

**“Trade Liberalization and Institutional Constraints on
Moves to Protectionism: Multilateralism vs. Regionalism”**

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Motivation

- **By simple metrics, GATT/WTO successful:**
 - **Increase in membership - 23 (1947) to 164 (2018)**
 - **Average industrial tariffs reduced to less than 4%**
 - **Rules-based system and dispute settlement accepted and respected by members**
- **Significant impact on trade volumes in manufacturing and agricultural sectors (Subramanian and Wei, 2007; Grant and Boys, 2012)**
- **Growing emphasis on “deep” integration through regional trade agreements (RTAs) (Baldwin, 2016)**
- **If Pareto-improving – why leave/undermine cooperative agreement(s)?**

Economic Logic of GATT/WTO

- **Seminal approach to modelling GATT/WTO due Bagwell and Staiger (1999)**
- **If countries are able to influence their terms-of-trade, unilateral incentive to raise tariffs beyond what is “politically-optimal”**
- **Nash equilibrium tariffs inefficient as countries would like to lower tariffs in order to reduce domestic distortion and generate more trade**
- **GATT/WTO is cooperative solution to cost-shifting externality, i.e., countries offer reciprocal tariff concessions without changing world relative prices**
- **Practical implication: negotiations are about reciprocal exchange of market access**

Economic Logic of GATT/WTO

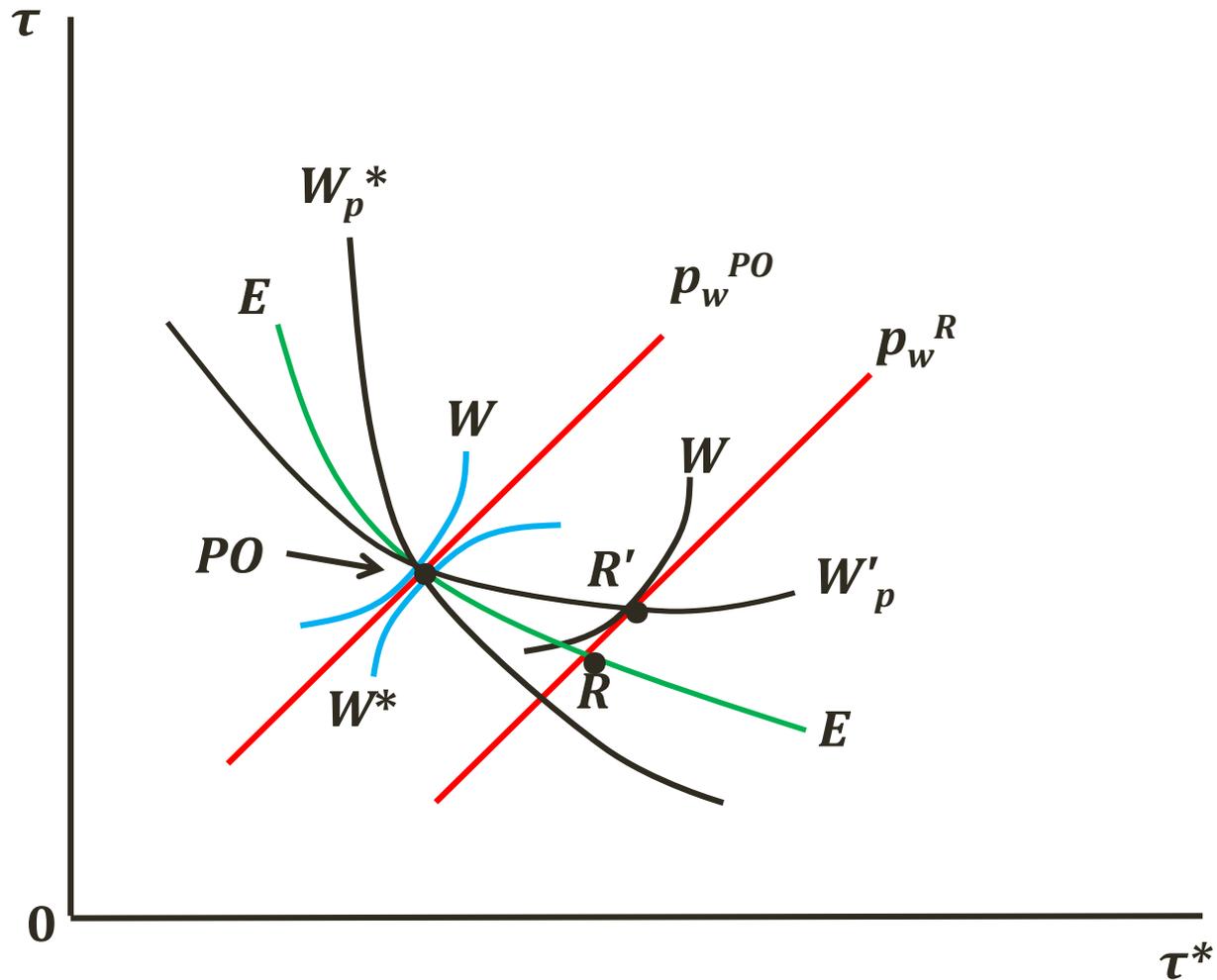
- **Reciprocity also helps explain idea behind “withdrawal of equivalent concessions” as part of dispute settlement**
- **Credible punishment for deviation from low-tariff equilibrium is reversion to Nash - in practice, rules of GATT/WTO seek to maintain balance of concessions and avoid punitive action (Zissimos, 2007)**
- **Objective is to ensure retaliation is proportional, minimizing chances of trade war**
- **Tariff concessions also applied on MFN basis – in combination with reciprocity, minimizes risks of third-country spillovers and prevents preference erosion (Bagwell and Staiger, 2010)**

Can US Trade Policy be Rationalized?

- If on efficiency frontier, and policies have been politically-optimal, it *cannot* be Pareto-optimal to raise tariffs
- US may be on efficiency frontier, but political preferences have changed enough in favor of *renegotiation* – why the change in preferences?
 - More weight attached to import-competing sectors and/or world price has fallen below *reference* price
 - US seeks “more reciprocal” tariffs with countries where it has a trade deficit
 - US does not appreciate “latecomers” problem
- US approach is unilateral based on notion that trade agreements are a zero-sum game

Economic Logic of GATT/WTO

Tariff equilibrium



US Trade Policy and Regionalism

- **US appears interested in regionalism rather than multilateralism, e.g., NAFTA renegotiations**
- **Decision puzzling in context of NAFTA renegotiating objectives (deep integration) and pulling out of TPP**
- **Current US brand of regionalism is probably better described as bilateralism though – echoing view of multilateralism as a zero-sum game**
- **Reflected in US position on Chapter 19 of NAFTA, and its application of countervailing duties in aircraft sector**
- **Objectives of NAFTA renegotiations suggests progress could be made in lowering trade barriers, but its actual approach may ultimately be self-defeating**

WTO Dispute Settlement and Protection

- **US political preferences may have changed, but institutional features of WTO have not**
- **System likely cannot be used effectively to counter current US policies:**
 - **Injury must have occurred before any relief is possible**
 - **If injury is proven, aggrieved member can seek compensation, but US may refuse to provide it**
 - **WTO can authorize retaliation – but US may simply refuse to comply and live with it, and even impose counter-retaliation measures**
- **Consequently, there may be little WTO can do to deter US economic nationalism**

Takeaways

- **Underlying economic logic of GATT/WTO is still relevant**
- **Enforcement of cooperative agreement will be placed under significant strain with threat of increased US trade protection, and even potential trade war**
- **Multilateralism is also under threat from US approach to regionalism, i.e., bilateralism based on idea that all trade agreements are a zero-sum game**
- **WTO has well-defined enforcement/legal mechanisms in place to handle disputes, but they probably cannot contain an all-out trade war**
- **RTA dispute settlement mechanisms are also weak at best**