the Atlantic

Ben W. Heineman Jr. - Ben Heineman Jr. has held top positions in government, law and business. He is the author of *High Performance with High Integrity* (Harvard Business Press, 2008).

High-Risk, High-Reward: Will Obama Seek a Free-Trade Pact With Europe?

By: Ben W. Heineman Jr.

December 11, 2012

Just after the New Year, President Obama will have to decide a whether to take a dramatic, high-stakes gamble on a very unsexy topic: a U.S.-E.U. free trade agreement. It will be one of the key high-risk, high-reward choices of his second term.

By removing all barriers on goods and by facilitating fairer and more transparent competition in services, investment, and public procurement, such an agreement could stimulate growth and increase jobs in the world's two largest economies, which together comprise more than 50 percent of the world's GDP.

Such economic benefits could occur without any additional government expenditure. An agreement could provide a needed, long-lasting jolt to the ailing economies on both sides of the Atlantic. It could avoid the dilemmas posed by the current policy choice between austerity at a time of anemic growth and stimulus at a time of fiscal disarray.

A high-level working group formed a year ago and made up of U.S. and E.U. officials is likely to recommend later this month that formal free-trade talks begin immediately. Already, European officials like British Prime Minister David Cameron, German Chancellor Angela Merkel, and various worthies at the European Commission have called upon President Obama to approve formal U.S.-E.U. trade negotiations.

But the risks for Obama are significant. Ideas to reduce barriers to U.S.-E.U. trade have bounced back and forth across the Atlantic for decades, with few results. Topics like harmonizing health, safety, and other regulations and reducing other national or regional preferences for trade in goods, services, investment, and procurement are still

contentious. Such a free-trade agreement must be a key administration foreign policy priority if it is to succeed (as NAFTA was), at a time when other parts of the globe and other global issues are clamoring for attention. And, even if they have priority status, formal talks hardly are guaranteed success (as shown in the stalled Doha Round of world trade negotiations).

The case for such talks begins with the potent existing relationship between the U.S. and E.U. economies -- a fact sometimes forgotten when all eyes are on China rising.

The flow of goods, services, and investment back and forth across the Atlantic accounts for one-third of global trade ($2 billion a day). In 2011, the U.S. sold three times more goods to the E.U. ($286 billion) than to China, and the E.U. sold two times more goods to the U.S. ($368 billion) than to China. In 2010, the US had $1.9 trillion of foreign direct investment in the E.U., and the E.U. had $1.5 trillion of foreign direct investment in the U.S. Fifty percent of U.S. overseas direct investment goes to the E.U. and 75 percent of the E.U. overseas direct investment goes to the U.S. Direct employment by U.S. businesses in the E.U., and E.U. business in the U.S., total close to 8 million, not including multiplier effects.

In general terms, the list of potential benefits from such an agreement is impressive, depending, of course, on how much of the trade and investment agenda is actually addressed.

- The economic consequences could be significant. A free-trade agreement could add half a percent to annual GDP growth in both the U.S. and E.U.. The elimination of all tariffs and halvling of regulatory, non-tariff barriers could mean an additional $250 billion in economic activity in the E.U. and $150 billion in the US. Job creation could number in the hundreds of thousands. And because so much transatlantic trade is between subsidiaries of single companies as part of supply chains, it could lower costs and make those companies stronger global competitors against newer multinationals from emerging markets.
- From a foreign-policy perspective, a free-trade agreement would signal to Europe that it remains a critical element in the American world view, at a time when America's public attention has been focused elsewhere. It would create and stimulate a powerful economic alliance at a time when international economics is an ever more vital component of national security. As such, it could act as a collective counter-weight to the growing economic influence of China: at present, the combined U.S./E.U. economies are almost three times bigger than China (US $15 trillion: E.U. $17 trillion; China $12 trillion). And, were the Obama administration to be successful in both a free-trade agreement with the E.U. and its current efforts to negotiate a Transpacific Partnership on trade, it could significantly shape the international economy for years to come.

- A U.S.-E.U. free trade agreement could set influential transatlantic standards on a variety of regulatory fronts which, while hardly front-page news, are critical to maintaining effective international competition and are now the source of endless

friction across the world. Standards in the areas of regulation of goods, services, investment, and procurement would help influence movement towards world regulatory standards (just as the recent U.S.-South Korea free trade agreement is viewed as state of the art).

- From a political perspective, the stars may be aligned on a complex transatlantic enterprise that has seen many false dawns. Republicans and business groups are, of course, generally in favor of an agreement. But because of the potentially stimulative effects and because the U.S. and E.U. have comparable wages and conditions for workers, labor groups on both continents and also left-center political parties have made favorable noises about launching a formal negotiation. Moreover, recent public opinion polls in the U.S. have consistently indicated a favorable view of trade with Europe, even as doubts about free trade generally have grown.

These positive general arguments run up against the realities of detailed negotiations at a time when poor economic conditions are stimulating national and regional protectionism, not economic liberalization for free markets, and at a time when the E.U. is struggling over the shape of a common set of monetary and fiscal policies. Arguments in favor of a free-trade agreement also have to overcome persistent, high visibility disputes between the U.S. and the E.U. These include: the E.U.'s resistance to genetically modified food and to hormone-treated beef; the U.S.'s "Buy American" procurement rules; agriculture on both sides of the Atlantic (U.S. subsidies and E.U. tariffs); endless debates about which region is unfairly subsidizing aircraft development (Boeing v. Airbus); U.S. refusal to allow foreign ownership in maritime and aviation industries; the E.U.'s stricter rules about privacy.

Any U.S.-E.U. negotiation would put these specific hot spots into a comprehensive framework. A phased, across-the-board reduction of remaining tariffs (averaging about 5-7 percent, although much higher for some products) is seen as an achievable goal by trade experts. But critical parts of the framework would involve detailed sector-by-sector attempts to reduce regulatory differences and other preferences that impede trade and investment. For example, trade in goods has specific regulatory barriers in autos, chemicals, drugs, electronics, and electrical machinery. Trade in services is critical, accounting for approximately 75 percent of GDP in both the U.S. and E.U. But, again, an agreement would have to harmonize or at least create greater convergence in parochial approaches relating, for example, to financial services, transportation, express mail delivery, telecommunications, wholesale and retail trade, and professional services. Opening public procurement to foreign tenders would mean addressing rules that, for political purposes, effectively bar such bidding. All these issues would entail hard, detailed slogging backed up by the political will from leaders on both sides of the Atlantic to get it done.

One of the critical political decisions will thus be to define terms of negotiation that are broad enough to achieve economic and foreign policy benefits and also to define a number of issues that are doable in order to gain momentum. Another critical decision

will be the end date of the negotiations. Some talk about 2014 or 2015. But that would still leave the complex politics of approval by both houses of Congress in the U.S. and by the institutions of the E.U. that are directly responsive to the 27 member states such as the Council of Ministers and the E.U. Parliament.

President Obama thus has a critical decision ahead of him about whether to make one his few second-term priorities a risky decision to seek a U.S.-E.U. trade agreement. If successful, this decision could have the reward, in the recent words of Secretary of State Clinton, of shoring up "our global competitiveness for the next century, creating jobs and generating hundreds of billions of dollars for our economies" and addressing the core of our national security -- "the economic future on both sides of the Atlantic."

Maybe President Obama will start this high risk-high reward process, get a negotiated agreement, but not get Congressional approval before the 2016 election cycle. Then, ironically, it could be left to a newly elected President Clinton to fight a U.S.-E.U. Free Trade Agreement through Congress in 2017 -- just as her husband had to fight NAFTA though Congress in 1994.

###

http://www.theatlantic.com/business/archive/2012/12/high-risk-high-reward-will-obama-seek-a-free-trade-pact-with-europe/266120/