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EU-US Trade Conflict: Transatlantic Policy Impact

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European Union–United States Trade Conflict: Transatlantic Policy Impact

Melanie Goergmaier*

Abstract:

From the Transatlantic Trade and Investment Partnership (TTIP) to the Trump Trade War, this paper will examine the historic transatlantic trade relationship between the EU and the US and the policy impact on both sides of the Atlantic. This paper will also provide policy recommendations for both sides on how to move forward based on the analysis. An outlook will be provided as well including trade history between the two entities over the years up until the current 2019 trends.

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EU-US Trade War: Transatlantic Policy Impact

International Trade Regime negotiations between the United States and Europe began in the 1940s. The goal of the conference held at Bretton Woods, New Hampshire in July 1944 was to agree on a set of institutions to regulate international trade and monetary relations. U.S. and UK policy makers drew important lessons from the previous century: international economic integration in the pre-1914 eras was worth emulating and a more open international economy requires purposive cooperation only sustainable with strong domestic political support for governments. Therefore, bilateral talks extended into multilateral negotiations in 1945. By 1947, negotiations had created an agreement on the postwar trade system. The International Monetary System was implemented with a fixed exchange rate system, the International Monetary Fund (IMF) and the World Bank. The implementation of an International Trade Organization failed which led to a General Agreement on Tariffs and Trade (GATT) for the international trading system embodying liberal ideas about the benefits of free trade. In addition, it may have also been of economic interest to the United States. The goal of the General Agreement on Tariffs and Trade (GATT) was to promote freer and fairer trade through negotiated reductions of formal tariffs according to two main principles: reciprocity (mutual balanced concessions) and multilateralism (trade rules extended without discrimination to all members). Unilateralism, bilateralism and trading blocs were prohibited except in certain circumstances (human rights violations, war etc.). The Bretton Woods Monetary System had fixed exchange rates. All currencies at the time of establishment were pegged to the dollar, which was pegged to gold. The International Monetary Fund was created to monitor national economic policies and to extend balance of payments financing to countries at risk using contributions from members to offer reserve credits to states with international payment problems. The World Bank provided financing for reconstruction of Europe after World War II. The goal was to achieve both national autonomy and international stability created by the fixed or pegged exchange rates, while still allowing sufficient flexibility to enable individual states to deal with extraordinary situations. The basic principle was to create multilateral surveillance through international institutions and institutional specialization at the international rather than the regional level. In addition, the non-discrimination policy goal was to create transparency for tariffs according to the GATT/ IMF. The GATT was emphasized on border controls and did not restrict domestic regulatory intervention. The Bretton Woods System allowed capital controls and national autonomy over exchange rate pegs – a product of postwar Keynesian views in the UK. Postwar regimes were characterized by very liberal formal principles (multilateralism and non-discrimination) at the international level with considerable scope for domestic interventionism (informal norms), particularly in macroeconomic management and social insurance policies. Therefore, the Bretton Woods compromise consisted of embedded liberalism including the following: economic middle ground between globalism, national economic management, free markets and government intervention; political class compromise among big businesses, labor and the middle class, ideological between the center left and the center right against extremes of fascism and communism, gradualism and exceptions for politically controversial measures.

In order to analyze the current situation, this paper will draw from recent history regarding proliferation of Regional Trade Agreements (RTAs) in the international trading system. The formation of regional trade agreements has been, by far the most popular form of reciprocal trade liberalization in recent decades. The discriminatory character of these agreements has raised three main concerns: first, that trade diversion would increase, because special interest groups would induce governments to form the most distortionary agreements; second, that broader external trade liberalization would reverse and third, that multilateralism could be undermined.

Various scholars have debated throughout the 20th century whether RTAs are “trade creating or “trade diverting”¹. Trade creation is the increase in intra-regional trade by shifting resources from inefficient domestic suppliers to more efficient producers in the region. Trade diversion is the increase in intra-regional trade by shifting resources from efficient external producers to inefficient producers in the region. Some

¹ Viner, Jacob. “Power Versus Plenty as Objectives of Foreign Policy in the Seventeenth and Eighteenth Centuries.” *World Politics* 1, no. 1. October 1948: 1-29.

scholars argue that RTAs should be referred to as Preferential Trading Agreements (PTAs) and are trade diverting and not creating. Bhagwati argues that RTAs are “Termites in the Trading System”² and therefore should be viewed as “stumbling blocks” and a form of protectionism as opposed to “building blocks.”³ On the one hand, scholars view RTAs as Building Blocs due to less actors involved leading to easier and faster negotiations, because RTAs tend to go further than tariff reductions and are “open”, hence compatible with multilateralism. On the other hands, scholars argue that RTAs are stumbling blocks, as they are inward-looking and protectionist, discriminatory (against WTO goals). Bhagwati argues that the surge of RTAs has led to a “spaghetti bowl effect” of trade agreements. This “spaghetti bowl” does not just exist between the US and Europe, for example, but it exists in Africa as well. In addition, an “East Asian noodle bowl” exists.

In “A Domino Theory of Regionalism,” Baldwin argues that RTAs discriminate against third parties⁴. In terms of economic laws, David Ricardo developed the concept of comparative advantage⁵. It is important to note that the RICARDO-Viner model assumes that factors (labor and capital) are immobile and do not move⁶. A brief example will help explain this concept. A country produces two goods: shirts and cars. This country, however, might have a comparative advantage for various reasons in shirts and, therefore, should focus on producing shirts instead of both shirts and cars. This will enable a country to optimize efficiency and produce more shirts. The country can import cars from another country that is more efficient in building them. RTAs — or PTAs — could technically violate the laws of comparative advantage. Three countries, for example, might join a RTA for political reason and forgo including another country for political reasons. However, perhaps the fourth country is more efficient and has a comparative advantage in a very useful product. For example, country X might produce cars much better than country Y, but country Y is accepted into the RTA, because it is a political ally with the other two countries in the agreement. This is an example of how politics can play a role in RTAs and hinder what — at least economically — would be a better arrangement for all parties in the RTA. Bhagwati also is very critical of “natural trading partners.”⁷ The question becomes the following: what constitutes a region? The term region is sometimes loosely used and does not have to do with geographic proximity. A country might appear to be a natural trading partner because it is close in proximity. How one perceives a country is a constructivist issue⁸, as will be discussed below in further detail.

Regionalism refers to the negotiation and construction of interstate or intergovernmental agreements or regimes, involving specific and conscious policy decisions by governments to coordinate economic and political activities within a region.⁹ Regionalism can be defined as a regional inter-state cooperation and is a special case of international or global cooperation. Different sectors and areas of regionalism include security/ politics, economic (preferential trade agreements) and environmental issues. Regionalism is a “political process of cooperation and coordination on economic policy among states”¹⁰. Multilateralism on the other hand is the idea that “Most Favored Nation”, should be applied to all states, and avoid discriminatory practices at all costs. PTA’s or Preferential Trade Agreements are agreements in which states cooperate on economic policy as it pertains to trade. There are two types of PTA’s: Customs Union and Free Trade Agreements. CU’s are agreements that have no internal barriers to trade and impose

² Bhagwati, Jagdish. *Termites in the Trading System: How Preferential Agreements Undermine Free Trade*. Oxford University Press, 2008.

³ Bhagwati, Jagdish. “Regionalism versus Multilateralism.” *World Economy* 15, no. 5, 1992: 535-56

⁴ Baldwin, Richard. “A Domino Theory of Regionalism.” *NBER Working Paper Series*, 1993, 4465.

⁵ Ricardo, David. *The Principles of Political Economy & Taxation*. Everyman’s Library. Science, No. 590. Dent: Dutton, 1911.

⁶ Ishikawa, Jota. “The Ricardo-Viner Trade Model with an Intermediate Good.” *Hitotsubashi Journal of Economics* 41, no. 1, 2000: 65-75.

⁷ Bhagwati, Jagdish Natwarlal. 1992. “Regionalism Versus Multilateralism”. *World Economy*. 15: 535-555.

⁸ Wendt, Alexander. *Social Theory of International Politics*. New York: Cambridge University Press, 2014.

⁹ Fawcett, Louise L’Estrange., and Andrew Hurrell. *Regionalism in World Politics: Regional Organization and International Order*. Oxford [England]; New York: Oxford University Press, 1995.

¹⁰ Mansfield, Edward D., and Helen V. Milner. “The New Wave of Regionalism.” *International Organization* 53, no. 3 (1999): 589-627.

a common external tariff to outside states. Free trade agreements on the other hand also have no internal barriers to trade, but do not impose a common external tariff on outside states.

Regional trade agreements are complimentary to the objectives of the General Agreement on Tariffs and Trade (GATT). Article XXIV of the GATT allows Free Trade Areas (FTAs) and Custom Unions (CUs) to exist as long as trade barriers do not rise on average after integration, agreements eliminate all tariffs and other trade restrictions on intra-regional exchange of goods and agreements are notified to the GATT, which may decide to establish whether these conditions are satisfied.

The last several decades have witnessed a proliferation of RTAs in the international trading system. As of 2006, 214 Regional Trade Agreements (RTAs) were active and in force¹¹. In 2010, the World Trade Organization (WTO) estimated that 271 RTAs existed around the world. Since the WTO came into being, the number of Regional Trade Agreements (RTA) in existence rose from 100 to over 300. According to the WTO, already 379 RTAs were in force as of 2013. Almost every country in the world has membership in at least one RTA. They have become a major international regime that demands attention. RTAs are fundamentally trade agreements, which discriminate between members and nonmembers. Nations who participate in these blocs eliminate tariffs on goods entering their markets from their FTA partners, but each member retains independent tariffs on goods entering from non-FTA members. In a world economy governed by the WTO and the reduction of tariffs barriers to trade, in which 164 countries are members¹², how is this possible? Why are RTAs so popular? Does the existence of RTAs destroy multilateral economic relationships around the world? Do RTAs discourage or promote free trade? What are the ramifications for the future?

The major principle of the General Agreement on Trade and Tariffs (GATT) was the Most Favored Nation clause (MFN), which requires the same rights to be given to every country in a trade agreement. The MFN is designed to avoid discrimination and preferential treatment. Article 24 of the GATT, however, allows Regional Trading Agreements. Based on this, some economists argue that RTAs are a “building block” and should be viewed as a positive, because they promote trade and exchanges between countries. In other words, RTAs are positive because they promote trade, and trade is better than protectionism.

Old Regionalism started shortly after the end of World War II with the European Integration from the late 1950s until the 1970s imposed from the outside by the superpowers. It was characterized by Cold War logic including the following: introverted and protectionist, specific and narrow objectives, exclusive in terms of membership, state-centric and state-dominated (Neofunctionalism, Intergovernmentalism). The resurgence of regionalism in the 1980s and 1990s was considered Post-Cold War Regionalism from a Mainstream International Relations Approach (Neorealism, Neoliberal Institutionalism). New Regionalism is based on post-Cold War logic as well. However, the approach is based on Constructivism and post-positivist theories, as it is often developed from within the region. It is inclusive, open, and linked with globalization guided by comprehensive and multidimensional objectives such as economics, politics and security involving the state, the market and civil society actors worldwide. Institutionalism places emphasis on the functions that regimes perform for states and view regional institutions as a joint attempt by states to manage the problems generated by increased interdependence (e.g. NAFTA). Realists explain the resurgence of regionalism with external balancing arguments (regional blocs are formed as a response to external or extra-regional threats or challenges). Constructivists argue that regional cooperation creates “shared identity” (of regional elites) leading to the emergence of self-sustaining integration (regional identity/ sense of community). At the domestic level, regional cooperation can also be driven by the preferences and goals of governments (Statist argument) or driven by the preferences of business groups (Interest Group Explanations).¹³ Tariffs reflect a balance of supply and demand for protection (political economy explanation). The formation of RTAs re-aligns political economy forces in non-members (due to discrimination) resulting in a pressure for either joining or creating a new RTA. If a new member joins an existing RTA, forces for inclusion get stronger in non-member nations (Domino Effect). The original trade

¹¹ Fiorentino, Roberto V., Christelle Toqueboeuf, and Luis Verdeja. *The Changing Landscape of Regional Trade Agreements: 2006 Update*. Geneva, Switzerland: World Trade Organization, 2007.

¹² World Trade Organization. *Members and Observers*. Accessed May 1, 2019.
https://www.wto.org/english/thewto_e/whatis_e/tif_e/org6_e.htm

¹³ Baldwin, Richard E. *A Domino Theory of Regionalism*. 1993

of goods turned into international investment in production facilities, training, technology and long-term business relationships utilizing infrastructure services such as telecoms, internet, express parcel delivery, air cargo, trade-related finance, etc. in order to coordinate the production process. As a result of these changes, the demand for deeper integration rules arose resulting in 21st century regionalism¹⁴. New international risks and threats to property occurred as firms began doing business abroad (behind the border barriers). In addition, obstacles arose to flows of goods, people, ideas and investment required to coordinate international production facilities (cross-border barriers). Incentives to remove these 21st century barriers are the source of demand for more complex trade disciplines. Since the WTO was otherwise occupied, this demand was filled by deeper RTAs and unilateral reforms. There are four deeper disciplines that appear in these RTAs, but not in the WTO: competition policy, movement of capital, intellectual property rights and investment assurances.

The advantages of RTAs outweigh the disadvantages. However, every argument has validity. Most RTAs are, in fact, created for power and protectionist reasons (Realist argument). However, the cultural factors are even more influential. The fact that a sense of community is created weighs even more. Therefore, the constructivist argument is the strongest.

President Obama and Secretary of State John Kerry demanded a free trade area of the Atlantic-Initiative for Europe and the US in 2013. By 2016, the negotiations were supposed to be completed (degradation of e.g. subsidies for export of agricultural products, the removal of customs duty, elimination of demanded import restrictions, disappearance of visa requirements, etc.). A trade area of 800 million dollars and millions of new jobs was intended to arise. Mutual trade would have been greatly increased.

Many have raised concerns about the rapid increase of RTA's and assert that their complex frameworks have created an overlap in policies and have stunted the progress of multilateralism. Others attest that RTA's enhance the multilateral system by providing necessary reform to countries who seek to become more integrated. Bhagwati asserts that PTAs are here to stay and are not going to disappear. He argues that RTAs have occurred in different waves. The "first wave of regionalism"¹⁵ occurred during the 1960s. Functionalism theory¹⁶ in connection with the European Integration Theories explains the development of the European Coal and Steel Community (see Treaty of Paris 1952) and the attempts to promote integration with the foundation of the European Economic Community (see Treaty of Rome 1957). Neofunctionalism refers to the positive spillover effect democracy and institutions can have on other states triggering more and more states to cooperate based on benefits such as peace, trans-national trade, and economic prosperity¹⁷. Intergovernmentalism, initially proposed by Stanley Hoffmann, was refined into Liberal intergovernmentalism as an explanation for the foundation of the European Union in 1992.¹⁸ In "the first wave of Regionalism," the US, contrary to Europe, promoted multilateral trade. However, Bhagwati coins the term standing on "Two feet.", because today, the U.S. tends to focus more on FTAs as a form of trade.

In the most recent wave of regionalism today, the US is a major player in RTAs. One could use Hegemonic Stability Theory (HST) to explain the current situation in connection with the U.S. being considered the most powerful country in the world. However, such an argument can be countered. It could be argued that the reason that RTAs have proliferated in recent years is because the US has not assumed the leadership role and has not provided the public good of trade openness. As previously mentioned, Kindleberger¹⁹ discussed the importance of having a country assume a leadership role and promote trade

¹⁴ Baldwin, Richard E. *21st Century Regionalism Filling the Gap between 21st Century Trade and 20th Century Trade Rules*. 2010.

¹⁵ Bhagwati, Jagdish. "Regionalism versus Multilateralism." *World Economy* 15, no. 5, 1992: 535-56

¹⁶ Mitrany, David. *The Prospect of Integration: Federation or Functional?* in *International Regionalism: Readings*, ed. Joseph S. Nye Jr. (Boston: Little, Brown and Company, 1968), p. 52

¹⁷ Haas, Ernst B., ed. (2004) [1958]. *The uniting of Europe: political, social, and economic forces, 1950–1957 (3rd ed.)*. Notre Dame, Indiana: University of Notre Dame Press.

¹⁸ Moravcsik, Andrew. "Preferences and Power in the European Community: A Liberal Intergovernmental Approach". *Journal of Common Market Studies*, December 1993.

¹⁹ Kindleberger, Charles. *The World in Depression 1929-1939*. London: Allen Lane, 1973.

openness. The failure of the US, which is considered the world hegemon by some, to promote trade openness is one argument for why we have witnessed a proliferation in RTAs.

It is important to note that not all scholars believe that the US is the world's hegemon. Offensive realists argue that a country can only aspire to dominate its region and that geography and the seas prevent a country from dominating the entire world²⁰. However, the US has lost a tremendous amount of "soft power,"²¹ but in terms of "hard power"²² and economics, the US is the most powerful country in the world; the current US GDP is approximately \$14 trillion dollars.

Ann Krueger examines the role of NAFTA, in particular, and believes that RTAs are a step in the right direction and help facilitate trade.²³ In addition, Mansfield and Milner support RTAs and view them as trading creating²⁴. It could be argued that RTAs are a form of trade, which is ultimately better than high tariffs and limited trade occurring among the international community.

POLITICS

This section will examine several other political aspects that could lead to the promotion of RTAs. As previously mentioned, a state might form an RTA due to natural inclinations of affinities for another state based on culture, history, language, etc. For example, Canada and the US are natural trading partners due to sharing a large border and because both countries are democracies. In addition, both countries have historical, cultural, and linguistic connections. However, other political reasons exist for RTAs. Rogowski discussed the political aspects that can occur in society between urban and rural sectors, for example²⁵. Also, certain groups can lobby the government and advocate for certain policies, such as protectionism or RTAs, for example. The farmer lobby in the US is very powerful, for instance, and tends to lobby for protectionism.

SECURITY

Various other security reasons exist and could help explain why a country would join an RTA with other countries. A group of countries might want to join in order to "balance against" other countries, according to realist logic²⁶. States might want to strengthen ties and linkages with potential partners in order to balance against other threats and potential issues²⁷. The Cold War, which lasted from 1945 until 1989, could be a perfect example when states formed trading blocks in order to increase linkages and balance. It is possible, for instance, that during the first wave of regionalism, which occurred in the 1960s, the US sought to increase ties with potential adversaries and participated in RTAs with allies, as opposed to adversaries, for security reasons.

²⁰ Mearsheimer, John J. *The Tragedy of Great Power Politics*. Updated ed. New York, NY: W.W. Norton, 2014.

²¹ Nye, Joseph S. *Soft Power: The Means to Success in World Politics*. New York: Public Affairs, 2009.

<<http://public.eblib.com/choice/publicfullrecord.aspx?p=903654>>.

²² Campbell, Kurt, and Michael O'Hanlon. *Hard Power: The New Politics of National Security*. New York: Basic Books, 2007. <<http://public.eblib.com/choice/publicfullrecord.aspx?p=952693>>.

²³ Krueger, Anne O. *Trade Creation and Trade Diversion under NAFTA* (December 1999). NBER Working Paper No. w7429. Available at SSRN: <https://ssrn.com/abstract=203157>

²⁴ Mansfield, Edward D., and Helen V. Milner. "The New Wave of Regionalism." *International Organization* 53, no. 3 (1999): 589-627.

²⁵ Rogowski, Ronald. "Political Cleavages and Changing Exposure to Trade." *The American Political Science Review* 81, no. 4 (1987): 1121-137.

²⁶ Layne, Christopher. *The Peace of Illusions: American Grand Strategy from 1940 to the Present*. Cornell Studies in Security Affairs. Ithaca: Cornell University Press, 2006.

²⁷ Layne, Christopher. "Offshore Balancing Revisited." *The Washington Quarterly* 25, no. 2 (2002): 233-48.

IR THEORY EXPLANATIONS

One can invoke the use of International Relations theory in order to examine RTAs. Neo-Liberal Institutionalism would view RTAs as a positive aspect because they promote cooperation. Keohane argued that institutions help promote cooperation, decrease transaction costs, and increase efficiency²⁸. As previously mentioned, Neo-Liberal Institutionalists argue that institutions can help mitigate anarchy. Constructivists challenge this argument. Wendt fundamentally challenges the realist notion that anarchy is the main structural element and is a given. Wendt argues that anarchy is a social construction.²⁹ Constructivism could be used to explain why countries join an RTA. A country might have a trade agreement in order to “socialize other countries” and promote certain norms, values, etc. Also, countries might join an RTA because they have common norms, values, etc. In addition, it depends on how a country views another state (enemy or friend).³⁰

Despite their peculiarities and incremental nature, free-trade agreements can serve the cause of freedom and development by breaking down barriers to trade between nations. RTAs get free trade moving along in five fundamental ways and make up for the flaws of the WTO. Moreover, RTAs act as a launching pad, or a stepping-stone, to further multilateral free trade rather than hinder it.

RTAs are possible, because they are legally allowed by the rules of the WTO (the General Agreement on Tariffs and Trade amended by the Uruguay round) as an exception to the principle of nondiscrimination. Nondiscrimination demands that all WTO members grant any advantage, favor, privilege or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other contracting parties. This means that if one country reduces a tariff to one nation, it must be done for all. The exception to this rule is found in Article XXIV of the WTO charter. It appreciates the desirability of increasing freedom of trade by the development, through voluntary agreements, of a closer integration between the economies of the countries [party] to such agreements. Thus, a member nation has the right to form RTA if they so desire for the purpose of closer integration. This forwards liberalization. There are of course limitations. Most important of these limitations are: RTA member countries cannot hike additional barriers to the other WTO member countries and, RTAs must eliminate duties and other restrictive regulations of commerce on substantially all trade between the constituent countries and do so within a reasonable length of time. The WTO places constraints on RTAs, so they do not engage in illiberal practices against others. Interestingly, Article XXIV, and therefore RTAs, can be waived entirely by a two-thirds vote of WTO members. States choose not to do so because they have much to gain from these arrangements. RTAs get free trade moving along in five ways. This makes up for the flaws of the WTO and thus, simultaneously encourages multilateralism and RTA proliferation.

In order to describe the advantages of RTAs and its proliferation, the institutionalist perspective highlights the necessary functions of the RTA in order to judge its beneficial use. Firstly, since the WTO contains many members in contrast to a RTA, the WTO's system of governance can prove to be quite inefficient, expensive and drawn out. It takes up to nine months to a year to settle a dispute. WTO negotiation rounds last years and sometimes, with no result. The need to gain consensus with all the members is a long arduous task and this is the root of the problem. The RTA system of governance provides a remedy to this because of its small membership. It would not take very long to settle a dispute and negotiate regulations. Not only that, RTAs are also flexible to the changing environment, their choice of partners and their policy scope³¹.

²⁸ Keohane, Robert O. *After Hegemony*. Princeton University Press, 2005.

<<http://www.myilibrary.com?id=275144>>.

²⁹ Wendt, Alexander. 2008. "Anarchy Is What States Make of It: The Social Construction of Power Politics". *Theories of International Relations*. 301-335.

³⁰ Jervis, Robert. *Perception and Misperception in International Politics*. 2017.

³¹ Fiorentino, Roberto V., Christelle Toqueboeuf, and Luis Verdeja. *The Changing Landscape of Regional Trade Agreements: 2006 Update*. Geneva, Switzerland: World Trade Organization, 2007.

Secondly, RTAs make it easy for countries that have been excluded from other RTAs to compete more fiercely and this would attribute to its proliferation. For example, if the United States was locked out of an RTA, American exporters would suffer unfairly. To get around that, the United States must create its own RTA, or join an existing one in order to compete on an equal footing. Since RTAs are an existing part of the world economic system, one would be foolish not to “go with the flow”. Thus, the benefits of joining an RTA system are obvious. It is an instrument used to remedy regional ties in order to create and maintain markets regardless of geographical location.

Thirdly, an RTA functions as an indication to the wider world that a country, most likely a developing nation, is preparing itself to join the global market. These indications assist the developing nation by attracting foreign investment as well as grants access to markets and, as a result, spur economic growth. RTAs give developing countries the confidence they need to enter the global market. More developing countries are joining RTAs. North-South RTAs make up for 27% of total RTAs and South-South 25% percent. Through RTAs, the nature of North-South trade relations appears to be evolving to a framework of reciprocity and ambitious trade policy scope. RTAs, in this case, serve as water wings for the infant country that is ready to swim in the waters of the free market. This would further explain its spread.

This leads to the fourth reason RTAs are so widely proliferated: they serve as the launching pad for further trade negotiations. As stated, because of its large membership, the WTO takes a very long time to initiate, negotiate and establish trade rules and regulations. The RTA, with its small amount of likeminded nations, would allow negotiations to be less painful and productive and therefore, more efficient in ensuring trade liberalization. These negotiations can serve as a springboard for additional multilateral discussions. Thus, RTAs prove more practical than WTO multilateralism. RTAs are seen as spaces for future multilateral trade developments. Connected to the fourth is the fifth factor: RTAs help nations cement ties to one another in order to continue their economic relationship. This is very attractive to nations and would again help explain its wide popularity.

RTAs spread ideas of free trade just like the WTO. Since both facilitate the idea of free trade, it can be concluded that RTAs assist multilateral trade. However, some scholars do not think this is exactly the case. Bhagwati, for example, believes that RTAs will lead the world down the path of solidified trading blocs and illiberal trade practices³². He argues that RTAs are not helpful to multilateralism. Rather, RTAs are a danger to trade liberalization. First, he argues that RTAs could divert trade from the cost-efficient non-member countries to the relatively inefficient member countries. He further points out that this would damage world welfare. This argument does have some weight, but as mentioned earlier, if a country is not a member of an RTA, that country can simply join or create one and that would allow for a more efficient allocation of resources and production methods.

Second, Bhagwati cites the “Spaghetti bowl” systemic concern. He states that when a country is a member of two or more RTAs, rules and regulations may crisscross and contradict one another. According to Bhagwati, with PTAs proliferating, the trading system can then be expected to become chaotic and interferes with the rules of origin. These distortions and ensuing confusion would ultimately raise prices and discourage trade. On the surface, all this red-tape and disorganization makes one large organization like the WTO a dream. However, one could argue that there is a trade-off between the WTO’s long drawn out court-like process and the Spaghetti bowl. Would one rather take the case to the WTO, spend lots of time and resources (not to mention the bad publicity), or go to the RTA of choice and resolve it through a relatively quicker, flexible and inexpensive negotiation? It would be more efficient to resolve disputes through an RTA. This encourages trade liberalization and explains RTA popularity. However, Bhagwati fails to see the benefits of RTAs in this case.

Third, Bhagwati maintains when poor countries enter into PTAs with...the United State and often the European Union, the lobbies in the hegemon countries insist on inserting into agreements a number of ‘trade-unrelated’ demands on the poor countries. As said, North-South RTAs make up for 27% of the world’s total RTAs. They are formed mutually through contracts. If Southern nations did not want to agree to these ‘trade-unrelated’ demands, they would not enter into these agreements. It would be in the

³² Bhagwati, Jagdish. "Why PTAs Are a Pox on the World Trading System." In *Termites in the Trading System*, Termites in the Trading System, Chapter 3. Oxford University Press, 2008.

interest of Southern nations to enter into RTAs with Northern nations because of their access to markets. Bhagwati's argument does not hold much water here.

A large part of Bhagwati's entails the fear of the world going back to the 1930's. However, the world's current level of integration and economic interdependence has changed quite a bit since then. Again, the exception to the WTO's nondiscrimination clause contains limitations, most importantly: RTA member countries cannot hike additional barriers to the other WTO member countries. Thus, the WTO places constraints on RTAs, so they do not engage in illiberal practices, especially the type Bhagwati fears. From this, the argument can be made that RTAs speed up the process of trade liberalization and multilateralism through decentralized blocs. This would explain why they have proliferated to the extent they did. As discussed, RTAs correct the deficiencies of the slow-moving WTO. They facilitate and encourage developing countries to enter trade relations with other nations to boost economic growth and development. RTAs are defended by the WTO and with the two-thirds waiving mechanism, this exception to reciprocity can be deleted if needed. Therefore, RTAs are not a threat to multilateralism, rather they encourage it.

Trade regimes can be multilateral, bilateral or regional in their nature. Different theoretical approaches can be applied to explain trade regimes creation, existence and success.

The multilateral trade regimes have been introduced with GATT (General Agreement on Trade and Tariff) and later replaced by a formal organization – the World Trade Organization (WTO). Regime theory of IPE attributes stability of international economic system to be associated with the regime itself, its norms and principles. Moreover, regime theory provides a set of tangible recommendations that can assist in making regimes more operational. Some of them have availability of information on the regime itself, clarity of its rules, and flexibility of the regime: possibility to adjust the rules according to the needs, how malleable regimes are, escape clauses, etc. From the regime theory point of view, multilateral trade regime's rules are codified by GATT and made operational by the WTO. Multilateral trade regimes are governed by two major principles shared by its members such as trade liberalization and non-discrimination. This makes regime attractive to its members. The principles are reflected in two major provisions codified in GATT as Most Favored Nation and National Treatment.

However, despite its advantages, the multilateral trade regime also has its disadvantages. From the point of view of regime theory, the non-binding and ineffective dispute resolution procedure does not put the WTO as a viable option for trade related disputes. This is the shortcoming of the regime making the states try to resolve their trade disputes under a different forum. HST attributes stability of the system to the overwhelming power of a hegemon that can either be benign or coercive but in either case provides the common good enjoyed by others. In case of the WTO, despite the obvious US hegemony as economic power, the presence of other powerful players such as Japan and the EU makes reaching decisions on particular issues quite difficult. There are still some issues pending and unresolved since the Doha round, which arguably demonstrate weaknesses of the regime overall.

Therefore, it can be argued that both Regime Theory and HST can find multilateral trade regime to be a suboptimal choice for the states in their trade policies. This can explain recent proliferation of a new wave of trade agreements. The first wave of trade agreements was mostly attributed to political integration and fostering of peace (the case of the European Union). The second wave of regionalism was mostly of economic nature. Moreover, the provisions of the GATT itself, as stipulated in article XXIV make Regional Trade Agreements (RTAs) possible.

Arguably, according to Art XXIV, RTAs are not to hamper but rather further advance the proliferation of international trade. Since they are possible only in the case of complete elimination of trade barriers, they should further provide liberation of trade flows. From the theoretical perspectives as well, both RTA and CUs (Customs Unions) make sense, since they enable members to address the issues that multilateral regimes are not capable of addressing (in case of RTAs, issues that are sensitive to the region). Moreover, the establishment of new regimes under RTAs and CUs allow member states to further advance their agenda by establishing the norms, rules and principles that are better tailored to their needs. Therefore, RTAs can be argued are optimal choice for many states in advancement of their trade agenda.

Both multilateral and Regional Trade Agreements provide an important tool for states to advance their policy.

Many scholars have expressed several reasons why RTAs have seen a surge over the last several decades, but two authors in particular make a clear point as to why they have become so prevalent. The rapid spread of RTAs can be connected to change in American economic policy. For quite some time, the US had been the “champion”³³ of multilateralism and inspired other countries to become more open with their trading policy. It was not until the conclusion of the Uruguay Round and the implementation of Article XXIV of the GATT (General Agreement on Tariffs and Trade), that persuaded the US to engage in more regional trade. Since then, the US has promoted RTA’s and other less developed countries have followed suit and adopted RTA’s as an alternative to multilateralism. There are 6 reasons why countries have engaged in RTA’s and have contributed to the increase in RTA’s. The 6 reasons are: security concerns, hegemony attract LDC’s, credibility among states, avoid divergence of trade, tit-for-tat among countries to join RTA’s and lastly, RTA’s allow powerful countries to advance un-related trade policies on weaker countries, in hopes of reform. It is also important to mention that many nations have become increasingly tired of dealing with the WTO and the difficulties that have been shown to come to agreements.

Some scholars have advocated for the spread of RTA’s and believe that they can positively contribute to the multilateral system. They understand that the current multilateral system, based on the structure of the WTO, is slow in advancing open trade policy. States are more inclined to strike agreements with each other, especially if they have similar characteristics and are of economy of scale³⁴. If RTA’s are struck among several less developed countries, it can spark economic reform and persuade governments in these countries to become more open. RTAs will help the multilateral system by reforming those nations that otherwise would not through the current multilateral paradigm.

On the other side of this debate, RTAs can be viewed as damaging to the multilateral system. Bhagwati believes that the fast spread of RTA’s has caused contradictions to occur, while allowing more powerful nations to impose “un-related” trade policies onto its weakest members³⁵. He uses the term “Spaghetti Bowl”, in order to imply the crisscrossing of overlapping policies and the confusion imposed on nations when trading with one another. In this sense, it is clear to see why RTA’s are stumbling blocks to multilateral trade. If countries are continually imposing different tariffs and policies on member and non-member states, this can eventually increase tensions among states and create a hostile environment. States, especially powerful states, can sidestep the bureaucracy of the WTO, in favor of striking agreements with other countries in order to expand their influence. Some scholars have assessed the second wave of regionalism has distinctive features that make it benign³⁶. First, there is a GATT/WTO framework to work under and have as a guide. The next distinctive feature is that liberal democratic reforms are being locked-in legally when signing an RTA. Another distinctive feature is that gains from trade are not being used to bolster political military power. This wave has the US as the hegemon leading the way at signing RTAs under high levels of interdependence. It is easier to get more done with less actors and it is possible to include more things like democracy and human rights in these agreements.

NAFTA and the EU are proof that RTAs can be beneficial and act as nice compliments to the WTO³⁷. Regional agreements are monitored by WTO member states and guided by those rules. However, RTAs act with much autonomy as it relates to the WTO. Member states fail to check their activities, and

³³ Mansfield, Edward D., and Helen V. Milner. "The New Wave of Regionalism." *International Organization* 53, no. 3 (1999): 589-627.

³⁴ Griswold, Daniel. "Bilateral Deals Are No Threat to Global Trade: DANIEL GRISWOLD." *The Financial Times*, 2003.

³⁵ Bhagwati, Jagdish N. *Termites in the Trading System : How Preferential Agreements Undermine Free Trade*. Oxford ; New York: Oxford University Press, 2008.

³⁶ Mansfield, Edward D., and Helen V. Milner. "The New Wave of Regionalism." *International Organization* 53, no. 3 (1999): 589-627.

³⁷ Abbott, Frederick M. "The North American Integration Regime and Its Implications for the World Trading System." In *The EU, the WTO, and the NAFTA*, The EU, the WTO, and the NAFTA, Chapter 6. Oxford University Press, 2001.

this can hurt trade³⁸. The US approach can be defined as competitive liberalization, because the US pursues free trade in all possible ways - "walking on two legs."³⁹

Bhagwati refers to RTAs as PTAs, because they are inherently preferential and discriminatory⁴⁰. He argues their vast proliferation came about during the Uruguay Round, because the US feared EU voting in unison at GATT, was tired of waiting for stalled multilateral talks and had poor leadership. He further argues that PTAs are proliferating and have become systemic. The "spaghetti bowl" model is a complex set of PTAs crisscrossing the globe from so many states signing so many different PTAs. He argues it is too complex for logistics and distorts international trade. It is impossible to reduce it all into a single integration model. Tariffs have to be reduced to negligible levels and make preferences worthless⁴¹.

There are many different positions when it comes to benefits and consequences of regionalism. Overall, RTAs act as compliments to the international trading system based on realist terms. States trade more within alliances than across alliances, because it is easier to monitor allies than non-allies⁴². States are always concerned with externalities and watching to see, if others are gaining relatively more than them. Fulfilling this is much easier in a small RTA than it is in the large WTO.

On top of this, states know what they are doing when they sign an agreement. States fail to monitor, if RTAs are WTO consistent⁴³. As an example, Obama created a team to monitor China and has won small disputes at the WTO, which eventually adds up. If a state thought it would experience consistent trade divergence, then it will not sign an agreement. The state does what is best for the state and if it does not feel it will receive benefits, it will not sign an agreement in self-help analysis.

If a transatlantic trade agreement between the US and the EU was to become reality, this could mean that a major hegemon (the US) is able to remain a hegemon by joining with another powerful entity (the European Union) in order to become the largest economy in the world overpowering China, which is threatening the US as a hegemon, according to Realists. In addition, other BRICS states such as Brazil, Russia, India and South Africa could potentially pose a future threat as well, which would then require a further extension of the US-EU trade agreement to include other entities such as Canada, for example.

The theory of interdependence also applies to an EU-US trade agreement as an example of how democracy can create other democracies due to the spillover effect.⁴⁴ Contrary to Realists, Neo-Liberal Institutionalists believe that cooperation and peace is possible due to institutions. Realists tend to have a more pessimistic outlook arguing that if one nation wins, another one loses. Neoliberal Institutionalists such as Keohane argue that institutions can be a win-win situation for everyone. This certainly applies to an EU-US trade agreement. Democratic Peace Theory⁴⁵ applies as well in this case, since one democratic nation

³⁸ Fabbriotti, Alberta, Joost Pauwelyn, and Gabrielle Marceau. "MULTILATERALIZING REGIONALISM AND THE FUTURE ARCHITECTURE OF INTERNATIONAL TRADE LAW AS A SYSTEM OF LAW." *American Society of International Law. Proceedings of the Annual Meeting*, 2009, 119-28.

³⁹ Zoellick, Robert. "US TRADE STRATEGY AND EUROPEAN INTERESTS." *CESifo Forum* 4, no. 3 (2003): 18-23.

⁴⁰ Bhagwati, Jagdish Natwarlal. 2008. *Termites in the trading system: how preferential agreements undermine free trade*. Oxford: Oxford University Press.

⁴¹ Fabbriotti, Alberta, Joost Pauwelyn, and Gabrielle Marceau. "MULTILATERALIZING REGIONALISM AND THE FUTURE ARCHITECTURE OF INTERNATIONAL TRADE LAW AS A SYSTEM OF LAW." *American Society of International Law. Proceedings of the Annual Meeting*, 2009, 119-28.

⁴² Gowa, Joanne. 1995. *Allies, adversaries, and international trade*. Princeton, N.J.: Princeton University Press.

⁴³ Fabbriotti, Alberta, Joost Pauwelyn, and Gabrielle Marceau. "MULTILATERALIZING REGIONALISM AND THE FUTURE ARCHITECTURE OF INTERNATIONAL TRADE LAW AS A SYSTEM OF LAW." *American Society of International Law. Proceedings of the Annual Meeting*, 2009, 119-28.

⁴⁴ Keohane, Nye, and Nye, Joseph S. *Power and Interdependence : World Politics in Transition*. Boston: Little, Brown, 1977.

⁴⁵ Doyle, M. "THE DEMOCRATIC PEACE." *International Security* 19, no. 4 (1995): 180-84.

applies a positive spillover effect to others⁴⁶. An EU-US trade agreement would also be based on soft power⁴⁷ principles as opposed to (military) hard power.

In trade politics, a society-centered approach is one in which a government's trade policy objective is designed by politicians in response to interest groups' demands. The society-centered approach emphasizes the relationship between organized societal interests and political institutions. These distributional pressures generate political competition as the interested parties (winners and losers) from trade turn to the political field to advance and defend their economic interests. With respect to trade policy preferences, followers of a society-centered approach argue that trade policy reflects the demands of the people, and this approach devotes considerable attention to the sources, the content, and organization of such demands.

In many cases, groups cannot organize because they confront a collective action problem⁴⁸. Collective action problems arise from a phenomenon called "free riding". The free riding concept describes the situations in which individuals depend on others to bear the costs of a program from which they derive benefits⁴⁹.

Even in the case where consumers share a common goal, the collective action problem prevents them from putting some pressure on politicians to achieve this goal. The incentive to free ride makes collective action in search of a common goal very difficult. The magnitude of the collective action problem depends in part upon the size of the group. In large groups, the incentive to free ride faced by each individual is very strong and large groups face very severe collective action problems. In small groups, each individual contribution is large relative to the total contribution and therefore each contribution has a greater impact on the group's ability to achieve its common goal. As a result, the incentive to free ride is weaker in small groups. The logic of collective action helps us understand why the interests of producers (organized in small groups) dominate trade politics, while the interests of consumers (organized in large groups) are often neglected. The large and heterogeneous group that bears the cost of the tariff finds it much more difficult to organize for collective action. Given these differing abilities to organize, trade politics is dominated by import-competing industries demanding protection.

In a society-centered approach, trade politics are driven by competition between organized interest groups. This competition sometimes revolves around class conflict, which confronts workers against business owners, and sometimes revolves around industry conflict, which confronts import-competing industries against export-oriented industries. The American electoral system is based on single-member districts. The nation is divided into mutually exclusive electoral districts with one person elected to represent each district. To win elections in this electoral system, politicians must satisfy the demands of the residents of their districts. Such an electoral system creates an incentive for groups to organize around narrow industry lines and creates incentives for elected officials to represent and defend the narrow interests of the industries in their districts. Industries needing protection will be most likely to organize. Consequently, American electoral institutions create strong incentives for elected officials to bring the narrow, industry-specific interests of import-competing industries into Congress. In Congress, legislative dynamics practically guarantee that any effort to protect a single industry will be transformed into legislation that protects many industries.

The state-centered approach suggests that one looks at the political influence of the industries concerned, and its supporters argue that national policymakers should intervene in the economy in pursuit of objectives that are determined to be independent from the domestic interest groups narrow self-interest. This approach suggests that such intervention may raise aggregate social welfare. Proponents of the state-centered approach, with its specific focus on government intervention, feel it is designed to promote the development of specific national industries. The society-centered approach is based on the belief that

⁴⁶ Kant, Immanuel, and Ted Humphrey. *Perpetual Peace and Other Essays on Politics, History, and Morals: A Philosophical Essay*. Indianapolis: Hackett Pub. Co, 1983.
<<http://public.eblib.com/choice/publicfullrecord.aspx?p=775229>>.

⁴⁷ Nye, Joseph S. *Soft Power: The Means to Success in World Politics*. New York: Public Affairs, 2009.
<<http://public.eblib.com/choice/publicfullrecord.aspx?p=903654>>.

⁴⁸ Olson, Mancur. *The Logic of Collective Action: Public Goods and the Theory of Groups*. Harvard Economic Studies; v. 124. Cambridge, Mass.: Harvard University Press, 1971.

⁴⁹ Sandler, Todd. *Collective Action: Theory and Applications*. Ann Arbor: University of Michigan Press, 1992.

protectionism reduces social welfare by depriving society of the gains from trade and by employing society's resources in comparatively disadvantaged industries, but proponents of the state-centered approach argue that, under certain circumstances, trade protection can raise social welfare. From the perspective of the society-centered approach, national policy reflects the balance of power among competing interest groups, but under specific circumstances governments are relatively unconstrained by interest-group demands. Therefore, a government's trade and economic policies represent the goals of national policymakers rather than the demands of interest groups.

Targeted government intervention in particular sectors, can increase aggregate social welfare. In the standard model, society does best by removing all forms of trade protection and by specializing in its comparatively advantaged industry. Factors of production will move into relatively advantaged industries because it is profitable to do so.

The infant-industry case for protection argues that there are cases in which newly-created firms will not be efficient initially but could be efficient in the long run if they are given time to mature. A short period of tariff protection is advocated to enable these infant-industries to become efficient and begin to export. Once this point has been reached, the tariff should be removed. There are two reasons why an industry may not be efficient in the short run, but could be efficient in the long run, one is economies of scale and the other economies of experience⁵⁰.

The formation of regional trade agreements has been, by far the most popular form of reciprocal trade liberalization in the past decades. The discriminatory character of these agreements has raised three main concerns: first, that trade diversion would increase, because special interest groups would induce governments to form the most distortionary agreements, second, that broader external trade liberalization would reverse and third, that multilateralism could be undermined.

In case of the WTO, the presence of multiple powerful players makes reaching decisions on particular issues quite difficult. Therefore, it can be argued that both Regime Theory and HST can find multilateral trade regimes to be suboptimal choices for states in their trade policies. This can explain recent proliferation of a new wave of trade agreements. While the first wave of trade agreements was mostly attributed to political integration and fostering of peace (the case of the European Union), the second wave of regionalism is mostly of economic nature. Moreover, the provisions of the GATT itself, as stipulated in the article XXIV make Regional Trade Agreements (RTAs) possible.

To follow a constructivist approach, RTAs as well provide more stable regimes as they tend to be present in states with cultural proximity (as in case of the European Union) that as well can facilitate success⁵¹. In the case of the European Union, cultural proximity is reflected in need for new member states to adopt all legal body of the Union and play according to the Union's rules.

Both, multilateral and Regional Trade Agreements provide an important tool for states to advance their policy. As both Regime and HST theory demonstrate, the attractiveness and flexibility of RTAs can explain their proliferation in recent years.

Mercantilism was dominating states from the 16th until the 18th century with protectionist and nationalistic trade policies based on the infant industry argument⁵² which was focused on domestic politics and domestic trade in order to protect the local state economies. International trade was only desirable in this period for imports and as long as there was a positive trade balance. Exporting gold and silver was avoided in order to keep the national domestic economies stable⁵³.

During the enlightenment period, however, Adam Smith came up with the "absolute advantage" theory⁵⁴. Smith emphasized the role of individuals to pursue wealth and trade freely. In his mind, trade should be allowed to be conducted internationally without any country border restrictions or barriers. The

⁵⁰ Kenen, Peter B. *Managing the World Economy : Fifty Years after Bretton Woods*. Washington, DC: Institute for International Economics, 1994.

⁵¹ Katzenstein, Peter J. "International Interdependence: Some Long-term Trends and Recent Changes." *International Organization* 29, no. 4 (1975): 1021-034.

⁵² Hamilton, and Hamilton, Alexander. *Report of the Secretary of the Treasury of the United States, on the Subject of Manufactures: Presented to the House of Representatives, December 5, 1791*. 1793.

⁵³ Gilpin, Robert., and Gilpin, Jean M. *The Political Economy of International Relations*. Princeton, N.J.: Princeton University Press, 1987.

⁵⁴ Smith, Adam. *An Inquiry into the Nature and Causes of the Wealth of Nations*. London: Electric Book, 2001.

theory of “comparative advantage”⁵⁵ was added to this notion referring to open trade as well, specifically to whoever produces most efficiently shall gain an advantage. For example, if a company can produce and sell cars more efficiently than other companies, they could have a competitive advantage. During this enlightenment period, Great Britain took the lead and created the period known as Pax Britannica. Due to the industrial revolution, a period of economic growth occurred, and this also triggered 100 years of peace between 1814 and 1914 until World War I. This economic growth and peace period was based on liberalism occurring after the mercantilist period ended. These liberalism notions also led to capitalism in combination with the industrial revolution as well as international trade.

Marx and Engels criticize capitalism, as it (in some instances) results in overproduction and therefore unemployment for some laborers and could consequently lead to the proletariat (workers/laborers) overthrowing the bourgeoisie (elite). Lenin took Marxism a step further and applied it to the Imperialism period in which the European states exploited their colonies in order to enrich their domestic economies⁵⁶. Some of these Marxist notions are still relevant in regard to domestic trade policies today. Unemployment and low wage jobs are affecting domestic support for potential trade agreements in the United States as well as in the European Union. Thousands of demonstrators went into the streets on a regular basis to oppose mega-regional agreements in Europe and in the United States such as TPP and TTIP, because they fear job losses and economic losses. Demonstrators believe that they may lose their current jobs, as some jobs may be transferred overseas once these trade agreements go into effect. These phenomena are referred to as domestic society-centered pressures against these regional trade agreements. In the past, citizens have faced collective action problems. While there were some demonstrations, it was not enough to prevent NAFTA, for instance. However, in the case of TTIP and TPP, the society-centered pressures have actually succeeded so far in preventing these trade agreements from being approved. The migration crisis in Europe has led to disapproval of the current administration of the European Union. Regional elections have turned out right-wing in Europe or far left either way back-lashing against the traditional parties in power. Demonstrators in Europe including interest groups (farmers, lobbyists, environmentalists) managed to take collective action as far as to demand from the European Commission to publish all documents related to TTIP on the internet. After so many pressures and demonstrations, the Commission has actually started to comply with the pressure of the people and politicians. In the United States, demonstrators against TPP also succeeded, because the very recent US election outcome on November 8, 2016 produced a new right-wing president (Donald Trump) who was generally opposed towards any type of Trade-Agreement during his campaign. Whether he can actually succeed with his Neo-mercantilist and protectionist nationalistic proposals remains to be seen. Some economic analysts do not believe that his policies will work, because a lot of great opportunities and economic boosts could be lost by not implementing TPP and TTIP.

Contrary to realist notions that state power shapes the international anarchic system, Keohane and Nye developed the complex interdependence theory in 1977. While acknowledging that the international system is anarchic, Keohane and Nye added that institutions play an important role to facilitate cooperation and trade among states. In 1982, Ruggie concurred that an “Embedded Liberalism” was necessary in order to keep capitalism and trade in check. He agreed with the Keynesian approach of stabilizing the liberal system with institutions and the state controlling the market up until a certain point, but not to the mercantilist extend. In 1983, Krasner added Regime Theory to this idea explaining how institutions such as the United Nations or the Bretton Woods institutions serve an important role in stabilizing the international system and facilitating trade. In “After Hegemony”, Keohane builds on Kindleburger’s hegemonic stability theory demonstrating that a hegemonic stabilizer was not necessarily needed due to international institutions.

According to Baldwin, the context and timing of TTIP and TPP could also be explained with the Domino Effect Theory. When the GATT (General Agreement on Tariffs and Trade) was implemented after World War II, the US was more focused on multi-lateral trade up until the Uruguay Round eventually led to the creation of the World Trade Organization (WTO) in 1995. At this time, the United States was still committed to multi-lateral trade and international multi-lateral trade was viewed as beneficial (Milner and Mansfield, 1999). However, when the Doha Round in 2001 stalled any further progress with the WTO rules, the United States decided to change the multi-lateral trade policy to a more

⁵⁵ Ricardo, David. *On the Principles of Political Economy and Taxation*. London: Electric Book, 2001.

⁵⁶ Lenin, Nikolai. *Imperialism, the Highest Stage of Capitalism*. 2017.

regional trade-policy. The WTO has too many member states who cannot all agree on and decide on trade policy. Therefore, regional trade agreements started rising in popularity resulting in NAFTA, for example, in 1994 (North American Free Trade Agreement between the United States, Canada and Mexico). This created a Domino Effect (Baldwin, 1993) leading other nations to engage in Regional Trade Agreements as well. NAFTA and regional trade agreements in general may have benefits and supporters, but they also have opponents. In “Termites in the Trading System”, Baghwatti criticizes regional trade agreements as preferential trade agreements, because they give preferences to certain states which was originally not allowed according to the WTO rules. States were not allowed to discriminate against other WTO member states according to the WTO Article 24 (Non-Discrimination Clause). However, regional trade agreements fall under an exception. However, Baghwatti (2003) still criticizes regional trade agreements due to their Spaghetti Bowl affect. When looking at a world map, it looks like a Spaghetti bowl, because there are so many intertwined and confusing trade arrangements within and across different regions.

The economic crisis and migratory pressures in the world in general and most specifically in Europe and the Western Hemisphere, in addition to the rise of populism and the rebirth of renationalization, have presented challenges serious to trade and regional integration projects. In my opinion, the comparable context and timing of TPP and TTIP are no coincidence. The economy is not growing as it used to. Republicans have blocked Obama in almost every policy he proposed except for in trade. They actually granted him Trade Promotion Authority which demonstrates how important these trade agreements are. If Democrats and Republicans and Congress and the Senate can actually agree on something with a clear majority, it is definitely a strong indication on its validity and importance. While there are some losers with trade agreements, there are overall more winners than losers. If TPP and TTIP are not implemented, there will be more negative consequences for the United States and for Europe than positive. This is one of the reasons why China and Russia were so happy with the election outcome, because China can now go ahead with their own trade agreement in Asia which was not going to happen had TPP been implemented. Consequently, China might even create a bigger economy than it already has and surpass the US and the EU once and for all. Hopefully, the Trump administration will be smart enough to catch on to this quickly, as it has already been all over the scholarly news (of course not the popular one as usual).

Today’s trade politics serve as a reminder of what could potentially repeat itself in history.

During the inter-war years (between World War I and World War II), Great Britain was unable to resume its leadership role due to the destruction of the war. The United States could have assumed a leadership role, but instead decided to pursue protectionist economic policies. This neo-mercantilist behavior in combination with weakened European economies from World War I eventually resulted in the Great Depression from 1929-1939. In the realist view, a hegemon was needed to stabilize the international system in order to keep other nations in checks and balances, in order to provide peace and protection⁵⁷. Similar to the US behavior back in the 1930s, the Trump Administration’s protectionist trade policies could potentially trigger another depression. Therefore, it is highly recommended that the US continues trade talks with the EU in order to form an official trade agreement and possibly create a repetition of the “Great Transformation”⁵⁸ in order to combat economic instability based on liberalist principles. In contrast to the Great Depression, liberalism is a double movement. First, creating a stable system for trade and cooperation and second stabilizing this system based on Keynesian notions by institutions. After World War II, the different nations were fed up with the economic instability caused by wars and therefore decided to found the Bretton Woods Institutions: the International Monetary Fund and the World Bank in order to finance development for the European Nations to rebuild after the war as well as for developing nations. In addition, the GATT (General Agreement on Trade and Tariffs) set the foundation for a more liberalist period again. In contrast to the Great Depression, liberalism can be viewed as a double movement. First, creating a stable system for trade and cooperation and second stabilizing this system based on Keynesian notions by institutions. In addition, a stable exchange rate system was created by pegging the dollar to gold and all other (European) nations pegged their currencies to the dollar. This system worked well for trade and

⁵⁷ Kindleberger, Charles. *The World in Depression 1929-1939*. London: Allen Lane, 1973.

⁵⁸ Polanyi, Karl. *The Great Transformation*. First Beacon Paperback ed. Beacon Paperback No. 45. Boston: Beacon Press, 1957.

created economic growth for several decades until the United States experienced a deflation in the 1970s. In order to devalue its currency, the US decided to leave the gold standard and all other nations consequently followed after that. In addition, the OPEC oil crisis occurred in 1973 setting an end to this stable and reliable Bretton Woods system. Several economic and financial downturns all over the world followed in Asia and Europe. Therefore, the 1980s were characterized of a more neo-liberal capitalist Reagan-Thatcher economic trend in order to boost the economies and encourage international trade again. These principles are still applicable today when it comes to EU-US trade policies.

Some scholars contend that both mega-regional trade agreements (TTIP and TPP) have been proposed in order to counter the emerging BRICS (Brazil, Russia, India, China, South Africa) which are threatening to overthrow the highly developed United States and the European Union, for example. Especially China should be a central focus of attention, according to Keohane (2009). Since the rise of China, the United States is no longer the hegemon, according to some Realists such as Gilpin (2001) and therefore, the United States sees it as a necessity to engage in trade-agreements in order to create a bigger economy with more opportunities. The United States economy alone can no longer compete with China. However, combining the European Union economy with the United States economy, would mean that through a joint trade agreement, both, the US and the EU, can overpower the Chinese economy. From a Liberalist point of view, these trade agreements are also attempts to prevent another economic crisis. The US economy is not growing as much as it used to be. Therefore, regional trade agreements are a way of boosting the economy and creating new opportunities on both sides of the Atlantic. From a Constructivist point of view, the United States and Europe share mutual (Western) values, cultures, norms, identities and ideas historically. Therefore, an EU-US regional trade agreement could also be viewed as a joint community of values from a Constructivist lens⁵⁹.

The context and timing of an EU-US trade agreement could also be explained with the Domino Effect Theory⁶⁰. When the GATT (General Agreement on Tariffs and Trade) was implemented after World War II, the US was more focused on multi-lateral trade up until the Uruguay Round eventually led to the creation of the World Trade Organization (WTO) in 1995. At this time, the United States was still committed to multi-lateral trade and international multi-lateral trade was viewed as beneficial⁶¹. However, when the Doha Round in 2001 stalled any further progress with the WTO rules, the United States decided to change the multi-lateral trade policy to a more regional trade-policy. The WTO has too many member states who cannot all agree on and decide on trade policy. Therefore, regional trade agreements started rising in popularity resulting in NAFTA, for example, in 1994 (North American Free Trade Agreement between the United States, Canada and Mexico). This created a “Domino Effect” leading other nations to engage in Regional Trade Agreements as well. NAFTA and regional trade agreements in general may have benefits and supporters, but they also have opponents.

In the case of TTIP, the United States and the European Union were unable to agree on the final terms during the last negotiation round in 2016. Due to the agricultural lobby in the United States, the US did not want to establish higher agricultural food and safety standards compliant with EU laws and due to consumer and agricultural lobbies in the EU, the EU was unable to lower its standards in order to find a compromise with the United States⁶². At the center of this debate was genetically-manipulated food, hormone treated meat and chlorine bleached chicken – all commonly accepted standards in the US but rejected by the EU. If the US were to increase these standards, the contents of TTIP could technically still be ratified. However, this seems quite unlikely under the current Trump administration which is neither very environmentally friendly nor very “green”/organic oriented. TTIP actually did not face too much opposition in the US. Most US citizens do not even know about TTIP, because the media did not focus on this agreement during the elections, but TPP was the sole focus of public and media attention. In Europe,

⁵⁹ Katzenstein, Peter J. "International Interdependence: Some Long-term Trends and Recent Changes." *International Organization* 29, no. 4 (1975): 1021-034.

⁶⁰ Baldwin, Richard. "A Domino Theory of Regionalism." *NBER Working Paper Series*, 1993, 4465.

⁶¹ Mansfield, Edward D., and Helen V. Milner. "The New Wave of Regionalism." *International Organization* 53, no. 3 (1999): 589-627.

⁶² Rogowski, Ronald. "Political Cleavages and Changing Exposure to Trade." *The American Political Science Review* 81, no. 4 (1987): 1121-137.

however, TTIP faced a lot of public and media opposition and would therefore probably not be able to pass unless it was to be re-negotiated under a different name and higher standards (from the US side compliant with EU norms). Since the Trump administration has signaled an intention to negotiate with single partners, it will be interesting to see how this will affect the outcome of a US-EU agreement.

Cultural influences on economic growth and trade with the example of locals versus cosmopolitans can have an impact⁶³. “Regular” locals are US citizens living in rural areas, for example in the Mid-West, and they have not much understanding of international cultures. They are mainly concerned with their local employment and local domestic environment. Cosmopolitans, on the other hand, usually live in big cities such as New York, London, etc.; they travel a lot and are familiar with different cultures and languages. The difference in this lifestyle and education also shows how their viewpoints on trade can be affected. Domestic locals tend to be against trade agreements whereas cosmopolitans tend to be pro-trade. Urban versus rural lobbies can make a big difference when it comes to influencing the farmers lobby, for example.

In both, TPP and TTIP, domestic pressures have been the main cause for the failure of these agreements. The consequence for the economies on both sides of the US territory may be that trade agreements with China could be formed leaving the US out. The EU, for instance, is already starting trade negotiations with China. The same could be true for Australia and Japan for instance. The US might find itself left out in the end, if the Trump Administration does not manage to boost the US economy and satisfy unemployed workers. However, the question remains whether this can be done by pursuing protectionist measures. Globalization cannot be halted, and jobs lost due to technological advances will not return. The only alternative remains to re-train those workers into other fields, which requires an investment in education. However, the Trump administration already made some budget cuts in the education sectors which is quite concerning given the unemployment dilemma connected to trade.

The more and more unequal distribution of wealth is not due to trade nor due to globalization, but due to domestic social welfare policies in order to protect citizens of the impact of globalization and trade agreements⁶⁴. The unequal distribution of wealth causes social and economic instability⁶⁵. However, the Trump Administration removed many of the protective measures the Obama Administration had put in place in order to prevent another financial crisis, in order to prevent banks overpowering the markets etc. As history has demonstrated, most mercantilist and protectionist trade policies did not last, because they create power for the nation and wealth for the government while decreasing international competitiveness. The Great Depression in the 1930s was a result of US protectionist policies. On the other hand, too much liberal trade without government control and stability measurements are not good either as the Reagan, Nixon period has shown removing too many industry protection measurements. Therefore, a balanced approach is important such as embedded liberalism supported by governing and regulating institutions for social (welfare) protection⁶⁶.

The economic crisis and migratory pressures in the world in general and most specifically in Europe and the Western Hemisphere, in addition to the rise of populism and the rebirth of renationalization, have presented challenges serious to trade and regional integration projects. The comparable context and timing of TPP and TTIP were no coincidence. The economy is not growing as it used to. Republicans in the US blocked Obama in almost every policy he proposed except for in trade. They actually granted him Trade Promotion Authority which demonstrates how important these trade agreements are. If Democrats, Republicans, Congress and the Senate can actually agree on something with a clear majority, it is definitely a strong indication on its validity and importance. While there are some losers with trade agreements, there are overall more winners than losers. If a joint EU-US trade agreement is not implemented, there will be more negative consequences for the United States and for Europe than positive. This is one of the reasons why China and Russia were so happy with the election outcome, because TPP and TTIP were both put on ice. Consequently, China might even create a bigger economy than it already has and surpass the US and

⁶³ Friedman, Thomas L. *The Lexus and the Olive Tree*. First Anchor Books ed. New York: Anchor Books, 2000.

⁶⁴ Stiglitz, Joseph E. *The Price of Inequality*. First ed. New York: W.W. Norton &, 2012.

⁶⁵ Piketty, Thomas, and Arthur Goldhammer. *Capital in the Twenty-First Century*. 2018.
<<https://doi.org/10.4159/9780674982918>>.

⁶⁶ Ruggie, John Gerard. 1982. "International Regimes, Transactions, and Change: Embedded Liberalism in the Postwar Economic Order". *International Organization*. 36, no. 2: 379-415.

the EU once and for all. Hopefully, the Trump administration will be smart enough to catch on to this quickly, as it has already been all over the scholarly news (of course not the popular one as usual).

Some of the US unemployment and economic problems which were the heart and center of the very recent November 8, 2016 US election outcome could be solved by copying other successful models such as a dual education and employment system that Germany offers for example. Therefore, I recommend for the US administration to copy these successful already existing models and apply them to the US system to come up with actual solutions for these ongoing problems. The key is to combine the best of each, the US and the EU, to come up with tangible and working policy recommendations that could actually be implemented by administration and governments domestically. A joint EU-US trade agreement is the first step in the right direction and will be ultimately be beneficial for both sides.