a single dispute settlement process. Losers in a panel decision may take the matter to a new Appellate Body but no longer have the ability to block panel decisions. Retaliation is authorized in the absence of a settlement.

oped countries was striking: by the end of the Round 73 percent of their industrial product tariffs, covering over 60 percent of total imports, were bound.

The Round made significant progress in reducing or eliminating nontariff barriers. The government procurement agreement strengthens the provisions of the earlier Tokyo Round code, opening a wider range of markets for signatory countries. In addition, the Round made extensive efforts to eliminate quantity restraints on trade and require countries to rely instead on price (tariff) measures. In the textile and apparel sector, the various bilateral quotas that have arisen to control international trade are to be raised, and phased out entirely by 2005. In agriculture, quantitative restraints and other nontariff barriers to trade are to be replaced by tariffs of equivalent restrictiveness. Finally, the safeguards agreement prohibits the use of voluntary export restraints.

The elimination of quantity restraints on trade, even when replaced by tariffs that reduce trade by the same amount, is an important liberalizing step. With a quota, when imports reach the quota limit, the domestic market is completely insulated from foreign competition. Quotas effectively carve up the market, whereas tariffs maintain competition. The anticompetitive effect is most striking if domestic producers collude to raise prices. Under a quota, imports cannot respond and thus provide no brake on domestic price increases, whereas under a tariff, imports increase at the tariff-inclusive price, limiting the ability of producers to raise prices.

NEW SECTORS

The Uruguay Round achieved significant liberalizations in the traditional areas of trade negotiations, but what made it a breakthrough agreement was its extension of trade disciplines to three new areas: agriculture, services, and intellectual property.

Agriculture

The Uruguay Round for the first time brings agriculture, a sector that accounts for 13 percent of world trade, under international trade rules. Measures to support farm incomes in the industrial countries have led to a variety of trade-restraining measures, excess production, and an expensive system of export subsidization that has done little to increase world demand for agricultural products but has greatly depressed world agricultural prices.

The agriculture agreement requires that nontariff barriers to agricultural trade be converted to their tariff equivalents, and that the resulting tariffs be reduced by a minimum of 15 percent in each tariff line and by an average of 36 percent overall. Countries are also required to grant minimum market access in products where there has been little or no trade. This means the end of the bans on rice imports in Japan and the Republic of Korea, and commitments by all countries to increase wheat, corn, rice, and barley imports by a total of 3.5 million metric tons.

The agreement also contains first steps to reduce agricultural subsidies. Export subsidies must be reduced by 36 percent in value from 1986–90 levels over 6 years, and the volume of subsidized exports by 21 percent. Since current U.S. and European subsidy levels exceed this base, the actual reduction will be considerably higher. Domestic subsidies that increase output must be reduced by 20 percent from their 1986–90 levels.

Since the United States has a strong underlying comparative advantage in agriculture, the mutual reduction in trade barriers and subsidization will be to the distinct advantage of U.S. producers. Because European export subsidization in the base period used for calculating reductions was 14 times that of the United States, and domestic support 4 times as great, the European Union's subsidy reductions will dwarf those of the United States. As a result of world income gains and the realignment of world sales due to the Uruguay Round agreement, annual U.S. agricultural exports are expected to increase by somewhere between $4.7 billion and $8.7 billion by 2005.

Services

The second new area opened by the Uruguay Round is international trade in services. This trade has grown to $1 trillion per year and now accounts for over a fifth of all international trade. Services trade liberalization is of major concern to the United States, the world's largest services exporter, with annual exports of over $170 billion and a surplus of $59 billion in 1993.

The General Agreement on Trade in Services (GATS) is the first multilateral agreement covering services trade issues. The GATS has two distinct components. The first is a general statement of principles, such as national treatment and MFN treatment, that cover trade in services, along with descriptions of how these are to be interpreted in individual sectors (Box 6–2). Recognizing the differing ways in which services trade can take place, the GATS covers cross-border trade, movement of persons, and investment issues. The agreement creates a general obligation to offer MFN treatment to signatories, requires transparency in regulation of services, and brings services trade disputes under the general dispute settlement mechanism of the WTO.

The first component of the services agreement does not in itself create any liberalization of services trade. Liberalization is provided in the second component, where each country lists the sectors to which it will apply GATS obligations, as well as any exceptions to those obligations that it will maintain in each sector. Once a sector and its exceptions are listed, those commitments are bound,

Box 6–2.—National Treatment, MFN, and Market Access Under the GATT and the GATS

The fundamental principles on which the GATS is based mirror in many ways those applied to goods within the GATT, but there are some important differences.

Most-Favored-Nation Treatment

GATT: A country agrees to treat goods from other GATT members no less favorably than it treats those from any other foreign supplier, on tariffs and other measures that affect the import or export of goods.

GATS: Identical, except that there is a one-time opportunity to exempt specific service sectors from MFN obligations, for a period of up to 10 years.

National Treatment

GATT: Once foreign goods have entered a country and paid any tariffs or other customs duties, they must be treated no less favorably than domestically produced goods, and subject to no taxes or charges that are not also levied on domestically produced goods.

GATS: The same, but only for sectors listed by countries in their sectoral commitments, and subject to any exceptions listed in those commitments.

Market Access

GATT: No obligation.

GATS: No explicit definition. However, countries agree *not* to impose various limitations (on total value or quantity, extent of foreign investment or ownership, or number of persons employed) in sectors in which they make commitments.

and no further limitations on trade may be applied. The sectoral commitments, although neither as extensive as originally sought by the United States nor as far-reaching as those under NAFTA, do contain important liberalizations. Most country commitments include a standstill on new barriers, which is significant in many countries where services sector regulation is just beginning to develop. Countries made broad commitments in trade in professional services and tourism and agreed not to restrict access to telecommunications services to resident foreign-owned service providers. Negotiations on specific commitments in financial services, basic telecommunications, and maritime transport services were not completed by the end of the Round and are to continue. Despite the negotiations that remain, the GATS is a breakthrough, not only for the specific liberalizations that it contains but also because it establishes the framework for further liberalization of trade in services, just as the GATT did for goods in 1947.

Intellectual Property Protection

The extension of multilateral trade rules to intellectual property protection is a further area where the Uruguay Round broke new ground. The Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs) adopts and strengthens existing conventions on intellectual property, adds protection for several new areas including integrated circuits and computer software, and provides a mechanism to enforce intellectual property rights. It also extends national and MFN treatment to intellectual property holders. The agreement, with just a few exceptions, eliminates the ability of countries to deny patentability to certain categories of inventions such as pharmaceuticals and restricts forced licensing of technology.

Enforceability was a major concern in the negotiation. Principles of intellectual property law are set out in the agreement, along with requirements for transparency in application procedures, and disputes are covered in the general WTO dispute settlement mechanism. In return for substantial concessions on protection and enforceability, less developed countries received a lengthy transition period: 5 years for most of these countries and 11 years for the least developed ones.

WIDENING PARTICIPATION

A failing of past trade negotiations was the limited number of countries that were active negotiating participants—many countries remained on the sidelines as free riders on others' liberalizations. Moreover, by the time the Uruguay Round was launched, GATT obligations had become a kind of a la carte system, where countries were free to subscribe to the agreements they chose and abstain from others. The Uruguay Round reversed this trend, both increasing the number of countries making concessions and achieving a much greater uniformity in the rights and obligations of GATT (now WTO) members.

The increased participation of countries in the negotiations was in large part due to a sea change in ideology in developing countries in favor of privatization, economic liberalization, and competition, as described in more detail below. But it also had much to do with the fact that the Uruguay Round was a "grand bargain," linking concessions by less developed countries on tariffs, services, and intellectual property with liberalization of trade in textiles, apparel, and agriculture.

The Uruguay Round has also done much to establish a single rulebook for international trade competition. In contrast to previous negotiations the outcome of the Uruguay Round, and WTO membership, is a single undertaking. With few exceptions (notably the agreement on government procurement), countries joining the WTO agree to all of its obligations—the GATT itself, the GATS, the TRIPs agreement, dispute settlement procedures, and others. Finally, the increasing perceived value of trade liberalization in many market economies and the breakdown of central planning in the economies in transition have resulted in a large number of new applicants for WTO membership, including China and Russia. Their accession negotiations require both adoption of WTO obligations and initial liberalization of trade, expanding the number of countries trading by a single set of rules.

DISPUTE SETTLEMENT

Strengthening the GATT dispute settlement mechanism has been a longstanding goal of the United States; indeed, it was listed first among the principal U.S. negotiating objectives in the Omnibus Trade and Competitiveness Act of 1988. The previous GATT dispute mechanism suffered from long delays, the ability of accused parties to block decisions of GATT panels that went against them, and inadequate enforcement. The dispute settlement agreement addresses each of these issues. It guarantees the formation of a dispute panel once a case is brought and sets time limits for each stage of the process. The decision of the panel may be taken to a newly created Appellate Body, but the accused party can no longer block the final decision. A country that loses a dispute must either bring the offending practice into conformity, offer suitable compensation to the aggrieved parties, or face retaliation, which is now authorized under the agreement. Furthermore, this strengthened mechanism now becomes the single dispute settlement mechanism for the WTO, covering the GATT, the GATS, the agreement on intellectual property, and other agreements.

The dispute settlement issue has been important to the United States because this country has been the most frequent user of the GATT dispute mechanism. Frustration with the old mechanism was one of the factors behind the development and use of Section 301 of the Trade Act of 1974, which allows the United States to retaliate against "unjustifiable" or "unreasonable" foreign practices that hinder U.S. commerce. The new dispute settlement mechanism changes the sequence in which Section 301 is used but does little else to limit its use. Section 301 requires that, if a case involves an existing trade agreement, the United States must use the dispute settlement provisions of that agreement. If the United States wins a WTO case, and if the losing party does not then change its practice or offer suitable compensation, Section 301 retaliation is authorized by the WTO.

Perhaps the most important use of Section 301 has been in the promotion of U.S. interests in cases not covered by multilateral trade rules, such as services and intellectual property in the past. Here Section 301 can be used as before both to promote U.S. interests and to prompt multilateral negotiations on new liberalization. Even with modifications in the use of the legislation, the *package* of the new dispute settlement mechanism plus Section 301 is a far stronger vehicle for defending U.S. interests. A strengthened dispute settlement mechanism and multilateral backing for retaliation greatly increase the leverage the United States will have in protecting its trading rights.

THE WORLD TRADE ORGANIZATION AND U.S. SOVEREIGNTY

The GATT of 1947 was unusual in that it started out as a trade agreement, not an organization. Through improvisation and experience its small secretariat became an effective coordinating body for multilateral trade negotiations. The Uruguay Round establishes a World Trade Organization to bring under a single umbrella a variety of trade agreements negotiated under GATT auspices along with the single dispute settlement mechanism, and to regularize and clarify the practice that had been built up under the GATT. Although both the single undertaking and strengthened dispute settlement were U.S. objectives in the Round from the beginning, their achievement and the creation of the WTO have raised fears in some quarters that the United States might be surrendering sovereignty to an international organization over which it would have little control.

These fears are unwarranted. The WTO is an administrative body, designed to facilitate trade negotiations and dispute settlement among its members, not a legislature for creating obligations. Its charter explicitly links it to the decisions and customary practice under the GATT, including the dependence on consensus in reaching decisions. Although the principle of one country, one vote has always characterized the GATT, in fact GATT votes were almost never taken; decisions were reached on the basis of consensus among members. In practice, the United States has always had a major influence over the course of GATT policy, not because it has had a larger formal vote but, in baldest terms, because it brought the largest market to the table. The WTO does not change this. What the WTO does is to define fallback requirements if consensus is not reached. These are both limited in scope and stringent. Interpretations of agreements and waivers of obligations require a three-fourths majority of the entire membership (not just of those voting), and the creation of a new obligation on a country is possible only if that country accepts it. In any case, each member has the ability to leave the WTO with 6 months' notice.

The most fundamental reason why U.S. sovereignty is not diminished by the WTO is that WTO agreements and dispute panel decisions do not have legal force in the United States (or in other member countries)—they are not "self-actuating." In situations where existing U.S. legislation is contravened or new legislation required, it is up to the Congress whether to take that action. If the United States were to lose a dispute panel decision on a matter of fundamental national interest, it need not bring U.S. law or practice into conformity. The United States could instead offer compensation through liberalization in other areas, or accept equivalent foreign retaliation through increased barriers to U.S. exports. Panels rule on disputes that arise on rules and disciplines that WTO members have agreed to; they do not create new obligations. Furthermore, U.S. negotiators were particularly careful to limit the scope of panel review in cases involving national health and safety standards.

To allay concerns about the operation of the WTO, the Administration supports the establishment of a WTO Dispute Settlement Review Commission. The commission, which will consist of five Federal appellate judges, will review all final WTO dispute settlement reports adverse to the United States to determine whether the panel has exceeded its authority or acted outside the scope of the agreement. Following three determinations by the commission in any 5-year period that panels have so exceeded their brief, any member of the Congress may introduce a joint resolution to disapprove U.S. participation in the WTO. If the resolution is enacted by the Congress and signed by the President, the United States would withdraw from the WTO. By focusing informed, high-level attention on the operation of the WTO, the review commission should help develop a fair, effective, and widely accepted dispute settlement system within the organization.

Of course, the Uruguay Round agreement and the WTO do place obligations on the United States, but the balance of obligations in this accord is favorable, both because the United States had considerable influence on the Uruguay Round outcome, and because this country has a transparent, rules-based system and the WTO represents a convergence toward a system of this type. This point is important to consider when weighing the strengthened dispute settlement apparatus of the WTO. As with any legal institution, the force of dispute settlement will be established through use and experience. The U.S. interest in strengthening a rules-based international trading system implies that the United States should actively bring cases to dispute settlement and, in general, abide by the results. This is not to say that the United States should ignore fundamental national interests in deciding whether to implement a WTO panel decision, but simply that our willingness to be bound by international trade disciplines will in large part determine whether those disciplines will be observed by others.

FUTURE MULTILATERAL NEGOTIATIONS

The Uruguay Round of multilateral trade negotiations was such an ambitious and far-reaching undertaking that much of the multilateral trade agenda for the next few years will consist of developing experience with the agreement. Nonetheless, there are a few sectors where negotiations still need to be completed, new areas opened up by the agreement that need to be fleshed out, and areas that were not covered in the Round that will clearly form the basis of the future multilateral trade agenda.

Four sectoral negotiations in services were incomplete at the end of 1993 when the Round was drawn to a close: financial services, basic telecommunications, audiovisual services, and maritime transport services. In both financial services and basic telecommunications, a U.S. commitment to national treatment under the services agreement and a standstill on new measures would commit our vast and generally unrestricted markets to foreign competition. Therefore, in exchange, the United States has insisted on a relatively high level of liberalizing commitments by its trading partners as part of any agreement.

Although agreements were reached in other service sectors, liberalization in services generally is still in its infancy. Further bargaining on specific service sector liberalizations will take up much of the trade agenda for the next several years. The Uruguay Round agreement also sets the stage for continued negotiations on agriculture, covering further reductions in subsidies and tariff rates, and expansion of the volume of imports subject to lower duties under tariff-rate quotas.

The trading world rarely stands still for a negotiation to conclude, and certainly not for one that lasted as long as the Uruguay Round. New trade issues have arisen in the interim that will occupy trade negotiators. The most prominent of these—trade and the environment, competition policy, investment rules, and labor standards—are described in more detail below. In many cases these issues arose in regional and bilateral negotiations, to which this discussion now turns.

PLURILATERAL INITIATIVES

Possibly the most distinctive legacy of this Administration in international trade is the foundation it has laid for the development of open, overlapping plurilateral trade agreements as stepping stones to global free trade. The Administration's plurilateral initiatives in North America, the rest of the Western Hemisphere, and Asia embody principles of openness and inclusion consistent with the GATT. They will serve as vehicles for improving access to foreign markets and easing trade tensions, and as models for future multilateral liberalization through the WTO in areas such as intellectual property rights, services, investment, and environmental and labor standards.

DYNAMIC EMERGING MARKETS

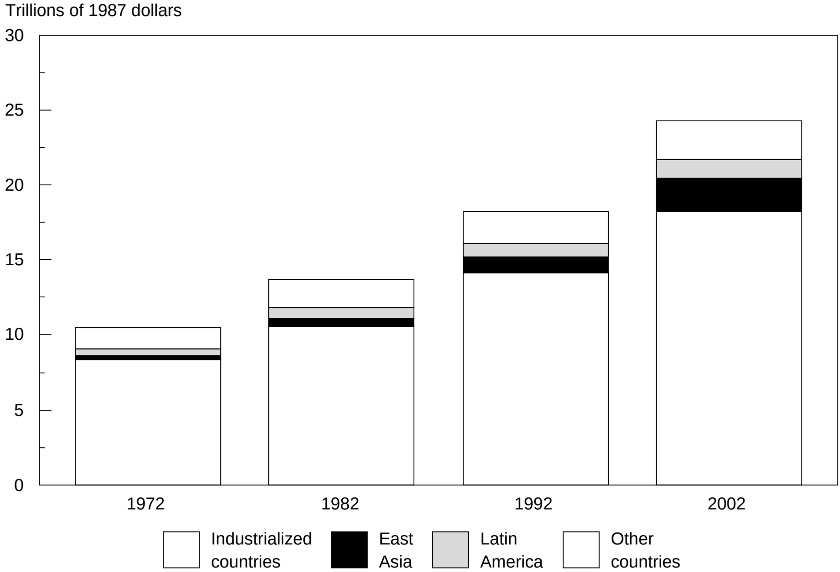
The recent U.S. emphasis on regional agreements responds to a massive shift taking place in the global economy. The economies of the world have long been categorized as either industrialized or less developed economies. Today, however, these distinctions are becoming obsolete as emerging economies in Asia, Latin America, and elsewhere are quickly approaching the ranks of the rich, industrialized countries. In the future these emerging economies are expected to grow rapidly and generate a larger share of world output and trade. The World Bank forecasts that developing economies will grow by 60 percent over the next decade, double the growth forecast for the industrialized countries. The share of gross world product produced in developing countries is expected to reach one-quarter by 2002, up from roughly one-fifth in 1972 (Chart 6–1). And purchasing-power-parity estimates, a more accurate method of making comparisons across countries, would attribute an even greater share of world output to developing countries.

Export and investment opportunities in emerging markets in Latin America and Asia will be a key engine of growth for the U.S. economy over the next decade. Exports are projected to grow far faster than other components of U.S. national income over that period. And this trend is already apparent. Over the last 7 years, U.S. exports of goods and services accounted for over one-third of economic growth, and export-related jobs grew over five times faster than total employment.

Much of this dynamism is driven by demand from newly industrializing and developing countries. Exports to emerging markets in Latin America and Asia are growing much faster than those to our traditional export markets. Already, U.S. exports to developing countries exceed exports to our traditional customers, Europe and Japan. This trend will continue, since emerging Asian and Latin American economies are expected to grow more than twice as fast as Europe and Japan.

Both Latin America and Asia are seeing a virtual explosion in the number of households with middle-class incomes and consumption patterns. By one estimate, China, India, and Indonesia will to-

Chart 6-1 **Income Growth in Industrialized and Developing Countries**
The share of world income received by developing countries is expected to reach one-fourth by 2002.



Source: International Bank for Reconstruction and Development.

gether have over 700 million middle-class consumers by the year 2010. That is roughly the current population of the United States, Europe, and Japan combined. As consumers in emerging markets join the middle class, their demand for household goods will soar, whereas in the United States and Europe most households already own such goods.

The rapid growth rates of emerging economies reflect a combination of factors, including technological catch-up to the most industrialized countries and, in many Latin American countries, recovery from the recessions associated with overindebtedness in the first half of the 1980s. More generally, economic theory predicts that lower income countries will grow faster than those with higher incomes, provided they are following sound economic policies. Because lower income countries have less infrastructure and plant and equipment, additional investments will be particularly productive. Less developed countries can also adopt and adapt technology that has already been discovered and developed in the rich countries. But there are prerequisites to taking advantage of additional capital and technology, among them stable political systems and sound economic policies. Broad access to primary education, an open economy, and sound macroeconomic policies all contribute to strong growth.

The most dynamic emerging economies have generally embraced market-oriented economic policies and opened themselves to the world economy. Not only have they lowered barriers to trade and investment, but they have adopted stable fiscal and monetary policies and transparent regulations. Many have also succeeded in improving the educational attainment of their work forces and have benefited from high rates of saving and accompanying high rates of investment. Sound economic policies will enable these countries to continue to take advantage of world capital flows and technological advances from abroad.

This rapid economic growth creates a number of opportunities for the United States. First, demand for U.S. products rises as the worldwide market grows. Many of these emerging economies will have particularly large demands for investment goods, transportation systems and products, infrastructure, environmental technologies, information systems, energy technologies, and financial services. These are all sectors in which the United States is particularly competitive.

In addition, countries that are growing rapidly are likely to invest more than they save. As long as they enjoy high growth rates and pursue sound economic policies, foreign capital will be readily available to finance this excess of investment over saving. Greater capital inflows in turn will permit greater imports from strong exporting countries such as the United States. Larger markets will also allow firms both in the United States and abroad to exploit greater economies of scale, as their fixed costs are spread across greater sales.

The Administration's regional initiatives in the Americas and in the Asia-Pacific community are critical for placing the United States squarely at the fulcrum of two of the most dynamic regions in the world.

REGIONAL BLOCS AS BUILDING BLOCKS

From a purely economic point of view, the effects of increased regional integration are well understood. The establishment of principles and dispute resolution procedures governing international transactions regularizes and improves the environment for intraregional flows of goods, services, and investment. A plurilateral trade agreement generates an increase in trade among member countries, due to reductions in the cost of importing from each other that are associated with lower tariffs and enhanced market access. Thus, for example, in 1993, 55 percent of the trade flows of countries that belong to the European Union (EU) involved other EU member markets. In general, cheaper imports and more efficient production patterns should improve the well-being of the participating countries. But plurilateral liberalization may also reduce trade with countries that are not members, since imports from nonmember countries do not benefit from the reduction of trade barriers. Trade diversion arises when members of a plurilateral trade arrangement switch from importing goods from the lowest-cost nonmember market to importing from members, even though the tariff-free cost of the goods in nonmember countries is lower than that in member countries. The beneficial trade creation effects are more likely to outweigh the harmful trade diversion effects if barriers to imports from nonmember countries are not allowed to rise—a condition that is codified in Article XXIV of the GATT.

Trade creation is also more likely to outweigh trade diversion when the "natural" costs of trade such as freight and insurance are low among members, because of geographical proximity or shared borders, and high between members and nonmembers. In general, countries trade the most with countries that are geographically close: proximity and shared borders lower transportation costs and thereby lower the total cost of imports. It is for this reason that plurilateral agreements are so often regional in nature.

Plurilateral trade initiatives generally take one of two forms. Customs unions, like the European Union, require members to remove all barriers to trade with other member countries and to maintain a common external tariff toward nonmember countries. As a member of a customs union, when Germany wants to change its tariffs on imports from nonmembers, it must first persuade France, Spain, and all the other EU members to do the same. In contrast, free trade areas such as NAFTA liberalize internally but do not impose any restrictions on members' external trade policies.

Stumbling Blocks

Traditionally, economists have voiced concerns that an increased emphasis on plurilateralism might divert attention and energy away from multilateralism and result in harmful trade diversion. And indeed, certain types of preferential trade agreements can undermine the multilateral system.

In general, preferential trade agreements that reduce the discretion of member countries to pursue trade liberalization with nonmembers are more likely to become stumbling blocks. Thus, for instance, members of customs unions are unable either to negotiate tariff reductions with nonmembers individually or to reduce external tariffs unilaterally. In contrast, NAFTA allows its members to enter into trade agreements with outsiders, and indeed Mexico has negotiated separate free trade agreements with several other Latin American countries since signing NAFTA.

In addition, as a bloc expands, its bargaining power in international negotiations and its market power in international commerce grow, especially if it imposes a common external tariff. This may have the undesirable effect that the bloc finds it advantageous to increase barriers to outsiders. These harmful effects are unlikely to arise in a free trade area as opposed to a customs union, and when external barriers are constrained by WTO disciplines.

Building Blocks

When structured according to principles of openness and inclusiveness, regional blocs can be building blocks rather than stumbling blocks for global free trade and investment. Seen in this light, carefully structured plurilateralism is a complement rather than an alternative to U.S. multilateral efforts.

There are a variety of ways in which plurilateral agreements can serve as building blocks for multilateral market opening. First, plurilateral accords may achieve deeper economic integration among members than do multilateral accords because the commonality of interests is greater and the negotiating process simpler. The multilateral framework of the WTO achieves liberalization by requiring each member to extend any new trade preferences to all trade partners on a nondiscriminatory basis. Although this principle is intended to generate broad liberalization across countries, it may have the unintended effect that countries are less willing to offer concessions to certain of their trade partners because they must then offer the same concessions to over 100 other countries. Plurilateral agreements, by achieving both greater depth and breadth in their disciplines, can support the multilateral system by forging ahead on issues that are likely to be incorporated in future multilateral negotiating rounds.

Second, a self-reinforcing process is set in place by the creation of a free trade area. As the market encompassed by a free trade area expands, it becomes increasingly attractive for outsiders to join in order to receive the same trade preferences as member countries. Companies from nonmember countries find themselves at an increasing competitive disadvantage as the free trade area expands, and they petition their national governments to apply for membership.

Third, plurilateral liberalization encourages partial adjustment of workers out of the import-competing industries in which the country's comparative advantage is weak, and into exporting industries in which its comparative advantage is strong. As adjustment proceeds, the portion of the work force that benefits from trade expansion and liberalization rises, and the portion that loses out declines, which in turn builds political support for liberalization in a self-reinforcing process.

For all of these reasons, when plurilateral agreements are structured according to principles of openness, they tend to overlap and expand, building toward global free trade from the bottom up.

Open Regionalism

Open regionalism refers to plurilateral agreements that are nonexclusive and open to new members to join. It requires first that plurilateral initiatives be fully consistent with Article XXIV of the GATT, which prohibits an increase in average external barriers. Beyond that, it requires that plurilateral agreements not constrain members from pursuing additional liberalization either with nonmembers on a reciprocal basis or unilaterally. Because member countries are able to choose their external tariffs unilaterally, open agreements are less likely to develop into competing bargaining blocs. Finally, open regionalism implies that plurilateral agreements both allow and encourage nonmembers to join. This facilitates the beneficial domino effect described above.

To ensure that its plurilateral initiatives strengthen the multilateral trading system and enhance market opening globally, the United States is pursuing a policy of open regionalism. The Administration is working to lay the foundations for a world with several overlapping, open plurilateral arrangements, with the United States playing a leadership role in North America, Asia, and Latin America, rather than two or three competing blocs.

THE NORTH AMERICAN FREE TRADE AGREEMENT

On January 1, 1994, a historic trade agreement between the United States, Canada, and Mexico went into force. In both the level and the scope of the disciplines covered, NAFTA is the most far-reaching and forward-looking trade agreement ever adopted by these three countries. NAFTA provides for phased elimination of tariff and most nontariff barriers for both industrial and agricultural products, protection of intellectual property rights, investment rules, liberalization of services trade, and an innovative dispute settlement mechanism (Box 6–3).

The Economic Effects of NAFTA

It is far too early to evaluate the full economic impact of NAFTA, since the provisions have been in place for only 1 year and many of the measures are being phased in over 10 to 15 years. There is a widespread consensus that NAFTA's overall net impact will be positive. But it is important to keep in mind that Mexico's GDP is only about 4 percent that of the United States, and that the United States had a preexisting free trade agreement with Canada when NAFTA was signed.

There are a number of reasons why NAFTA will benefit the United States. First, prior to NAFTA, Mexico had trade barriers that were 2.5 times higher on average than those in the United States. Thus it is Mexico that will undertake the greater reduction in trade barriers. Second, although investment barriers in Mexico have been

Box 6–3.—NAFTA Highlights

- Phaseout of most tariffs and nontariff barriers in industrial products over 10 years, including for all textiles and apparel that have substantial regional content
- Phaseout of tariffs and most nontariff barriers in agricultural products over 15 years
- Investment rules ensuring national treatment, eliminating most performance requirements in all sectors, and reduced barriers to investment in the Mexican petrochemicals and financial services sectors
- Liberalization of financial, land transportation, and telecommunications services markets
- Mechanisms for enforcement of national labor and environmental laws
- A dispute resolution mechanism
- Protection of intellectual property rights
- Funds for environmental cleanup and community adjustment along the border

lowered, making it easier to establish operations there, the fact that trade barriers are also being reduced makes investment in Mexico less necessary. Evidence suggests that most U.S. direct investment abroad is intended to gain market access, not to exploit low-wage workers or lax regulations. And indeed, some U.S. investments in Mexico have already increased U.S. exports dramatically. For instance, one major U.S. discount store chain has opened 9 stores in Mexico. The chain's Mexico City store alone sells $1 million worth of merchandise on an average weekend, most of which is imported directly from the United States.

Third, although wages are lower in Mexico than in the United States, the productivity of Mexican workers is also lower than that of U.S. workers. Moreover, companies make plant location decisions based on a variety of factors in addition to wages, including telecommunications and transportation infrastructure and business services, all of which are more sophisticated in the United States.

Perhaps most important is the simple fact that trade liberalization encourages specialization that benefits both countries. Thus, while NAFTA is expected to raise production in Mexico of goods that require a lot of low-skilled labor hours, there should be a concomitant increase of production in the United States of goods that require highly skilled labor. Specialization allows both types of goods to be produced more cheaply, lowering the cost of living for the population on both sides of the border. Moreover, increased trade and investment associated with NAFTA should result in higher income in Mexico, which in turn will translate into greater demand for U.S. exports, and increased investment and employment in export industries in the United States.

Although the beneficial effects will take years to manifest themselves fully, the results to date confirm the view that NAFTA is good for the United States, Mexico, and Canada. So far there is little evidence of the sucking sound that critics had alleged would accompany NAFTA. Indeed, the sounds most associated with NAFTA are those of trains, trucks, and ships loading cargo bound for destinations across the border. Overall, U.S. exports to Mexico grew by 21.7 percent in the first three quarters of last year over the same period in 1993—more than twice the growth rate of U.S. exports overall. Imports from Mexico have also increased by 22.8 percent, but much of this import growth is associated with the strength of the economic recovery in the United States during the period, and would most likely have taken place in the absence of NAFTA, since U.S. barriers on many Mexican imports were already low.

While the rapid growth in trade between the United States and Mexico testifies to the opportunities created by NAFTA, it is important to emphasize that the bilateral balance of trade is not a scorecard by which to judge the success or failure of the agreement. The United States gains from its imports from as well as its exports to Mexico, from the ability to specialize and compete more effectively in world markets, and from the opportunities opened up to U.S. firms in Mexico as it develops. Trade between the two countries will grow rapidly, but the trade balance will fluctuate, depending on macroeconomic conditions in the two countries, just as the rapid growth in the U.S. economy boosted U.S. imports during the past year.

The NAFTA also benefits the United States through the more prosperous and stable Mexico that it fosters. This is particularly important, since the United States and Mexico are so closely linked by geography as well as economy. As Mexican wealth and political stability increase, the result is not only a larger market for U.S. exporters, but also higher environmental standards and reduced illegal immigration.

NAFTA and the Peso

On December 22, 1994, the Mexican Government decided to abandon the fixed exchange rate between the Mexican peso and the dollar, allowing the peso to float. The decision came after intense pressure on the peso in foreign exchange markets had severely depleted Mexico's international reserves. The pressure resulted from Mexico's inability to finance its large current account deficit, which reached almost $30 billion in 1994, or about 7.6 percent of GDP.

Following Mexico's debt repayment problems in the early 1980s, its government pursued a course of macroeconomic stabilization that included fiscal restraint, wage and price restraints, and a target range for the dollar value of the peso. As part of its inflation-fighting measures, starting in the late 1980s, the government adjusted the target range for the peso more slowly than the rate of inflation. By 1994 the peso had appreciated significantly in real terms, making foreign goods cheaper for Mexican consumers. Real appreciation was accompanied by increasing trade and current account deficits, which were financed by borrowing from foreign investors, a large portion of which took the form of short-term portfolio investment. As the Mexican presidential election approached in 1994, an uprising in the State of Chiapas and the subsequent assassination of the ruling party's candidate contributed to investor uncertainty. As investors lost confidence and the inflow of portfolio capital dried up, the government found it increasingly difficult to maintain its exchange-rate policy, and eventually it decided to let the market determine the value of the peso.

Shortly afterward, the Mexican Government announced a comprehensive economic plan to restore confidence and stabilize the economy. At the request of the Mexican Government, the United States organized a financial stabilization package of $18 billion designed to restore investor confidence and give the Mexican Government breathing room to implement its economic package. The package included multilateral and private sector participation.

However, despite the decision to float the peso and the announcement of the international support package, pressures on the peso continued. Investors became increasingly reluctant to roll over maturing short-term obligations of the Mexican Government and, in some cases, of Mexican banks. The flight from Mexican assets also showed signs of spreading to other emerging markets.

In order to restore confidence in emerging financial markets, the President decided to expand U.S. financial support for Mexico to $20 billion. The U.S. support includes short- and medium-term swaps (an exchange of dollars for pesos for a specified period of time) and longer term loan guarantees. The Treasury's Exchange Stabilization Fund is providing a substantial portion of this support. In addition, the Federal Reserve is providing a part of the support, in the form of short-term swaps. These guarantees and swaps are structured to provide maximum protection for U.S. assets and to encourage the Mexican Government to return to private sector financing as soon as possible. In order to make use of the guarantees, the Mexican Government will be required to pay large up-front insurance fees. All drawings will be backed by claims on the proceeds from oil exports. The swap facility must be fully repaid; it is not a grant. The United States has had a swap line with Mexico for over 50 years, and Mexico has repaid all of its drawings.

Additional financial support will come from a variety of sources. The International Monetary Fund (IMF) made a commitment to provide a total of $17.8 billion, from a combination of its own resources and contributions from member countries. The Bank for International Settlements committed $10 billion in short-term financing, Canada committed itself to provide a $1 billion swap facility, and Argentina and Brazil committed themselves to arrange $1 billion in financial assistance to Mexico.

Together, these resources will enable the government of Mexico to refinance its debt and shift to longer term maturities, thereby easing the current liquidity squeeze. The support package imposes stringent financial conditions. Mexico must implement an economic plan that includes reductions in government spending, an incomes policy to reduce inflation, and tight control of credit. Mexico has also pledged to accelerate the privatization of key industries and increase access for U.S. and other foreign investors. These measures are designed to ensure that Mexico will be able to restructure and service its debt and to restore economic stability and growth.

It is also important to understand that NAFTA neither contributed to the peso devaluation nor in any way affected the U.S. Government's response. Indeed, the NAFTA measures adopted by Mexico to lock in market reforms and provide safeguards for foreign investors have, if anything, shored up investor confidence and mitigated the peso depreciation. The United States is providing support to Mexico because we have a stake in the stability of a country with whom we share a 2,000-mile border and important commercial ties. There is no commitment under NAFTA to do so.

NAFTA Side Agreements

NAFTA includes three innovative side agreements that reflect the Administration's commitment to ensure that expanded trade does not result in deterioration of environmental or labor standards on either side of the border or in damaging import surges. The labor and environmental side agreements define guiding principles and create institutions to ensure that each member country enforces its own laws protecting labor and the environment. They are described in detail below. The side agreement on import surges creates an early warning mechanism to identify sectors where rapid growth of imports is likely to generate significant dislocation of domestic workers. If a domestic industry is threatened by serious injury from an import surge during the NAFTA transition period, a temporary snapback to pre-NAFTA duties is permitted as a safeguard. However, if exports from a NAFTA member do not account for a substantial share of total imports or do not contribute significantly to the threat of injury, the member country's exports must be excluded from safeguard actions.

Adjustment

Although the United States chose to join NAFTA because it will benefit U.S. consumers, shareholders, farmers, and workers generally, it was also recognized that some jobs in some industries would be threatened by increased imports from Mexico. NAFTA contains a number of provisions intended to mitigate these adjustment costs. First, the elimination of trade barriers is phased in over 10- to 15-year horizons in industries where liberalization is expected to require significant adjustment. Second, there are safeguard provisions (described above) permitting the temporary imposition of trade restrictions when surges in imports cause serious injury to a domestic industry. Third, the U.S. implementing legislation established a Transitional Adjustment Assistance (TAA) program for workers who experience or are threatened with job loss or reduction to part-time status as a direct result of either increased imports from or a shift of production to Mexico or Canada, to help them retool and reengage. There is no requirement that the dislocation be directly related to NAFTA, although it must have occurred after NAFTA went into effect. Assistance includes employment services, training, income support following exhaustion of unemployment insurance, job search allowances, and relocation allowances.

As of November 1, 1994, the NAFTA-TAA program had approved assistance for over 12,000 workers. In two-thirds of these cases, the dislocation was associated with either a shift of U.S. production to or increased imports from Mexico. Eighty-eight percent of the NAFTA-TAA-certified layoffs were in manufacturing firms, 9 percent were in agriculture, and 3 percent were in services industries. Within manufacturing, the apparel, industrial machinery and equipment, electronic and other electric equipment, and instruments and related products industries accounted for 72 percent of the certified layoffs. Most of the firms that have qualified for NAFTA-TAA so far are smaller manufacturers producing apparel or parts and components with either less skilled workers or less sophisticated factory equipment.

The NAFTA-TAA program indicates that increased trade with Mexico and Canada has had an adverse effect on some workers, although the number of job losses has been small relative to the 100,000 jobs estimated to have been created through expanded exports to Mexico. Reemployment data on NAFTA-TAA-certified workers are not yet available, so it is too early to tell how long-lived the job displacement effects will be. However, it is important to recognize that layoffs and other displacements are a constant feature of the U.S. economy, and that relative to overall annual job losses for workers with over 3 or more years on the job (1.5 million per year on average between 1991 and 1993), the displacement associated with NAFTA is very small.

NAFTA and Open Regionalism

NAFTA is both the United States' most significant plurilateral initiative to date and a likely model for such initiatives in the future. As such, it is worth noting that NAFTA is consistent with open regionalism along all the dimensions discussed above. First, it explicitly prohibits any increase in external barriers, and indeed external barriers in all three of the member countries are scheduled to fall as part of the Uruguay Round agreement. Second, it imposes no constraints on the ability of member countries to lower their barriers to nonmember countries, and indeed Mexico has granted trade preferences to several nonmember countries since the agreement was signed. And third, NAFTA contains a provision specifying that the members can choose to admit additional members. Indeed, the President, together with the Prime Minister of Canada and the President of Mexico, announced the start of accession negotiations with Chile in December 1994.

SUMMIT OF THE AMERICAS

On December 9, 1994, the President convened the first-ever hemispheric summit held in the United States—and the first to be attended solely by democratically elected leaders. The summit celebrated an unprecedented conjuncture in the hemisphere's history. For the first time, all 34 leaders share a common commitment to democracy and open markets. Many of the Latin American leaders have put their countries on a course of stable, sustainable economic growth by taking difficult steps to address the indebtedness, rampant inflation, and high unemployment that robbed this region of a decade of growth.

The cornerstone of the summit was the call by all leaders for the creation of a Free Trade Area of the Americas (FTAA) by 2005. This will create a market of over 850 million consumers with a combined income of roughly $13 trillion. It will also level the playing field for U.S. exporters, who currently face Latin American trade barriers over three and one-half times those in the United States. It is critical to secure a commitment to work toward a hemispheric free trade area now, even though it will take years to achieve, in order to set the standard in the region and ensure that subregional integration initiatives are consistent with the goal of creating the FTAA and with the multilateral system.

The President tangibly demonstrated his commitment to this goal by announcing that the United States along with our NAFTA partners Mexico and Canada will initiate negotiations with Chile on accession to NAFTA. The inclusion of Chile would expand the total population of NAFTA to 381 million and its combined income to 30 percent of the world's total. The United States is an important trade partner for Chile; U.S. exports already account for over 20 percent of Chile's total imports.

The decision to start accession discussions with Chile reflects the enormous progress that country has made in achieving macroeconomic stability, liberalization of trade and investment policy, convertibility of the currency, improvement of living standards, and alleviation of poverty. Through a combination of stabilization and liberalization measures, Chile has achieved sustained real growth of 7 percent on average over the past 8 years. It has brought its external tariffs down by 79 percent since 1975. These measures have led to significant inflows of foreign capital, and the ratio of foreign debt to GDP has been reduced by nearly 60 percent since 1985. At the same time, inflation has fallen to 10 percent per year and unemployment is a low 4.5 percent.

At the Summit of the Americas the leaders set in place a process for achieving free trade in the hemisphere. Over the next several months members of existing subregional trade groups such as NAFTA will hold consultations on achieving regional trade liberalization. The United States will initiate discussions to determine interim steps with each of the countries in the region through previously established Trade and Investment Councils. The Administration will hold discussions with the Congress and with the United States' NAFTA partners on NAFTA expansion. In addition, the Organization of American States' Special Committee on Trade will develop a compendium of all existing trade agreements within the hemisphere to increase transparency and identify areas of potential trade facilitation, such as customs harmonization. Meetings of the countries' ministers are scheduled for June 1995 and March 1996 to review progress and further define the work program.

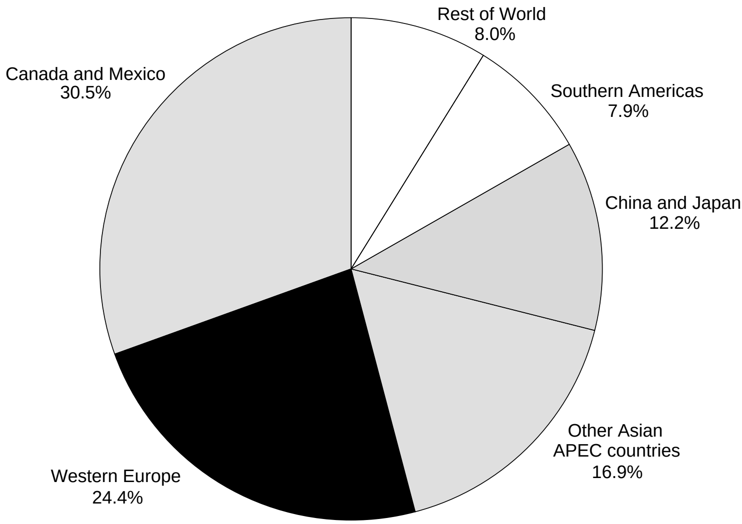
Economic Impact

The southern Americas (here defined to include Central America, the Caribbean except for Cuba, and South America) make up one of the most economically dynamic regions in the world. Sustained income growth in the region reflects in part a robust recovery from the recessions associated with the debt crisis of the early 1980s, and in part significant structural reforms on the domestic front and in trade policy. Many of the countries in the region are expected to continue to experience high growth rates due to the reduction of both debt levels and inflation through macroeconomic stabilization measures. The southern Americas account for about 6.5 percent of world population and 3.5 percent of world income. Brazil is by far the largest country in this region, with over 40 percent of the region's income and population.

As income in this region grows, its imports from the United States will grow even faster. Over the past 5 years, exports from the United States to the southern Americas have grown almost 10 percent per year—far faster than the region's income growth. By far the greatest share of the region's imports—29 percent—come from the United States. This reflects in many cases geographical proximity, as well as historical and cultural ties. Interestingly, however, Brazil's largest trade partner is not the United States but the European Union, which accounts for 25 percent of Brazil's trade compared with 22 percent for the United States. Overall, the southern Americas currently account for nearly 8 percent of U.S. exports, as shown in Chart 6–2.

Chart 6-2 **U.S. Merchandise Exports by Region in 1993**

By far the majority of U.S. exports go to our NAFTA partners, Western Europe, and the APEC countries. The southern Americas take nearly half of the remainder.



Note: The southern Americas include Central America, the Caribbean except for Cuba, and South America. Percents do not add to 100 because of rounding.
Source: Department of Commerce.

As noted above, Latin American tariffs are over three and one-half times those in the United States on average. Thus, trade liberalization is likely to result in increased market opportunities for U.S. products and associated export and job growth. A variety of studies have analyzed the impact of a possible hemispheric trade agreement on the U.S. economy. Most of these studies find that the effects of expanding NAFTA southward will be beneficial for both the U.S. economy and our regional trade partners.

In addition to the direct beneficial effect of cheaper imports from the United States and expanded export opportunities, countries in the southern Americas would benefit from the enhanced credibility of their market reforms that a trade liberalization agreement with the United States or NAFTA would bring. This commitment to a liberal trade regime should increase investment by both domestic and foreign investors and contribute to long-term growth. This is good for the United States both because it will improve the prospects for peace and political stability in the region and because it will further raise the purchasing power of southern American consumers, increasing their spending on U.S. goods.

If instead the United States should fail to recognize the historic opportunity that this conjuncture represents, and if we do not work to improve access to southern American markets for both trade and investment, U.S. companies and workers will lose out to foreign competitors. Most countries in the southern Americas have already joined one of four preferential subregional trading blocs. Most of these subregional blocs have plans to adopt a common external tariff (CET). This will make it more difficult for countries to liberalize individually and will result in diversion of imports in favor of member-country products and away from U.S. products. In the case of Mercosur—the largest group, whose membership includes Argentina and Brazil—a CET was scheduled to go into effect in January 1995 on products accounting for roughly half of imports from nonmember countries. Coverage will be expanded to all products by early in the next century. Led by Brazil, Mercosur is also working to conclude agreements with Chile and Bolivia, as well as with the European Union, and has plans to create a South American Free Trade Area. Unless we move soon, U.S. exporters will be at a disadvantage relative to their competitors inside these blocs.

ASIA-PACIFIC ECONOMIC COOPERATION

Asia-Pacific Economic Cooperation (APEC) was first established in 1989 as a regional forum for economic cooperation. APEC has since expanded to include 18 members: Australia, Brunei, Canada, Chile, China, Hong Kong, Indonesia, Japan, Malaysia, Mexico, New Zealand, Papua New Guinea, the Philippines, Singapore, South Korea, Taiwan, Thailand, and the United States.

At the President's invitation, the leaders of the APEC countries met in 1993 in Seattle. There they put forth their vision of an Asia-Pacific economic community. Last November in Bogor, Indonesia, the APEC leaders established a common frame of reference for achieving that vision. They made a political commitment to eliminate barriers to trade and investment in the region by the year 2020. All countries will begin to liberalize at a common date, but the pace of implementation will take into account the differing levels of economic development among APEC economies: the industrialized countries will achieve free and open trade and investment no later than 2010, and the developing economies no later than 2020. The leaders also reaffirmed their support for the multilateral trading system and APEC's continued commitment to global trade liberalization and to the WTO-consistency of any APEC trade and investment initiatives. The APEC leaders instructed their ministers to work together to develop a detailed blueprint, laying out an action plan and timetable to achieve progressive liberalization in the region. The leaders will review this blueprint at their meeting in Japan in 1995.

Over the next year the Administration will work to ensure that the action plan describes comprehensively and in detail the process by which Asia-Pacific free trade and investment will be achieved. The Administration will consult closely with the Congress and the U.S. business community as it works with our APEC partners to develop a plan that addresses the widest possible range of barriers to the free flow of goods, services, and capital. APEC may focus initially on trade facilitation issues, such as standards conformance and customs simplification. The liberalization process will build on the Uruguay Round's achievements, possibly accelerating the implementation of commitments in the early stages of APEC liberalization, and also on the work program undertaken by APEC's Committee on Trade and Investment. Negotiators may work on issues not covered adequately in the WTO and issues of particular importance to APEC members—including investment, intellectual property, rules of origin, some service sectors, government procurement, competition policy, and infrastructure, as well as elimination of tariffs and nontariff barriers.

The Economic Importance of the Asia-Pacific Region to the United States

APEC's markets are critical to U.S. exporters, both for their size and because of their dynamism. The 14 Asian APEC economies already account for $135 billion, or nearly 30 percent of U.S. exports in 1994 (Chart 6–2). By comparison, Western Europe accounts for less than one-quarter. The Asian APEC economies are among our fastest-growing export markets: U.S. exports to Asian APEC members grew 9.9 percent per year on average over the past decade, compared with 8.3-percent growth in U.S. exports to the rest of the world. Their aggregate income of nearly $6 trillion accounted for one-quarter of world income in 1992 and is projected to grow 4.4 percent per year in real terms over the next decade. U.S. exports to the region are projected to grow even faster than income, at a rate of 6.4 percent per year.

Although the opportunities for U.S. businesses are tremendous, the obstacles are often very large. Between 1989 and 1992, automobile sales in Malaysia, the Philippines, and Thailand doubled, but tariffs on automobile imports into these countries remain high at between 17 and 57 percent. Studies estimate that Asian APEC members will invest $1.1 trillion in infrastructure projects over the next 6 years. China, which alone accounts for nearly half of this planned investment, has tariffs of 38 percent on machinery and equipment and 15 percent on steel. Overall, manufactured imports into Asian APEC markets face tariffs much higher than the average tariff on imports into the United States. Market-opening initiatives through APEC will help reduce these barriers, creating tremendous opportunities for U.S. companies and workers.

U.S. companies must remain actively engaged in the region or risk losing out to Asian competitors. Currently 58 percent of total imports by Asian APEC economies are from other Asian APEC economies—over three times the share from the United States. And this intra-Asian share is growing rapidly. The liberalization measures that APEC members will undertake will be critical in ensuring that U.S. firms are able to compete on equal terms in this large, booming market.

BILATERAL NEGOTIATIONS

At any time the United States is engaged in several negotiations with individual countries on trade issues or disputes. These bilateral negotiations are less glamorous than multilateral or plurilateral trade initiatives, but they are extremely important in opening up markets, settling disputes, and protecting U.S. trading rights. In addition, these negotiations are often where new trade issues are first discussed or tested. Although the United States has bilateral negotiations at one time or another with almost every country with which we trade, we focus here on two bilateral relationships of particular importance, those with Japan and China, and on the Administration's broader export strategy.

JAPAN

One of the most prominent of our bilateral trade relations, and the one that generates the most negotiating activity, is that with Japan. This is to be expected given the size of the trade involved ($155 billion in total trade in 1993, the second largest among our trading partners), the size of the bilateral trade imbalance (a U.S. deficit of $60 billion, our largest with any country), and the character of the barriers to foreign goods within Japan.

Last year's *Report* examined the character of the Japanese economy and Japanese trade in detail. Japan has relatively low formal trade barriers outside the agricultural sector. Yet at the same time Japan has strikingly low levels of import penetration in many sectors in which there is very large mutual trade among most industrialized countries. Japanese domestic prices for traded goods are often significantly above world market prices, even after accounting for taxes, tariffs, and higher distribution charges.

Although there are examples of foreign firms that have done very well in the Japanese market, there are also widespread complaints, and not just from American firms, that the Japanese market is closed to outsiders. The barriers are often subtle and take a variety of forms. Government licensing, regulation, and administrative guidance, restrictions on product specifications or pricing, and procurement practices all can be difficult for foreign firms to satisfy, and often difficult even to discover. In other cases private practices, such as control over distribution channels, group affiliations, or share crossholdings, make it difficult for foreign firms to sell or invest in Japan. The fact that the barriers vary from industry to industry, and are often opaque, means that negotiations are extremely detailed, sector-specific, and time-consuming. The Market Oriented Sector Specific (MOSS) negotiations of 1985–86 were the first of a series of targeted attempts to open individual markets. The Semiconductor Trade Agreement in 1986 also focused on the effective opening of a single sector. The Structural Impediments Initiative (SII) of 1989–90 took a somewhat different approach, focusing on the macroeconomic balance between national saving and investment that lies behind both Japan's large global current account surplus and the large deficit in the United States, while at the same time tackling a series of regulatory and competition issues that stood in the way of increased foreign sales in Japan.

The President and the Japanese Prime Minister announced their Framework for a New Economic Partnership at the July 1993 economic summit in Tokyo. The Framework contained macroeconomic goals and five sectoral and structural "baskets" for talks between the two nations. The macroeconomic goals included a shift to domestic demand-led growth in Japan to reduce its current account surplus, and a reduction in the U.S. fiscal deficit and an increase in the U.S. saving rate. The baskets were government procurement, regulatory reform and competitiveness, major sectors (most prominently, automobiles and parts), economic harmonization, and follow-up on the implementation of existing agreements.

Negotiations were complicated by two major changes in Japan's government, and in addition, talks broke down temporarily in February 1994. Despite their rocky path, a series of results and agreements were reached in the fall of 1994. Both sides made progress in macroeconomic policy that should narrow the overall deficit in each country. The Congress passed the Administration's deficit reduction program in August 1993, and the Japanese Diet voted to increase government spending and cut income taxes, while postponing a planned increase in consumption taxes. Japan's fiscal measures have contributed to its emergence from recession, and its current account surplus has fallen as a percentage of GDP and should fall further in the near term.

In the economic harmonization basket, the United States reached an agreement on intellectual property protection last August that enhances the ability of U.S. inventors to apply for and be granted patent protection in Japan. In procurement, the United States reached agreements in telecommunications equipment and services covering purchases both by the government and by the dominant Japanese telecommunications firm (in which the government still owns the majority share), a combined market of $11 billion per year. The agreements call for more complete information about procurement plans to be made available at an earlier stage, full consideration of international standards for equipment, and the use of overall best value to judge competing bids. A similar agreement was reached in medical technology products and services, a market of $2.6 billion per year.

Two agreements were reached in financial services. In insurance, a market worth $320 billion per year, Japan agreed to ease restrictions on the introduction of new products, ease rate restrictions on policies to large customers, and deregulate the industry in such a way as not to prejudice the interests of foreign insurers, who are now active in only a small, specialized segment of the market. In January 1995 the United States and Japan reached an agreement to further liberalize the Japanese financial sector. The Japanese Government agreed to open the $200 billion public pension fund market to foreign investment advisory services, relaxed the conditions for issuing corporate debt, agreed to introduce a domestic derivatives market, and eliminated various restrictions on cross-border capital movements.

In the $4.5 billion flat glass industry, where the existence of restrictive practices had been confirmed by Japan's Fair Trade Commission, an agreement was reached in December committing Japanese distributors to carry imported glass, and requiring the Japanese Government to consider foreign glass in public procurement.

The one critical area where no agreement has been reached is automobiles and parts, the largest single sector in the Framework talks. The issues in these negotiations are access to the Japanese auto dealership network, the removal of regulations that limit foreign sales of replacement auto parts, and increased participation in the original-equipment auto parts market, including participation in the design stage. In response to the meager progress in the automobile trade talks, the Administration initiated a Section 301 investigation in October covering the replacement parts sector, where the involvement of the Japanese Government is clearly defined, and made it clear that the United States expected progress in the original-equipment parts and automobile markets as well.

From the beginning, the Administration has insisted that the Framework negotiations should lead to agreements that produce significant, measurable results. The two countries agreed that objective criteria, either qualitative, quantitative, or both, be used to evaluate the agreements over time as to whether tangible progress was being achieved. Arguments over these criteria were the most controversial part of the Framework. The Administration was widely criticized, both in Japan and elsewhere, for attempting to "manage trade" or set market share targets.

These criticisms are and were disingenuous. None of the agreements set market share targets, either for U.S. firms or for foreign firms generally. A wide range of objective indicators was suggested and ultimately agreed to, with different indicators for different sectors depending on the characteristics of each sector. Furthermore, none of the market access concessions are limited to U.S. firms; Japanese market-opening measures are available to all on an MFN basis.

The Administration intends to continue to explore market-opening measures with Japan, and to ensure that agreements lead to tangible increases in opportunities for U.S. and other foreign suppliers to sell in Japan. In addition to the negotiations on automobiles and auto parts, the Administration is now engaged in discussions on reducing barriers to foreign investment in Japan and more rigorous enforcement of Japanese antitrust laws.

The Framework negotiations on deregulation have recently taken on increased importance due to internal developments in Japan. The high cost to Japan of its extensive regulation of the economy has become increasingly apparent, and there is growing demand within the Japanese business community for deregulation. The United States has both specific and general interests in a thoroughgoing deregulation of the Japanese economy. Many of the sectoral issues concern regulatory barriers, and the United States has presented detailed requests for regulatory changes. But the United States also has a strong interest in generalized deregulation of the Japanese economy, which would reduce barriers to entry for all firms in Japan, both domestic and foreign.

Despite the length and occasional acrimony surrounding sectoral liberalization negotiations with Japan, the talks work. One study has shown that U.S. exports to Japan in those sectors covered by trade negotiations increased almost twice as fast as total U.S. merchandise exports to Japan, and estimated that the negotiations were responsible for an additional $5 billion in annual U.S. exports. It is also important to emphasize that it is not only the United States but also the Japanese consumer who gains from these agreements, in the form of lower prices and a wider choice of goods.

CHINA

The Administration is pursuing a carefully balanced economic policy toward China that takes into account the tremendous opportunities for U.S. exports associated with that country's rapid growth, as well as its geopolitical importance and Americans' concerns about China's protection of human rights. The goals of U.S. policy are threefold: promotion of U.S. commercial interests, to raise standards of living in the United States; encouragement of continued economic reform within China and its integration into the world economy, with the expectation that these will help realize U.S. foreign policy goals including democratization and protection of human rights and the environment; and promotion of global cooperation and integration in the interests of peace and prosperity.

Economic Importance

China's economy is large, dynamic, and relatively poor. Although it is estimated to be the world's third-largest economy in purchasing-power-parity terms, China's per capita income even by that measure is roughly one-tenth that of the United States. Measures based on current exchange rates rank China eighth in total output and yield a per capita income nearly 50 times smaller than that of the United States. Even if China's recent real growth rates of 9 percent per year (the highest in the world) are maintained, it will be decades before per capita income in China approaches those of developed countries today.

For much of its history since the 1949 communist revolution, China maintained a virtually closed, centrally planned economy, which was accompanied by economic stagnation. Sweeping economic reforms undertaken since the late 1970s have contributed to explosive growth and a decline in central government control. In the agricultural sector this has taken the form of decollectivization and a return to smallholder farming. In the industrial sphere the management of state-controlled firms has been decentralized, and the government has permitted the rapid growth of township and village enterprises; private enterprises now account for half of industrial output. By the early 1990s prices for 95 percent of retail sales, 90 percent of sales of agricultural commodities, and 85 percent of capital goods sales were determined by the market. Factor markets have also been liberalized: state control of labor markets has been reduced, and previously repressed capital markets have been allowed to develop in fits and starts, although they remain primitive by Western standards.

As the government has instituted market reforms and liberalized, China's economy has become increasingly integrated into the global economy. China's share of world trade grew from 0.6 percent in 1977 to 2.5 percent in 1993—making it the world's 11th-largest exporter. Similarly, flows of foreign direct investment into China exceeded $25 billion in 1993, in marked contrast to the prereform years when such investment was prohibited. And these two trends are closely related: firms with foreign equity participation accounted for two-thirds of the expansion of exports in 1992 and 1993.

China has run global trade deficits in most years since reforms were initiated—indeed, China registered a deficit last year of $12.2 billion. However, China has run a growing bilateral trade surplus with the United States, which reached $22.8 billion in 1993. China's persistent surplus with the United States in part reflects its specialization in inexpensive mass-market consumer goods. China similarly runs bilateral surpluses with Japan and Europe for this reason. Moreover, increases in the bilateral surplus with the United States since the mid-1980s in large part reflect the movement of labor-intensive production of goods such as shoes, garments, and toys from Hong Kong and Taiwan to China, to take advantage of lower wages. Table 6–2 makes clear that the increase in the U.S. deficit with China has partially been offset by declines in the deficits with Hong Kong and Taiwan.

TABLE 6–2.— *U.S. Trade Deficits with China, Hong Kong, and Taiwan*

[Millions of dollars]

Year	Total	China	Hong Kong	Taiwan
1987	25,876	2,796	5,871	17,209
1993	31,392	22,777	–319	8,934

Source: Department of Commerce, Bureau of the Census.

The Chinese trade regime has been liberalized in several ways. The role of state trading firms in intermediating international trade has been greatly reduced. Export subsidies have largely been eliminated. The former system of multiple exchange rates for differing types of transactions was unified and the currency devalued; the yuan is now convertible for most categories of transactions. As trade has been liberalized, China's trade pattern has increasingly conformed to conventional theories, with China exporting labor-intensive products and importing capital goods. Nonetheless, China's trade regime has remained selectively protectionist, with multiple overlapping barriers to trade in some goods and discriminatory rules on investment and services. The absence of effective protection for intellectual property rights has cost U.S. businesses hundreds of millions of dollars in lost sales.

Ultimately the combination of rapid economic growth and greater, albeit uneven, trade openness means that China will be a major market for U.S. goods and services. China's market presents the greatest growth opportunities in aerospace, power generation equipment, environmental technologies, and computers, among merchandise exports. Among services there are opportunities in financial (including insurance), information, distribution, accounting, audiovisual, and legal services.

Most-Favored-Nation Status

China is subject to the Jackson-Vanik Amendment to the Trade Act of 1974, since the U.S. Government defines China as a nonmarket economy. The amendment requires that each year, in order for China to qualify for MFN status, the President must issue a waiver certifying either that China does not impede emigration or that providing MFN status will lead to increased emigration. In May 1994 the President renewed MFN status for China in the context of a broader policy that includes delinking MFN renewal from human rights issues other than emigration; a ban on imports of Chinese munitions; maintenance of the U.S. economic sanctions imposed in response to the Tiananmen Square tragedy, including denial of Chinese participation in Overseas Private Investment Corporation and Trade and Development Agency programs; and a vigorous and broad-based human rights policy. The President determined that renewal of MFN status offered the best way to promote the full range of U.S. interests in China, including human rights, strategic, and economic interests. Moreover, the President determined that China had made sufficient progress on the conditions he had imposed when renewing China's MFN status in May 1993—in particular, on compliance with a 1992 agreement on the treatment of prison labor, in addition to guaranteeing freedom of emigration.

The decision to pursue a vigorous human rights policy separately from MFN renewal reflected a determination that protection of human rights is most likely to be achieved through a combination of carefully targeted initiatives and China's continued economic reform and integration with the world economy. The Administration is promoting human rights in China by a variety of means including increasing international broadcasting to China, support for nongovernmental organizations (NGOs) there, encouragement of multilateral participation in our human rights initiatives, and development, in consultation with the business and NGO communities, of a set of ethical principles for business conduct as models for all companies engaged in international business.

The decision also recognized that substantial economic disruption in both China and the United States would accompany MFN revocation, along with significant damage to the broader bilateral relationship. Revocation of MFN status would result in tariff increases on Chinese imports of 5 to 10 times their current level, depending on the product. The ultimate effect on consumer prices and consumption would depend on the particular demand and supply elasticities in each product market, but they would likely be large, with estimates of decreased Chinese imports ranging from $6 billion to $15 billion annually.

MFN renewal ultimately will promote the goal of improved human rights protection more effectively than revocation would, because increased foreign trade contributes to China's integration with the world economy, economic decentralization, and the growth of a middle class. As the economy has grown and become increasingly decentralized, a new business society has developed that is independent of the state. Further, with greater wealth and access to foreign goods and to modern telecommunications, Chinese citizens are increasingly exposed to a broader set of ideas, undermining the government's monopoly on information. The result is a diffusion of economic power and information, creating the preconditions for a civil society, and with it more pluralistic forms of governance and a greater respect for human rights.

Bilateral Issues

Despite China's economic reforms, a variety of barriers still frustrate U.S. exporters, and lack of enforcement of intellectual property laws costs U.S. firms in the computer software, publishing, and audiovisual industries hundreds of millions of dollars a year. Although China committed itself to protect copyrights, patents, and trademarks for foreign goods in the U.S.-China Bilateral Trade Agreement of 1979, compliance has been a recurrent problem. In May 1991 the U.S. Government launched an investigation under the Special 301 provision of the trade act of 1988. In January 1992 the United States and China signed a memorandum of understanding that committed the Chinese Government to strengthen patent, copyright, and trade secret laws; to provide patent protection for products as well as processes; to join two international conventions on copyrights; and to treat software as a literary work under Chinese law, resulting in protection for 50 years.

Although China subsequently carried out all the institutional and legal changes, enforcement has remained a problem. China continues to be a major producer of pirated compact discs and computer software, often in joint ventures with Taiwanese and Hong Kong partners; the pirated goods are increasingly exported to third markets. In response, negotiations were begun in 1993 to strengthen Chinese enforcement of existing laws, and the United States initiated a second Special 301 investigation in June 1994. In January 1995 the U.S. Trade Representative released a preliminary retaliation list in an attempt to persuade the Chinese to be more forthcoming in the negotiations. China itself would benefit by improving its protection of intellectual property rights. Other countries in the region have significantly strengthened their protection of intellectual property rights in recent years, recognizing that it is an essential step in order to have access to cutting-edge technology and investment from abroad, as well as to encourage innovation at home.

U.S. exporters also encounter a wide array of market access problems. Starting in the mid-1980s, the U.S. Government has held a series of bilateral negotiations to persuade Chinese authorities to reduce the number, secrecy, and severity of administrative barriers to imports, including import licensing requirements, quantitative restrictions, and product testing and certification requirements, as well as to increase the transparency of trade rules.

The United States initiated an investigation under Section 301 in October 1991. The Chinese Government signed a memorandum of understanding in October 1992, following publication of a U.S. retaliation list. Under the agreement China committed itself to dismantle 90 percent of all import restrictions, to eliminate import substitution regulations, to reduce tariffs and eliminate the import regulatory tax, to improve transparency, and to base all phytosanitary and sanitary standards and testing on sound scientific principles. In return, the United States agreed to terminate the Section 301 investigation, to work with China on its accession to the GATT (now the WTO) and to liberalize restrictions on Chinese access to technology. To date, there has been little progress in increasing the transparency of approval processes for import licenses or quotas, or in eliminating restrictions on the imports of agricultural products through sanitary and phytosanitary standards; however, negotiations with China to resolve these issues are continuing.

WTO Accession

China has applied for membership in the WTO, and formal negotiations for accession have been in progress since 1988. The United States has consistently made clear that it wants China to become a member of the WTO, and the Administration is working with China and our other trade partners toward this goal. But the United States and the other WTO members are determined that China must join on commercial, not concessional, terms. This is critical for maintaining the integrity of the global trading system and integrating China into it. Moreover, implementing transparent trade rules and promoting open trade and investment should strengthen China's economy and lock in its economic gains.

Every country that joined the GATT in the past agreed to adhere to basic obligations. These include transparency of the trade regime, uniform application of trade rules, national treatment for goods, and a foreign exchange regime that does not obstruct trade. These basic obligations are the foundation of GATT rules; without them the other disciplines are meaningless. Thus, for instance, there is no point in agreeing on disciplines for trade laws if, as is currently the case in China, they are not uniformly applied throughout the country. Similarly, there is no point in negotiating market access agreements if, as in China today, the trade rules are not transparent.

Although U.S. relations with Japan and China are both very important, they are only part of a large number of bilateral trade relationships. Market-opening negotiations and, on occasion, trade disputes are a normal and continuing part of U.S. trade policy. This Administration has put strong emphasis on opening markets for U.S. exports. But its bilateral negotiations are only part of a broader strategy to promote U.S. exports.

THE NATIONAL EXPORT STRATEGY

The Administration has focused on encouraging American exports by eliminating U.S. export barriers and by improving the efficiency of U.S. export promotion efforts. The Administration's Trade Promotion Coordinating Committee unveiled the National Export Strategy in September 1993. Since then the Administration has succeeded in meeting the goals it had set out: removing obstacles to exporting, improving trade finance, supporting U.S. bidders in global competition, helping small and medium-sized U.S. firms enter export markets, and promoting U.S. exports of environmental technologies and services.

The Administration has implemented almost all of the 65 objectives laid out in the 1993 National Export Strategy report:

- Unnecessary export controls have been eliminated for computers, affecting $30 billion worth of exports. Most authorization requirements for the export of telecommunications equipment have been eliminated.
- The value of exports requiring licenses has fallen to one-third its previous level, and the licensing process has been streamlined.
- Trade finance has been buttressed by increasing the limit on project finance through the Overseas Private Investment Corporation from $50 million to $200 million. Coordination with State and local sources of trade finance has improved, and partnerships with the private sector are being encouraged.
- Export assistance centers have been opened throughout the country, providing "one-stop shopping" for small businesses seeking Federal export information and financing assistance.
- The Administration has countered the advocacy efforts of foreign governments with efforts of its own on behalf of U.S. exporters, helping U.S. firms compete and win over 90 major contracts worth a total of $20 billion. These contracts include a multi-billion-dollar Saudi Arabian telecommunications procurement, power and energy projects throughout Asia, and a

project to build an environmental surveillance and air traffic control system in Brazil.

Efforts have also been made to discourage and counter the "tied aid" practices of other nations: concessional loans or grants that are only available to recipient governments if they procure equipment produced by the donor country's firms. Worldwide, the proportion of aid that is tied has decreased dramatically since 1992—the result of new tied aid guidelines adopted through the Organization for Economic Cooperation and Development (OECD, whose membership includes the major donor countries), and of the U.S. Government's subsequent aggressive enforcement of these guidelines. These guidelines make many new aid projects ineligible for tied aid financing and therefore open to international market competition.

Further, the National Export Strategy has focused on new opportunities in the economies expected to grow especially quickly in the coming years. These "big emerging markets" include China, Taiwan, Hong Kong, Korea, Indonesia, India, Mexico, Argentina, Brazil, Poland, Turkey, and South Africa.

A year ago the Administration set the goal of raising total U.S. exports to $1 trillion by 2000. The success of this past year has led the Administration to raise this goal to $1.2 trillion, which would represent almost a doubling of the 1993 export level.

NEW ISSUES IN TRADE NEGOTIATIONS

Since the mid-1980s, when the blueprint for the Uruguay Round negotiations was determined, a series of new trade issues have arisen that will occupy negotiators for the next several years. While these issues—trade and the environment, competition policy, rules on investment, and trade and labor standards—have already made a limited appearance in multilateral discussion, they have played a greater role in recent plurilateral and bilateral negotiations. Progress achieved in those negotiations will likely have a significant influence on future negotiations at the multilateral, plurilateral, and bilateral levels.

TRADE AND THE ENVIRONMENT

Protection of the environment and an open trading system are sometimes seen as conflicting goals. Many environmentalists are concerned that free trade will come at the expense of the environment, and many free traders are concerned that efforts to incorporate environmental concerns into the international trading system will degenerate into disguised protectionism. However, there is no inherent conflict between liberalizing trade and protecting the environment, and the Administration has focused on potential complementarities between good trade policies and sound environmental policies.

In fact, free trade and environmentalism have much in common. In both cases the benefits from achieving progress are spread across a wide group of people, while the interests that are harmed are more concentrated. Trade liberalization benefits consumers (and workers producing exports) but may harm workers in import-competing sectors. Similarly, environmental protection benefits a diffuse group of people, while the cost is concentrated on a smaller group, those overusing environmental resources. Thus, while the gains from liberalized trade and a cleaner environment outweigh the losses in the aggregate, it still can be difficult to achieve progress, since the costs of the action are concentrated on a small group who vociferously oppose action, while the benefits may be so diffuse as to make it difficult to mobilize potential supporters.

Moreover, both trade liberalization and international environmental issues require the use of multilateral tools. Without such tools there is a tendency for countries to engage in damaging environmental and trade policies designed to further their own interests at the expense of their neighbors. Multilateralism can ensure that progress is made on enough fronts so that all countries gain from trade and a protected environment. The GATT and its successor the WTO are well suited for tackling world trade issues. But there is as yet no analogous forum for comprehensively addressing global environmental issues. Instead there are a variety of international agreements and organizations committed to working on environmental problems.

There are also complementarities between good trade policies and good environmental policies. Agricultural protection in industrialized countries is a case in point. The protection of developed-country agriculture leads to more intensive farming, often of lands that are of marginal use, causing unnecessary soil erosion, loss of biological diversity, and the excessive use of pesticides and chemicals. Liberalizing trade in agriculture and lowering agriculture production subsidies can lead to a pattern of world farming that causes less environmental damage.

Also, high trade barriers to labor-intensive imports, such as clothing, from developing countries lead these countries instead to export products that are intensive in natural resources, causing environmental damage. In addition, high-value-added natural resource-based products such as wood or paper products often face high tariff barriers, whereas the raw natural resource itself does not; this forces developing countries to rely on exports of unprocessed natural resources while denying them the revenue gains from the downstream products.

Just as trade policy improvements have the potential to help the environment, environmental policy improvements can lead to economic gains. For instance, making polluters pay for the cost of the environmental resources they use encourages efficient resource allocation and undistorted world trade. The elimination of government underpricing of public natural resources can also reduce trade distortions.

Empirical evidence on the relationship between trade and the environment reinforces the notion that the two are not in conflict. For instance, trade liberalization may act to increase income levels through more-efficient resource allocation. In fact, the evidence suggests that openness to world trade is one of the strongest predictors of rapid income growth in less developed countries. Income growth in turn has beneficial effects on the environment. One study suggests that, as a country's income per capita rises beyond a point around $5,000, its environmental record improves. As people can afford to, they devote more resources to environmental protection, and political pressures for environmental protection increase.

Most evidence suggests that international differences in environmental compliance costs have not had a significant impact on trade and investment flows, primarily because these costs are almost always a very small fraction of value added in production. In the United States, for example, pollution abatement costs in over 93 percent of all industries are less than 2 percent of value added. Such small differences are unlikely to cause firms to migrate to take advantage of differential costs of environmental regulation; other considerations are far more important.

It is important to put aside the notion that trade itself is the cause of environmental degradation. Although economic activity certainly may diminish environmental resources, international trade, like trade among the States, is simply a means of making economic activity more efficient. The above examples and the available empirical evidence suggest that trade *itself* need not pose a particular threat to the environment. By the same token, most often the best response to an environmental problem is not to restrict trade. Instead, policies aimed *directly* at an environmental problem are likely to be more effective. For instance, if the use of a particular input in a firm's production is causing pollution, it is most effective to address the use of the input itself, rather than limit trade in the resulting product.

NAFTA demonstrates how trade liberalization can serve as an impetus for improved environmental policies. NAFTA specifically ensures its members' right to safeguard the environment, and it encourages all the NAFTA parties to strengthen their environmental efforts. NAFTA maintains all existing U.S. health, safety, and environmental standards. It allows States and cities to enact even tougher standards, while providing mechanisms to encourage all parties to harmonize their standards upward. The NAFTA side agreement on the environment created a new North American Commission on Environmental Cooperation, with a council made up of the three countries' top environmental officials. There is a mechanism to ensure that countries effectively enforce their own environmental laws, and a provision that guarantees public participation in monitoring of environmental laws. Finally, two new institutions have been established to fund and implement environmental infrastructure projects along the U.S.-Mexican border. The North American Development Bank (NADBank) will make loans for environmental cleanup and community adjustment on both sides of the U.S.-Mexican border. The NADBank will work closely with the new U.S.-Mexican Border Environment Cooperation Commission, which will review and certify proposals for environmental infrastructure projects.

NAFTA shows that it is possible to use trade concessions as a carrot to encourage environmental improvements, rather than using trade penalties as a stick to punish poor environmental behavior. Without NAFTA it is unlikely that there would have been an incentive for the member countries to strengthen their commitments to environmental cooperation. NAFTA also sets an example for other trade agreements in the use of international mechanisms and national commitments to ensure that free trade is compatible with enhanced environmental protection and sustainable development.

Environmental concerns were also addressed in the most recent Uruguay Round negotiations. The preamble of the agreement establishing the WTO recognizes the importance of environmental concerns. This is the first time that a broad multilateral trade agreement has recognized sustainable development as a guiding principle. The WTO negotiators have agreed to establish a full WTO Committee on Trade and the Environment to ensure the responsiveness of the multilateral trading system to environmental objectives. Issues this committee will tackle include, first, whether countries may use their trade policies in a way that discriminates between like products on the basis of the processes and production methods used; second, the relationship of the GATT to international environmental agreements; third, the circumstances under which countries may use trade measures to protect the environment; and fourth, the scope of the exceptions for environmental measures provided by the GATT under Article XX, which covers measures necessary to protect human, animal, and plant life.

COMPETITION POLICY AND TRADE

The relationship between national competition policies and international trade has emerged as an important issue for future negotiations. Historically, concern with international cartels has motivated discussions of competition and trade policy; the current revival of interest, however, is driven primarily by questions of market access. As tariffs and other formal trade measures have fallen, domestic barriers to competition have come under increasing scrutiny. Barriers to foreign entry can arise for numerous reasons. Government procurement practices, either through explicit "buy national" policies or through carefully drawn or nontransparent product specifications, can favor domestic over foreign producers. Health and safety standards, inspection procedures, and other product regulations can also operate as protectionist barriers. These areas have already been subject to extensive negotiation, and agreements were concluded in the last two GATT negotiating rounds that require transparency and nondiscrimination in procurement and product standards.

The most intense interest, however, now falls on barriers that can arise from the practices of private firms. These are often vertical restraints—control over distribution channels, exclusive sales arrangements or refusals to deal, rebates on sales—that impede new entrants. These barriers may also derive from close affiliations among firms within corporate groups that effectively limit sales by outsiders. Vertical and other private restraints on trade have been the subject of negotiations between the United States and Japan in the SII and the Framework negotiations (discussed above). Since GATT rules do not cover restrictive practices by private parties, except as they are supported by government measures, there is particular interest in the role of national competition policy authorities in fostering market access in these cases.

The second area of concern about anticompetitive business practices is the advantages they might create for sales in other markets. If industries are characterized by economies of scale or learning effects (in which production efficiency rises as cumulative output grows), greater output or longer production runs resulting from limited imports could confer a cost advantage on domestic producers. Restrictions on competition at home may also change the character of global competition among oligopolistic firms. When restrictions are successful in creating monopoly power at home (a less price-elastic home than foreign demand), sales in foreign markets at a lower price than at home (dumping) are a predictable result. Alternatively, collusion among domestic producers in the home market to maintain prices in the face of declining demand, perhaps under the auspices of an officially sponsored recession cartel, can result in venting of surplus production in foreign markets, increasing the instability and operating risks in markets that are open.

Although there is increasing overlap between trade and competition policies, there has been little coordination of international trade policy with antitrust policy. In large part this is because the practices that trade and competition policy deal with are distinct. International trade negotiations under the GATT have dealt with government actions that restrict trade or discriminate against foreign goods. Private practices that discourage imports have been beyond the GATT's reach, except to the extent that government measures support or are necessary to sustain those restraints. Antitrust policies, in contrast, can be effective in dealing with the actions of private parties. However, antitrust laws in some countries do not cover government-owned firms, and antitrust laws seldom apply to other governmental activities.

The extension of international trade disciplines in the GATT has clearly increased competition. As trade barriers have dropped, the extent of effective competition in domestic traded-goods industries has risen. Indeed, Justice Department guidelines now take the extent of international competition explicitly into account, as do the agencies in charge of competition policy in other nations.

However, the extent to which existing competition policy can be harnessed to increase trade liberalization is less clear-cut. Many of the private barriers to entry fall in the area of nonprice vertical restraints to trade, where there is appropriately no presumption of illegality. In many instances vertical restraints, such as exclusive dealing arrangements or ownership interests in distributors, can increase efficiency and ensure product and service quality, even as they act as barriers to new entry. Competition, and not entry opportunities for individual firms, is protected under U.S. antitrust law, and in the absence of evidence of restraints on competition in the domestic market it may be difficult to win a case on the grounds that a new firm cannot gain entry.

One area in which competition policy may have beneficial results is antidumping policy, the most prominent of U.S. policies against unfair trade. In the United States, duties are assessed on imports sold at "less than fair value," in other words, at a price that is either less than the price at which the good is sold in the home market, less than the sales price in a third-country market, or less than the calculated cost of production. If dumping is found, and if the dumped goods are determined to cause injury to the domestic industry, duties are assessed to bring the price of the goods up to "fair value."

There are two rationales for antidumping laws. The first is that the sale of imported goods at less than fair value may be part of a strategy of predatory pricing, designed to force American competitors out of business. The second rationale, and one that directly addresses why only foreign firms are subject to antidumping procedures, is that dumping arises from an asymmetry in competitive conditions between the home market of the dumping firm and the market in which goods are sold. Restricted competition in the dumper's home market creates a situation in which dumping is profitable, creates opportunities for the dumping firm that are not available to firms based in the more competitive market in which goods are dumped, and is therefore seen as unfair. Recent advances in trade theory suggest that such advantages may be possible, depending on the competitive characteristics of the industry.

The value of a competition policy approach is that it may allow a more careful distinction between pricing practices that are unfair and those that simply reflect normal cyclical and market variations. A well-developed body of antitrust law exists to deal with predatory pricing. The courts consider such factors as the size and strength of rivals, the ease of entry in the industry, whether the pricing practices are likely to force firms out of business, and whether the alleged predator could eventually recover its losses from its current low price. Foreign firms selling in the U.S. market are subject to U.S. antitrust law, and the Justice Department and the Federal Trade Commission have brought cases against foreign firms that affect U.S. competition. Competition policy addresses not only predation but also other unfair trade practices, such as vertical restraints, and seeks to avoid the conditions that enable firms to engage in unfair practices.

Ideally, the problem of competitive asymmetry could be addressed by policies that increase competition in the home market of the dumping firm. The progressive reduction of trade barriers, the negotiated elimination of other market access barriers, and the interpenetration of major markets by foreign direct investment all tend to both increase and equalize the competitive environment across markets. Indeed, within some regional groupings where integration has proceeded sufficiently, such as the European Union and the Closer Economic Relations arrangement between Australia and New Zealand, competition policy has entirely replaced dumping review as a means to control unfair trade practices, just as within a single national economy.

Efforts on competition policy and trade will take place on a variety of fronts. Differences in antitrust philosophy and accumulated case law across major countries make harmonization of competition policies unlikely in the foreseeable future, except in closely integrated regional groups. But the global character of most markets has been the impetus for increasing consultation and cooperation among competition policy agencies, and this is likely to lead to some convergence in practice and approach. There is also likely to be increased cooperation in cases that span international boundaries, such as a recent case involving the leading U.S. software producer. As this cooperation increases, one possible step would be an agreement to remove the antitrust exemptions for market division and price fixing by exporters; these exemptions are contained in various national laws including the Webb-Pomerene Act and the Export Trading Company Act of 1982 in the United States and the Export Trade Act of 1952 in Japan. In addition, to facilitate future cooperation, the United States is preparing to negotiate antitrust mutual assistance agreements. These agreements would provide a framework for joint prosecution of international cartels and for effective case-by-case assistance.

Trade negotiations, from the bilateral to the multilateral level, will continue to focus on market access issues, and thus inevitably deal with entry barriers and competition policy. The approach so far has been piecemeal, barrier by barrier and sector by sector; this is particularly evident in services negotiations, but also true of recent U.S.-Japan bilateral negotiations. The key to faster progress will be whether general principles that cut across sectors can be formulated. For example, these might deal with the definition of national treatment in markets where entry is by individual license, or the access of foreign firms to private industry associations that have a regulatory role or provide services necessary for participation in the domestic market.

INVESTMENT

Increasing emphasis on market access will push investment issues to the fore of future trade negotiations, just as it has elevated competition policy issues. This is particularly true of trade in services, where delivery often depends on having a physical presence in the market where the services are sold. But such presence is also crucial for many manufactured goods, where design must be tailored to market requirements, where service and reputation are important, or where fast response is key.

Thus, whereas foreign direct investment was once seen as a substitute for international trade, it is increasingly viewed as a complement or even a necessary component of trade. The evidence on U.S. outward foreign direct investment bears this out. Roughly 60 percent of U.S. exports are sold by American firms that have operations abroad. The evidence also indicates that the countries where U.S. exports are most successful are the same countries where U.S. firms have the largest investments, and where investment restrictions are lowest. Furthermore, nearly $1 of every $5 in sales by U.S. companies abroad is earned by American sales affiliates or wholesaling companies that have established local facilities to sell U.S. exports. Access to foreign markets is the strongest motivation for investing overseas, not lower production costs. Only about 8 percent of the production of U.S. companies abroad is exported back to the United States; the vast majority is sold abroad in the local market.

The investment issue is a clear example of the progress that can be achieved when negotiations are limited to a small group of nations. The investment rules in NAFTA contain most of what is desired in an investment accord, including guarantees on right of establishment, national treatment for foreign investors once established, freedom to repatriate earnings, and transparency in the rules governing foreign investment. The Administration is encouraging similar liberalization in its regional efforts in Latin America and Asia. These principles have also been advanced in U.S. bilateral investment treaties; 12 comprehensive treaties have been signed since 1993, including treaties with the former Soviet republics of Georgia, Ukraine, and Belarus.

Progress in regional and bilateral negotiations should spur multilateral agreements on investment issues. Last September the Administration called for a June 1995 launch of negotiations in the OECD to establish a multilateral investment accord. This agreement would go beyond bilateral investment treaties and existing OECD undertakings, and would require the removal of existing barriers to investment in all OECD countries.

TRADE AND LABOR STANDARDS

The international promotion of labor standards is an important goal of this Administration. The Administration negotiated an innovative NAFTA side agreement on labor standards, and it pressed for and got agreement to include discussion of the relationship between workers' rights and international trade in the meetings of the Preparatory Committee of the WTO. In the Uruguay Round implementing legislation, the Congress directed the President to seek a working party on labor standards within the WTO.

The labor side agreement to NAFTA, the North American Agreement on Labor Cooperation, provides a mechanism for the three NAFTA partners to address interactions between national labor standards in an environment of expanded trade and investment. The agreement commits each country to promote a set of guiding principles subject to its domestic law, but does not establish common minimum standards. The principles include freedom of association and the rights to organize and bargain collectively, as well as prohibitions on forced labor and restrictions on child labor. The agreement emphasizes a cooperative program aimed at improving labor standards in all three countries through technical assistance and the exchange of information. It also contains mechanisms to encourage the enforcement of national labor laws in the three countries and provisions to make the laws more transparent. Enforcement mechanisms include public channels of communication, exchanges of information, and consultations at a variety of levels. If a conflict arises between countries over a persistent pattern of failure to enforce national occupational safety and health, child labor, minimum wage laws, or technical labor standards, in circumstances that are related to trade, the agreement provides for binding arbitration and assessment of penalties.

The promotion of labor standards has a long history in international diplomacy and U.S. policy. The International Labor Organization (ILO) was established shortly after the First World War to promote agreement on labor standards and to monitor progress in achieving them. The United States tried, unsuccessfully, to add a labor article to the GATT in 1953, and tried to incorporate these issues in the Tokyo Round and the Uruguay Round negotiations. Adherence to labor standards is also a condition for country participation in the Caribbean Basin Initiative and the U.S. Generalized System of Preferences, and for eligibility for Overseas Private Investment Corporation insurance. Furthermore, since 1988, denial of workers' rights has been defined as an unfair trade practice in Section 301 of the Trade Act of 1974 and may be subject to action if it harms U.S. economic interests.

Although there is no fixed definition of core labor standards, widely accepted standards reflected in ILO Conventions and U.S. trade law include freedom of association, the right to organize and bargain collectively, freedom from forced labor, and a minimum age for the employment of children. Core labor standards represent fundamental human and democratic rights in the workplace, rights that should prevail in all societies whatever their level of development. They are also necessary to ensure that individuals have the freedom and the information necessary to make their own choices about occupations, earnings, and working conditions. The observance of labor standards can strengthen work force productivity as a whole by raising health and worker morale, and raise the general educational level by keeping children in school. In the absence of such standards, firms may find it difficult to respect workers' rights on their own.

A related concern is that countries could, by routinely abusing workers' rights, lower labor costs so as to gain an unfair advantage in international trade. This would certainly be the case if a particular foreign industry obtained the advantages of a labor force whose rights were not guaranteed—for example, because it had access to a conscript labor force. Whether foreign industries can reap the advantages of abuse of labor rights when such abuse pervades an entire economy is less certain. It is possible to artificially depress labor costs in the short run, but over longer periods of time any advantage gained by the overall abuse of labor standards may be minimal or nonexistent.

The Administration is committed to a multilateral process designed to build consensus and encourage adoption of core labor standards. There is widespread agreement, for instance, that standards should be appropriate to a country's level of development. The ability to compensate workers is limited by overall productivity (output per worker) in the economy, and that compensation may be paid in some combination of wages and better workplace characteristics, in proportions that may vary across societies. The Administration's goals are to achieve broad support for trade at home and abroad by ensuring that the benefits of trade are widely shared by those engaged in the production of internationally traded goods and services, and ultimately to raise living standards worldwide.

DOMESTIC POLICY AND TRADE POLICY

International trade has been and will remain a powerful source of growth, opportunity, and challenge for the American economy. The Yankee trader and the clipper ship were trademarks of this country early in its development, and today the United States remains the world's largest exporter and importer. Recognition of the gains from liberalizing trade go back to our beginnings as a Nation, and recent changes in the nature of goods and services trade, together with advances in theoretical understanding, have served to strengthen this conclusion (Box 6–4).

However, few things bring only benefits, and structural adjustment and change are the essence of a dynamic economy. The most potent force in the modern economy has been technological change, which can result in painful adjustments for firms, workers, and communities, even as it raises overall living standards over time. The mechanization of agriculture, the replacement of mechanical technology with electronics (in cash registers, adding machines, typewriters, and aircraft), and the growth of large retail stores all displaced workers. Recent technological change associated in part with increasing computerization is likely to have increased the demand for skilled workers across a broad range of industries, leading to a rise in the wages of skilled relative to unskilled labor (an issue discussed in Chapter 5).

Trade adds to the opportunities and dynamism of the economy, and to the adjustments required over time. Attempts to estimate the relative importance of international trade in economic restructuring have assigned a much larger role to technological change and other factors, but international trade competition has surely played a part, as discussed in Chapter 5. When import competition

Box 6–4.—The Gains from International Trade

By allowing each country to specialize in the production of the goods and services in which it is most efficient, trade raises the value of production and welfare in all trading countries. However, the gains from international trade go well beyond this basic tenet of comparative advantage. In industries where there are increasing returns to scale, international trade creates a larger market and lower unit costs, further raising the total output that can be produced. An integrated world market also allows technological development and production startup costs to be spread over a larger number of units.

But the largest gains from international trade may come from the competition that international markets provide. When competition is imperfect, the opening of markets to trade dilutes monopoly rents, lowering prices and raising output and welfare. International trade introduces new technologies (Box 3–7 in Chapter 3), spurs domestic producers to raise product quality, increases the range of goods available to consumers, and lowers product prices. A recent cross-country study of productivity at the firm level suggests that achieving and maintaining high productivity requires that companies compete directly against the best firms in the global economy, and evidence shows that, along with rates of aggregate saving and investment, openness to international trade is a significant determinant of faster growth. This is the reason why more and more developing countries have unilaterally lowered their trade barriers, and the search for higher growth was the primary motive for the Single Market Program of the European Union.

increases, there are pressures for protection to slow or halt the fall in production and employment in the affected industry. Indeed, many of the trade barriers in the United States and other developed countries arose to protect output in industries where employment was declining.

Raising or maintaining import barriers imposes costs on the rest of the economy through higher prices. Estimates place the total costs to consumers of U.S. tariff and nontariff barriers as high as $70 billion per year. Since protection often is applied to "cheap goods" or to consumer staples such as clothing and food products, these costs fall most heavily on the poor. The costs extend beyond consumers, to higher costs for other industries that use the protected products as inputs. Furthermore, one cannot reduce imports while leaving exports unchanged; overall levels of exports and imports are linked through the macroeconomic balance between national saving and investment and through the exchange rate. Thus, reducing imports would ultimately slow the growth of U.S. exports, upon which the jobs of over 10 million Americans now depend.

In addition to its high cost, trade protection is far from a solution to industrial adjustment. In most protected industries adjustment pressures arise from changing technologies and demand, and import protection has been able to slow employment declines only marginally. Estimated costs per job saved through protection run very high; one study put the average consumer cost per job maintained at $170,000, which is six times the earnings of the average U.S. worker.

The President's policy to "compete, not retreat" rests on the recognition that a dynamic economy, with its associated opportunities and despite its hardships, provides the best prospects for increasing incomes for Americans over time. The Administration has chosen to continue to press for further trade liberalization in order to open up foreign markets for U.S. exports, while at the same time vigorously promoting U.S. commercial interests abroad. But the commitment to embrace change requires a commitment to assist individuals when they are hurt by it. In other words, sound domestic policy is a necessary concomitant of sound international trade policy and reinforces the case for liberalization. Thus the Administration has advocated income support for those who lose their jobs due to trade displacement, as in the NAFTA Transitional Adjustment Assistance program, and has advocated greater investment in human capital, through programs of training and retraining, both to ease adjustment and to raise the incomes of Americans.

CONCLUSION

While recognizing the difficult adjustments that international trade may bring about, one should not lose sight of the significant gains that this country has reaped from its engagement in international markets. Since 1987, U.S. exports have grown at a rate of almost 10 percent per year in real terms, well outstripping export growth in Japan and the European Union, and reversing the decline in the U.S. share of world exports that occurred earlier in the 1980s. Export growth has been responsible for about one-third of total output growth since 1990, and it made the most recent recession considerably less severe than it otherwise would have been. As detailed in Chapter 2, export growth was a significant component in the strong performance of the American economy in 1994. Growth of exports has also been an important contributor in moving Americans toward higher paying jobs. The accompanying rise in U.S. imports has also been beneficial, providing consumers with more choices and raising the purchasing power of American incomes. Competition from abroad has made U.S. firms more efficient, more quality-conscious, and, in the end, more competitive.

The United States will continue to reap large gains from international trade. In the near term, recoveries in Europe and Japan will boost U.S. exports and help narrow this country's trade deficit. The longer term trends are also quite favorable for the United States. The positive changes in economic policy in many developing and transition economies will lead to faster growth and a sharp rise in their imports of capital goods, a sector in which U.S. competitiveness is very high. Both multilateral and plurilateral trade agreements have led to much larger reductions in the trade barriers of our partner countries than in our own already low barriers, and this will continue as APEC and the Western Hemisphere move toward free trade. The new areas that have recently been suggested for international negotiations—agriculture, services, intellectual property, competition policy—are all areas where the competitive balance is strongly in the United States' favor. Finally, strengthening of the underlying rules and the international dispute settlement system will lead to a convergence toward a rules-based, transparent, and nondiscriminatory world trading system, much like the one the United States already has. The balance of concessions and prospective gains from this convergence are greatly to our advantage.

This Administration will continue to pursue a more open world trading system, through multilateral, plurilateral, and bilateral trade negotiations. These negotiations will seek to lower barriers to trade in conventional sectors and to extend market liberalization to newer sectors and issues. Although we negotiate on a variety of levels, the basic goal is always the same: the advancement of open markets on a nondiscriminatory basis. This goal has characterized our bilateral negotiations, which have sought open markets, not special entry for American firms. In plurilateral negotiations we have emphasized the principle of openness to new entrants. The United States also has a strong interest in strengthening the underlying rules of the trading system and the dispute settlement process, both because to do so fosters more efficient and fairer trade, and because it results in the kind of system in which American firms most comfortably operate and compete.