AMERICAN INSTITUTE FOR CONTEMPORARY GERMAN STUDIES THE JOHNS HOPKINS UNIVERSITY

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SEPTEMBER 2018

Making the Atlantic Great (Again)? Prospects for New U.S.-EU Trade Negotiations

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Does the idea of narrowing the economic divide across the Atlantic have enough enduring power to prevail in an era of "America First"?

Is there an interest-based, "realist" case for transatlantic economic cooperation?

Can the traditional, all-or-nothing model for a U.S.-EU free trade agreement succeed in an era of impatient politics?

The idea of a free trade agreement between the United States and the European Union can seem at once inevitable and impossible. Over the last twenty-five years, as the EU has grown from fifteen to twenty-eight member states to become an economic superpower, the multilateral trading system enshrined in the World Trade Organization has turned more ungovernable. As a result, the logic of leveraging a transatlantic economic pact that would encompass nearly half of global GDP to bolster and reform the seventy-year-old rules-based, liberal economic order has become increasingly compelling.

At the same time, however, the very complexity involved in bringing together two economic giants, roughly equal in size, each convinced of the superiority of its commercial, financial, and regulatory model, presents a daunting task to practitioners of economic statecraft. It should not be forgotten that even without a free trade agreement (FTA), the transatlantic economy has become deeply integrated to the tune of more than $1 trillion in annual trade in goods and services, a foreign investment stock of $5 trillion, and 9 million jobs directly created by U.S. and EU companies in each other's market. Given this impressive market-driven inter-weaving of the two economies, it is legitimate to ask whether the U.S. and the EU need to be in a hurry to formalize their relationship through an FTA.

A Pendulum Swing in Transatlantic Economic Relations

This push and pull—between the imperative of transatlantic unity faced with a more unruly global economy and the forces of inertia that rise up when the awesome task of integrating the mammoth U.S. and EU economies comes closer into view—forms the backdrop to the decision by President Donald Trump and European Commission President Jean-Claude Juncker at their White House meeting on July 25 of this year to launch a process aimed at reducing transatlantic trade barriers. Among the goals the two leaders set for themselves are to eliminate tariffs, non-tariff barriers, and subsidies on most industrial goods, and to increase trade in services. That exchange also established an Executive Working Group composed of senior U.S. and EU officials whose first meeting took place on August 20 in Washington.

The July 25 meeting is a clear sign that the pendulum in U.S.-EU economic relations is shifting again—away from concerns about the risks inherent in the complex task of trying to deepen bilateral trade relations and toward appreciation of the opportunities that a more seamless transatlantic market can offer both sides. That this phenomenon is occurring under a president who has taken the U.S. out of one major trade agreement (the Trans-Pacific Partnership or TPP) and threatened to do the same for another (the North American Free Trade Agreement or NAFTA) is a striking demonstration of the enduring power of the idea of narrowing the economic divide across the Atlantic.

While this re-found enthusiasm for strengthening transatlantic economic ties holds promise, both the United States and the European Union have learned from experience that progress is not guaranteed. This most recent attempt to liberalize trade between the U.S. and the EU is the third in just over ten years, and neither of the previous two can be deemed an unmitigated success.

The Legacy of Past Talks: A Modest Harvest…And Seeds for the Future

The Transatlantic Economic Council (TEC), which was established in 2007 under President George W. Bush with key backing of German Chancellor Angela Merkel, aimed to reduce the non-tariff barriers to trade between the U.S. and the EU, such as differing approaches to standard setting, testing, and compliance. More than tariffs, it was the lack of common regulatory practices that was deemed to be holding back the realization of the full potential of transatlantic commerce.[1] But the TEC made little progress, owing to the slow-going, technical nature of the matters being negotiated, the participation of regulatory agencies unused to putting trade liberalization on a par with purely domestic concerns, and the lack of high-level political support for its agenda.

The Transatlantic Trade and Investment Partnership (TTIP) launched in 2013 by President Barack Obama and EU Commission President José Manuel Barroso established the high watermark of ambition in the U.S.-EU bilateral relationship. Here were the two largest economic blocs in the world proposing to achieve a comprehensive free trade agreement with the three major goals of facilitating market access in trade in goods and services, aligning approaches to regulation, and forging rules to respond to common global economic challenges.

A U.S.-EU free trade agreement—once feared as a potential deathblow to the multilateral trading system because of the sheer size of the two participating economies—was now heralded as the one remaining avenue to preserve the spirit and accomplishments of that very system. A geoeconomically ambitious view of TTIP saw the U.S. and the EU as its starting point, to be followed by its expansion to important, like-minded economies around the Atlantic perimeter (Canada, Mexico, Turkey, Switzerland, Brazil, Argentina). These countries would form the core of a new, high-standard global trading platform that China's state-capitalist model would have to adapt to and that could later be integrated into the WTO.[2]

Neither the U.S. nor the EU has officially withdrawn from the TTIP negotiations, but by the fall of 2016 they had hit a rough patch caused in large part by issues relating to investment protection, public procurement, and agriculture. The decision in June of that year by the United Kingdom to leave the EU and the election of Donald Trump that November—both signs of growing public concern about the terms of regional and international economic engagement—contributed to an attitude of benign neglect toward the talks that has prevailed since.

While the TTIP talks stalled and are not likely to be revived in their original form, much was accomplished during three years of negotiations that can be taken up by the new Executive Working Group. Of the twenty-seven chapters under negotiation, in April 2016 the European Commission considered eighteen of them to be in either an "advanced state of consolidation" or on the way to that goal. These included politically significant areas in the rules chapter like competition policy, facilitating the participation of small- and medium-sized enterprises in world trade, and the role of state-owned enterprises.[3]

Bilateral Tensions, Diplomatic Convergence

As the new U.S.-EU trade talks begin, there are two distinct dynamics that will shape their course. On the one hand, there is the fraught nature of the bilateral relationship. In June of this year, the Trump administration included the EU in the tariffs it placed on imports of steel and aluminum as a way to protect U.S. national security, something that the EU—composed mostly of NATO allies—found hard to fathom. Spurred on by presidential frustration about the volume of car imports from Europe and in particular from Germany, the U.S. Department of Commerce has also opened an investigation into whether foreign-made automobiles pose a threat to national security. More broadly, the current White House appears to view trade balances not as a reflection of savings, investment, and consumption patterns but rather as a gauge of who is winning and losing in international commerce. Germany—which maintains the world's largest current account surplus—is clearly a key source of irritation for the administration.

In parallel with these strains in bilateral ties, however, an emerging effort at joint diplomacy can be discerned, one that stems from the common U.S.-EU interest to push back against China's trade practices and to create greater fairness in the global economy. In the joint statement following their July 25 White House meeting, Presidents Trump and Juncker made such cooperation a key feature of future U.S.-EU talks, pledging to "reform the WTO and to address unfair trading practices, including intellectual property theft, forced technology transfer, industrial subsidies, distortions created by state owned enterprises, and overcapacity."[4]

The groundwork for this high-level commitment was laid by a series of three meetings among U.S. Trade Representative Robert Lighthizer, European Trade Commissioner Cecilia Malmström, as well as Japanese Minister of Economy, Trade, and Industry Hiroshige Seko to address Chinese trade practices that began at the December 2017 WTO ministerial meeting in Buenos Aires and were followed up in Brussels in March and Paris in May of this year.[5] While neither the Trump-Juncker statement nor the communiqués following the trilateral meetings of trade ministers mentioned China explicitly, the intent is clear.

More direct evidence of transatlantic cooperation on China can be found in the support the U.S. provided to the EU in November 2017 at the WTO in a case centered on whether Beijing should be granted "Market Economy Status" within the multilateral trade body. A finding in favor of China acquiring that status could considerably constrain the ability of the U.S. and the EU to push back against China's subsidized exports and other market-distorting policies.[6]

The "Realist" Case for Transatlantic Economic Cooperation

Although there appears to be growing appreciation in Washington of the value of U.S.-EU cooperation to improve global trade rules, the Trump administration's view of international relations is a challenging one for transatlantic cooperation. Unlike almost all previous administrations since World War II, the starting point for the Trump White House when it looks across the Atlantic does not appear to be shared U.S.-European values such as democracy, the rule of law, and a liberal world order but rather how the European Union fits into a desire to expand U.S. power. As a consequence, if U.S.-EU trade cooperation is to be a success during the Trump presidency it will need to be consonant with this muscular version of foreign policy "realism," one that sees the world as a nearly irredeemable arena of competition for dominance.

While caution is in order, the emerging U.S-EU efforts at joint engagement on China may demonstrate that even a U.S. administration that puts "America First," that jealously guards the country's national sovereignty, understands that to achieve its preferred policy goals some of the means to that end will have to be supplied beyond U.S. borders. The Trump administration may hold dear the assertion of U.S. power; the fact remains that there is not enough of it to go around—certainly not enough to reshape the global trading system in a way that more durably advances U.S. interests.

The European Union has its own interests, of course, and while it shares an ambition with the United States to rein in the predatory aspects of China's state-capitalist model, it differs with the U.S. administration on the value of upholding the existing global economic order. By and large, the EU views the rules-based trading system rooted in the WTO, in the hundreds of FTAs countries around the world have entered into, and in the informal set of norms and practices promoted by the OECD, the G7, and the G20 as supportive of both its economic prosperity and its global economic influence. President Trump, on the other hand, has decried his country's existing FTAs as "bad deals" and expressed his dissatisfaction with U.S. participation in many leading international economic organizations—especially the WTO, which he sees as curtailing U.S. global economic might.[7]

If these latest U.S.-EU trade talks are to stand a chance of success they will have to be firmly rooted in a case-by-case way in their common economic interests. The priority should be on aligning each other's policies on key issues like the behavior of state-owned enterprises, technology transfer, or localization requirements for investment and innovation in a way that multiplies their effect. This could be done through informal coordination of domestic policies (such as foreign investment screening or competition policy), mutual support in WTO cases, common approaches in their respective FTAs with third countries, as well as a bilateral U.S.-EU agreement that included a vigorous rules chapter.

Reform of the World Trade Organization can and should also be on the agenda if for no other reason than there exists no ready-made replacement for the Geneva-based organization for ensuring that international trade takes place in an orderly, rules-based way. The alternative is the law of the jungle, which would hardly guarantee happy outcomes for the U.S. and its close trading partners like the EU, which, unlike authoritarian states, are constrained in their actions by the checks and balances of democratic politics. But as modernizing the WTO so that it better accounts for the impact of China's state capitalism on the global trading system is likely to be a long process, it may not be wise to make it the test case for transatlantic cooperation in an era of impatient politics.

What About the Transatlantic Market?

Beyond joint economic statecraft to address the challenge from China, the other main thrust of new U.S.-EU trade talks will have to be the transatlantic market itself. While bilateral trade tensions like the national security based tariffs on EU steel and aluminum, the EU's counter-tariffs, the investigation into a similar tariffs for automobiles, and Trump's unhappiness with Germany's trade surplus present a dispiriting backdrop for liberalizing transatlantic trade, there should nonetheless be common ground. U.S. and EU tariffs on each other's goods are low, on average around 2 percent. But given the size of the enormous transatlantic market, and that 50 percent of goods trade across the Atlantic takes place between branches of the same firm,[8] a U.S.-EU zero-tariff deal would contribute considerably to transatlantic prosperity and to the global competitiveness of U.S. and EU companies.

The July 25 Trump-Juncker joint statement also mentioned non-tariff barriers to trade. The failure of the TEC to meet its expectations suggests that aligning regulations would be the work of years. And even though U.S. and EU levels of health, safety, and environmental protection are roughly the same,[9] because of deeply rooted cultural differences about risk tolerance it is worth asking if in many areas (food and chemicals, for example) common regulatory ground could ever be found.

With the U.S. administration expressing an interest in reducing transatlantic trade barriers on an accelerated timetable,[10] the Executive Working Group is likely to recommend that instead of using the traditional negotiating framework for a free trade agreement—where nothing is agreed until everything is agreed—the two sides commit to several parallel tracks of talks, allowing each issue to be harvested according to its own individual calendar. The hope would be that such a process produces enough early "wins" for each side—political commitments covering a few specific industrial goods sectors—that confidence builds to tackle more politically contentious areas, such as agriculture or government procurement, leading ultimately to a full-scale FTA. Perhaps this more modest and practical approach will offer a way to turn the transatlantic pendulum, swinging without success between inevitability and impossibility, into something more akin to a steady state.

With a multilateral trading system that has become more ungovernable, the logic of a U.S.-EU pact is compelling—but the lesson of the past ten years is that forging closer transatlantic trade ties will require a tremendous investment of statecraft.

While the U.S.-EU bilateral relationship is strained, there is an emerging convergence on economic diplomacy as even a power-maximizing U.S. administration may see the value of allies to counter Chinese state capitalism.

Instead of single-track free trade negotiations, which could take years, the U.S. and the EU may opt for political agreements on individual industrial sectors providing short-term "wins" for both sides that can later be built into a broader deal.

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This publication is made possible by the generous supporters of the AICGS Geoeconomics Program.

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