ST 24 Dec 2008

Obama will have to make trade a major priority

By Deborah Kay Elms
For The Straits Times

COMMON wisdom suggests that incoming US President-elect Barack Obama is not an enthusiastic supporter of global free trade. One of his early choices to serve as the US Trade Representative, Mr Xavier Becerra, backed out of the job because he perceived the role would be insufficiently important in an Obama Administration. Mr Obama has named former Dallas mayor Ron Kirk instead. He has limited experience in international trade.

This choice does suggest that the incoming administration does not intend to have trade play a major role, as Straits Times senior writer Tion Kwa argued yesterday. Yet events will likely push the United States to give trade a much more prominent position than currently envisioned.

The depth and extent of the financial and economic meltdown in the United States cannot be overstated. Vice President-elect Joe Biden has warned that the economy might "tank" in the short term, without vigorous government support.

To address these problems, Mr Obama has chosen a team of heavyweight economic advisers. He has directed them to focus first on stimulating the economy and creating millions of new jobs. Mr Biden has suggested a spending bill of up to US$800 billion (S$1.1 billion) will be forthcoming in January.

In this environment, international trade might seem more like a luxury good than a necessity. Yet events in the past month suggest this attitude will change rapidly. In November, global leaders pledged to refrain from embracing protectionist policies at an emergency summit in Washington devoted to the economic crisis.

Within days of this pledge, state after state backed away from free trade and instituted subsidies for export industries or raised new barriers to imports. Exports are plunging worldwide, including in Japan, China, New Zealand and Thailand. Indonesia has begun requiring new import licenses and has imposed additional fees on a wide range of products. India raised duties on soya beans. Others have instituted new laws and requirements on foreign investment.

Russia has raised tariffs significantly on a range of products. Given that Russia is the largest market for US poultry products, this action will harm American farmers. Riot police were called out in Vladivostok to break up protests over new rises in import duties on automobiles.

The US has not been immune to domestic pressure for relief. The on-again, off-again bailout of the US automotive industry can be seen as a government subsidy for domestic manufacturers. The terms available to General Motors, Chrysler and Ford are not available to foreign manufacturers, making it probably illegal under World Trade Organisation rules. Russia and other states may choose to intervene in similar ways to assist their own domestic car producers.

With each action, the world slips closer to one closed from international trade. The global and domestic consequences of these actions will be significant. The Great Depression of the 1930s was more about protectionist closures of international markets than about domestic financial meltdowns.

For a country like Singapore, which is very open to global trade flows, the implications of closing markets will be felt quickly and painfully. The pain will not be confined to only small economies, however, as global integration and interconnected supply chains mean that even the largest states are dependent on free movement of goods and services.

Stimulating domestic demand sounds very good to government leaders from Washington to Beijing. The reality, however, is that their domestic consumers are unlikely to demand sufficient quantities of goods and services (even assuming that these could be produced domestically) to drive the economy forward in the short term. Instead, the largest markets like the US, the EU, China and Japan, need each other.

Open trade is critical for smaller states like Singapore. The domestic market will never be of sufficient size to provide the kinds of jobs and incomes or goods and services that citizens desire and producers depend upon.

Developing states are equally dependent on open trade. Their domestic consumers cannot buy enough commodity products, textiles, or footwear to keep their farms, mines and manufacturing sectors humming. And most developing states are reliant on external markets for more advanced goods and services. A turn towards protectionism will be catastrophic for most. Without openness, they will see growth rates plunge.

In this environment of rapidly closing markets and rising barriers, global trade will increasingly be seen as a major priority for Mr Obama. It may not have started out as one, but he will have to address closing markets in a hurry. Otherwise, the world economic situation may continue to deteriorate for far longer.

The writer is head of the Temasek Foundation Centre for Trade & Negotiations, Rajaratnam School for International Studies, NTU.