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International Trade Developments

Mexican Trucks Gain Access to U.S. Highways

The Euro-Mediterranean Partnership

A WTO Agreement on Competition Policy: Prospects and Pitfalls

U.S. Trade Developments

International Economic Comparisons

U.S. Productivity and Cost: Preliminary Fourth-Quarter and Annual Averages for 2001

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INTERNATIONAL TRADE DEVELOPMENTS

Mexican Trucks Gain Access to U.S. Highways

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A 6-year-old dispute between the United States and Mexico has apparently ended. The United States agreed that, as soon as possible after January 1, 2002, it would grant access to U.S. highways for Mexican trucks, provided that U.S. safety standards are met. This decision was accompanied by measures for significant improvements in the U.S. inspection process.

On February 6, 2001, the United States lost its first major case under a North American Free Trade Agreement (NAFTA) arbitration panel, which ruled that the United States must open its borders to Mexican trucks. In the words of the panel: "the U.S. blanket refusal to review and consider for approval any Mexican-owned carrier applications for authority to provide cross-border trucking services was and remains a breach of the U.S. obligations."[2] The panel recognized the right of the U.S. Government to require Mexican trucks to comply with U.S. safety standards, but recommended that it review applications from Mexican truckers for access on a case-by-case basis.[3] President Bush signed into law a transportation spending bill on December 18, 2001, which allows Mexican trucks to operate in the United States, and spells out the requirements Mexican trucks need to meet before they are granted access.[4]

[1] The views expressed in this article are those of the author. They are not the views of the U.S. International Trade Commission (USITC) as a whole or of any individual Commissioner.

[2] North American Free Trade Agreement, *Arbitral Panel Established Pursuant to Chapter Twenty in the Matter of Cross-border Trucking Services —Final Report of the Panel*, Secretariat File No. UNITED STATES-MEX-98-2008-01, Feb. 6, 2001, par. 295, found at Internet address *http://www.nafta-sec-alena.org/english/index.htm*, retrieved on Apr. 2, 2002. The panel refers to obligations under Annex I (reservations for existing measures and liberalization commitments) Article 1202 (national treatment for cross-border services), and Article 1203 (most-favored-nation treatment for cross-border services).

[3] NAFTA Arbitral Panel, *Final Report of the Panel,* op. cit., par. 300.

Background

The dispute over access of Mexican trucks to U.S. highways began at the end of 1995, when the United States delayed permission for Mexican-domiciled cargo and passenger services to operate in California, Texas, Arizona, and New Mexico, as agreed earlier in the context of NAFTA. While under NAFTA, Mexican trucks would have access to the entire United States on the first day of 2000, the accord also provided for an interim phase of cross-border trucking that would open up these four states to Mexican trucks in December 1995.[5] NAFTA further specified that, in order to operate in the United States, Mexican trucks and truck drivers must meet U.S. safety standards. To adapt Mexico to meet this requirement, transportation officials of both countries had engaged in extensive preparations to harmonize motor vehicle safety processes between the two countries.[6]

[4] Public Law 107-87, *Department of Transportation and Related Agencies Appropriations Act 2002*, Dec. 18, 2001; 115 Stat. 833.

[5] NAFTA, Chapter 12, Annex 1212.

[6] Regulatory harmonization pertaining to U.S. and Canadian truck transport services began in the 1980s and the U.S.-Canadian border was opened to cross-border trucking in 1982, years before NAFTA became effective in 1994. A Land Transportation Standards Subcommittee (LTSS) was established to address standards for drivers and vehicles of safety compliance.

However, shortly before the December 1995 due date of the interim (transitional) phase, President Clinton postponed the opening of the border states to Mexican trucks, citing unmet safety conditions. This action followed intense lobbying by the International Brotherhood of Teamsters (Teamsters) against opening the border to Mexican trucks. The Teamsters and others claimed that Mexican trucks have been involved in countless accidents, that they heavily pollute the air, and that the flow of illicit drugs into the United States increases when Mexican trucks are allowed across the border. The most frequently cited causes of accidents were that Mexican trucks are old, unsafe, and operate without weight limits, and that drivers lack adequate training, work long shifts, and engage in inappropriate behavior on the road.[7]

A 1997 study of the General Accounting Office (GAO) entitled "Safety Concerns About Mexican Trucks Remain Even as Inspection Activity Increases," underscored the Teamster's position on safety. The "status quo," i.e. restriction of Mexican trucks to a narrow commercial zone, 20 miles wide or less north of the border, remained unchanged.[8] As before, goods had to be transferred from Mexican trucks to U.S. trucks for being hauled past the border zone into the United States.

Bilateral consultations on adapting Mexican trucks and drivers to U.S. safety requirements continued after 1995, but no agreement was reached. Mexican officials insisted that their country's safety inspection system was already consistent with that of the United States. In 1998, the Government of Mexico formally protested under NAFTA dispute-settlement procedures the U.S. postponement of the interim trucking provisions' implementation.

Interest in the issue intensified in 1999, as the January 1, 2000 deadline for Mexican trucking access to the entire United States came into view. U.S. authorities found that, restrictions notwithstanding, a number of Mexican trucks that were not in compliance with U.S. standards had already found ways to haul cargo beyond the commercial zone into U.S. territory.[9] Hence, in December 1999, President Clinton signed the "Motor Carrier Safety Improvement Act of 1999,"[10] part of which provided for "Foreign Motor Vehicle Penalties and Disqualifications."[11]

In addition, since inadequate U.S. border inspection was blamed in part for unsafe Mexican trucks circulating on U.S. roads, the Department of Transportation (DOT) embarked on a program of improving the inspection process.[12] Most important, the opening of the border to Mexican trucks did not take place on January 1, 2000, as mandated by NAFTA. Mexican trucks continued to be restricted to the border zone.[13]

The Dispute During 2001

In 2001, cross-border trucking continued to be a major unresolved issue in U.S.-Mexican trade relations. Since NAFTA became effective in January 1994, trade between the United States and Mexico has grown significantly, increasing the importance of cross-border trucking services. Over four fifths of bilateral trade is transported over highways. The NAFTA ruling in February that the United States is in violation of its treaty obligations, coupled with the advent of new administrations in both countries, gave added urgency to this issue.

Once again, the safety problem had to be addressed. Testifying before the House Subcommittee on Transportation, the Inspector General of the DOT said on March 2, 2001, that since 39 percent of Mexican trucks inspected at the border failed to meet U.S. safety standards, a greater border inspection presence was needed to accommodate a large flow of trucks.[14] Ready to comply with the verdict of the NAFTA arbitration panel, DOT proposed in May 2001 that, beginning January 1, 2002 it would allow Mexican trucking companies to apply for permission to operate in the United States. When in the United States, Mexican trucks would have to adhere to the same rules as do U.S. trucks. DOT also proposed rules for Mexican service providers on how to submit trucks

[7] Brendan M. Case, "Mexican Truck Debate Veers Between Fears and Facts," *The Dallas Morning News,* Aug. 20, 2001.

[8] See also USITC, *The Year in Trade 1995: Operation of the Trade Agreements Program*, USITC Publication 2971, August, 1996. P. 56.

[9] An 1999 report of the Federal Motor Vehicle Safety Administration (FMCSA), based on an analysis of roadside inspection in FY 1998, identified 254 Mexican domiciled motor carriers that operated improperly beyond the commercial zones and the border States. Report is cited by the Inspector General of the Department of Transportation (DOT), *Interim Report on Status of Implementing the North American Free Trade Agreement's Cross-Border Trucking Provisions*, report No. MH-2001-059, May 8, 2001, p. 16.

[10] Public Law 106-159, *Motor Carrier Safety Improvement Act of 1999*, Dec. 9, 1999; 113 Stat. 1748.

[11] Title II, Sec. 219.

[12] See also USITC, *The Year in Trade 1999: Operation of the Trade Agreements Program*, USITC Publication 3336, August 2000, p. 61.

[13] Magdolna Kornis, "Implementation of NAFTA Provision to Open U.S. Roads to Mexican Trucks on January 1, 2000, has been Delayed," *International Economic Review,* Jan.-Feb. 2000.

[14] Bureau of National Affairs (BNA), "Transportation: DOT Official Calls for More Inspectors to Examine Trucks at the U.S.-Mexican Border," *International Trade Daily*, Mar. 6, 2000.

for inspection, and on other aspects of safety compliance.[15]

However, the DOT proposal and the pertaining budget request on expanded inspection met with opposition in the congressional debate of the 2002 transportation spending bill. A House bill of June 26, 2001 (HR 2299) would prohibit any funding for processing Mexican truckers' applications for access, in effect postponing again the opening of the border on January 1, 2002.[16] The Senate version of August 1, 2001 (S 1178) proposed to subject Mexican trucks to an array of safety regulations, and required that the trucks should be certified in Mexico even before they apply to U.S. authorities for permission to operate in the United States.[17] The Bush Administration and other advocates of opening the border found these requirements restrictive and discriminatory against Mexico.[18]

Principal Arguments for and Against

The proponents for free access into the United States for Mexican trucks include President Bush, President Fox, U.S. trucking associations, and the Mexican Association of Private Transport. Voices opposed to implementing the NAFTA trucking provisions, which would keep Mexican trucks off U.S. roads, include the U.S. Teamsters Union and the Mexican National Cargo Chamber (CANACAR), the latter representing some four fifths of Mexican commercial trucks.

U.S. Arguments

U.S. advocates for free access argued that the U.S. Government should avoid reneging on NAFTA obligations. President Bush, the most notable U.S. advocate of opening the border, stated on July 25, 2001, that "Mexico is our close friend and ally and we must treat it with respect and uphold NAFTA and the spirit of NAFTA."[19] The President has vowed to veto any legislation that prevents the United States from meeting its NAFTA obligations.[20]

The American Trucking Associations (ATA) were also firmly opposed to further delay of implementation, emphasizing the efficiency aspect of cross-border trucking. In his testimony in July 2001 at a hearing in the U.S. Senate, the Chairman of ATA described the present system as cumbersome and costly, claiming that it "requires no less than three drivers and three tractors to perform a single international freight movement."[21] He was referring to the frequent current practice of using separate long-haul truckers on either side of the border, plus a so-called drayage truck in between. The drayage truck is a short-haul truck, whose only function is to ferry the load across the border through the maze of customs officials and brokers. ATA's Chairman argued that with the implementation of NAFTA this system could be replaced by a less costly and more efficient one.

U.S. trucking companies favored NAFTA in part because they were interested in opportunities provided by the Mexican market, which were expected to be jeopardized by U.S. restrictions of Mexican trucks in the United States. Yet, reportedly, U.S. fleet-owners' interest in providing actual trucking services in Mexico was limited, due to the perception that their employees would be handicapped by the poor condition of Mexican roads, fear of crime, and language differences.[22] For U.S. interests, more important than being able to provide trucking services might be the investment opportunities in Mexican trucking that would open up following the implementation of NAFTA.[23]

On the other side of the U.S. dispute, Jim Hoffa, the Teamsters' President, continued to argue against the implementation of NAFTA. He testified in the Senate that U.S. inspection facilities are "...still inadequate to evaluate and monitor the safety of

[15] Federal Motor Carrier Safety Administration, "Instructions for Completing Applications for Certificate of Registration for Foreign Motor Carriers and Foreign Motor Private Carriers," form op-2. Found at *http://www.dot.gov/factsfigs/licensing/op.2.htm* on Sept. 21, 2001.

[16] Amendment to the DOT appropriation bill, offered by Rep. Martin Sabo (D-Minn.)

[17] A bipartisan proposal of Sen. Richard C. Shelby (R-Ala.) and Sen. Patty Murray (D-Wash.), the so-called Murray-Shelby proposal, imposed tough safety restrictions on Mexican trucks.

[18] USTR Zoellick commented on the proposal being debated in the Senate that it violates the spirit of NAFTA by holding Mexico to a different standard than the United States or Canada (BNA, *International Trade Daily.* Aug. 2, 2001). See also Sara J. Fitzgerald, "Why Stricter Standards on Mexican Trucks Will Hurt Our Neighbor and Ourselves," the Heritage Foundation, *Executive Memorandum No. 766,* Aug. 10, 2001, found at Internet address *http://www.heritage.org/library/execmemo/em766.htm*l, retrieved on Apr. 2, 2002.

[19] White House, "Fact Sheet on Trucking," *Office of the Press Secretary,* found at *http://www.whitehouse.gov* on Sept. 6, 2001.

[20] Ibid.

[21] Duane W. Acklie, statement prepared for hearing on the NAFTA Arbitration Panel Decision and Safety Issues Related to Implementing the North American Free Trade Agreement's Motor Carrier Provisions, testimony before the Commerce, Science and Transportation Committee, U.S. Senate, July 18, 2001, p. 2.

[22] To date very few U.S. trucks are to be found on Mexican roads, even though the Mexican Government has not taken any reciprocal action thus far of restricting access for U.S. trucks.

[23] Chris Kraul, "NAFTA May Deliver Blow to Truckers," *Los Angeles Times*, Aug. 15, 2001.

Mexican trucks as they cross the border,"[24] and that "...there is real evidence that trucks from Mexico cannot meet all the U.S. safety standards."[25] In addition, Mr. Hoffa disputed that the United States is obligated under the terms of NAFTA to act on the panel's recommendation to begin accepting applications on a case-by-case basis; he advocated instead, to keep the border closed for as long as needed and let Mexico take reciprocal action.[26]

Meanwhile, not everyone in the United States agreed with the Teamsters' concern about safety. A New York Times editorial wrote in August that "The Teamsters Union and some of its Congressional allies have grossly overblown the threat on American highway safety from an open border. Mexico's long-haul trucking fleet is a lot more modern and its drivers are a lot more professional than the union's scare tactics would suggest."[27] Advocates of free access generally claimed that safety concerns were based solely on the poor records of the drayage trucks. The owners of these trucks had no incentive to maintain them, since they provided short-haul service.[28] With free access–these sources allege–the well-maintained long haul trucks would drive out the drayage trucks, thus the safety problem would diminish.

Analysts also considered other important possible consequences of free access; they speculated for example on how large the volume of Mexican trucks on U.S. roads would become, and how U.S. truck drivers' wages would be affected by the presence of Mexican drivers on U.S. roads. Antagonists of free access were concerned that opening the border would attract an invasion of Mexican trucks to the United States. Others doubted this outcome, arguing that Mexican truckers would need years to build a network of U.S. customers to keep their trucks loaded in both directions, i.e. minimize "dead-heading" (empty trucks) on the way back.[29] As to the effect of free access on wage levels, from the beginning of the dispute, advocates of free access have charged that the Teamsters' position on safety actually masked another concern, i.e. that competition by the low wages of Mexican truck drivers would depress U.S. wages in the trucking industry.[30]

Mexican Arguments

As in the United States, Mexican views differ sharply on the issue of free trucking access to the United States. Not all Mexicans agree that free cross-border trucking would be in their interest.

The administration of Mexican President Vicente Fox, convinced that competition with the United States would be the best avenue to make Mexican trucking more efficient, is determined to see NAFTA's trucking provisions implemented.[31] On August 2, 2001, President Fox announced that, in case the restrictive U.S. bills of August 2001 become law, he might consider barring U.S. trucks from his country in retaliation against the United States.[32] Mexican officials have been deliberating other forms of retaliation as well, such as curtailing agricultural imports from the United States[33] or imports of U.S.-made fructose from the United States.[34]

The Fox Administration's position that implementation of NAFTA would improve the efficiency of Mexican trucking services is shared by a minority of Mexican truckers, those whose operations are already state of the art. The associations representing advanced truckers, including the Mexican Association of Private Transport, also favor unrestricted cross-border trucking.[35] These advanced fleets, generally owned or contracted out by big companies, including Coca-Cola and Cemex (Mexico's large cement manufacturer), are believed to be fully competitive with U.S. truckers.

However, some four fifths of the commercial truckers in Mexico, represented by the Confederation of Mexican Transporters (CANACAR), are not competitive with their U.S. counterparts either in the U.S. or the Mexican market. Even though labor costs are lower in Mexico, the cost of parts, fuel, financing, and insurance is significantly higher. Concerned about the challenges of free competition with U.S. trucks, these Mexican fleet-owners prefer to maintain the "status quo" of being restricted to the border zone. CANACAR, presumably relieved by the reluctance of the U.S. Congress to admit trucks from Mexico into the United States, requested the Mexican Government not to insist on implementing NAFTA, but to aim instead

[24] Jim Hoffa, President, International Brotherhood of Teamsters, statement at hearing on Cross-Border Truck and Bus Operations, testimony before the Commerce, Science, and Transportation Committee, U.S. Senate, July 18, 2001, transcript of hearing, p. 46.

[25] Ibid.

[26] Ibid.

[27] "Free Trade and Mexican Trucking," editorial, *The New York Times,* Aug. 6, 2001.

[28] Brendan M. Case, *The Dallas Morning News,* op. cit.

[29] Brendan M. Case, *The Dallas Morning News,* op. cit.

[30] Boston Globe, "Truck Safety Ploy," editorial, Aug. 12, 2001. See also Magdolna Kornis, op. cit.

[31] Chris Kraul, *Los Angeles Times*, op. cit.

[32] Even though Mexico thus far has not restricted their entry, no U.S. trucks are operating on Mexican roads.

[33] Bureau of National Affairs,"Truck Battle Intensifies," *International Trade Daily*, July 31, 2001.

[34] Bureau of National Affairs,"Mexican Truckers Say $2 Billion Lost Due to U.S. Noncompliance with NAFTA," *International Trade Daily,* July 3, 2001. Mexican antidumping duties on High-Fructose Corn Syrup (HFCS) from the United States and taxes on soft drinks sweetened with HFCS from the United States are another major trade issue between the two countries.

[35] Chris Kraul, *Los Angeles Times*, op. cit.

at the suspension of the NAFTA provision on trucking.[36]

After the long-sought access of trucks to the United States had been finally granted at the end of 2001,[37] a Mexican Congressman and president of the Confederation of Mexican Transporters (CANACAR) said that "... any U.S. company can now destabilize the Mexican trucking industry, because it is not a competition between equals."[38]

Agreement

General concern about foreign access to the United States increased sharply in the wake of terrorist attacks of September 11, 2001, threatening further delays in the resolution of the trucking issue. Yet, before the end of the year, the House and the Senate reached a bipartisan compromise for the purposes of the 2002 transportation appropriations bill,[39] allowing Mexican trucks to enter the United States, provided they met specified old and newly added safety requirements. This is the bill President Bush signed into law on December 18.[40]

U.S. and Mexican transportation and trade officials began to negotiate operating regulations to be imposed on access by U.S. and Mexican trucks to one another's country. A report issued by the General Accounting Office at the end 2001 praised Mexican efforts to improve truck safety and air emission regimes.[41] The same report urged DOT to reach agreements with the border states and the other federal agencies involved, regarding the development of extended truck inspections. DOT reportedly expects to open the border to Mexican trucks sometime in the second quarter of 2002.[42]

[36] Chris Kraul, *Los Angeles Times*, op. cit., and Bureau of National Affairs, "Wary of Discrimination, Mexico to Inspect Coming Rules on Cross-Border Truck Safety,"*International Trade Daily,* Dec. 13, 2001.

[37] See following section.

[38] John Nagel, Bureau of National Affairs, "Mexico's Trucking Rules Will Mirror U.S. Cross-Border Regulations," *International Trade Daily,* Dec. 6, 2001.

[39] A conference report on DOT funding was cleared by the House on Nov. 30, 2001, and by the Senate on Dec. 4, 2001.

[40] P.L. 107-87.

[41] General Accounting Office, "North American Free Trade Agreement: Coordinated Operational Plan Needed to Ensure Mexican Trucks' Compliance with U.S. Standards," Dec. 21, 2001, GAO 02-28.

[42] Rossella Brevetti, Bureau of National Affairs, "GAO Faults U.S. Readiness to Ensure Safety of Mexican Trucks," *International Trade Daily*, Jan. 9, 2002.

The Euro-Mediterranean Partnership

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The EU has renewed its attention on its Mediterranean neighbors and made important progress under the trade component of the Euro-Mediterranean Partnership, its broad policy initiative with the region. To help achieve the long term goal of forming a Euro-Mediterranean free-trade area by 2010, the EU is negotiating bilateral association agreements with Mediterranean countries. Empirical research suggests that the welfare effects of the association agreements are positive, but that the benefits from the proposed Euro-Mediterranean free-trade area would be greater, especially for the Mediterranean partners.

With a revived focus on Mideast affairs and countries stemming from the events of September 11, 2001, the EU has renewed attention to its Mediterranean neighbors and made important progress under its broad policy initiative with the region. In 1995, the EU launched the Euro-Mediterranean Partnership (sometimes referred to as the Barcelona Process), a comprehensive initiative governing the EU's economic, political, and social relationship with its 12 Mediterranean neighbors. The major goals of the Partnership are to promote peace, stability, and prosperity throughout the region. To help ensure these goals are met, the Partnership aims to create a Euro-Mediterranean free-trade area (FTA) by 2010. The population of this FTA could measure over 700 million, counting countries in central and eastern Europe that are currently negotiating to join the EU, somewhat less than the approximately 800 million people that would comprise the Free-Trade Area of the Americas (FTAA), currently under negotiation among Western Hemisphere countries. In the run-up to 2010, the EU is negotiating association agreements with Mediterranean partners to expand free trade bilaterally. Currently, the EU has concluded association agreements with all but one of these Mediterranean countries.

Background

The 12 Mediterranean partner countries, with a population of about 229 million, are: Algeria, Morocco, and Tunisia–the 3 collectively known as the Maghreb–Egypt, Israel, Lebanon, Jordan, the Palestinian Authority, Syria, Turkey, Cyprus, and Malta. Cyprus and Malta have applied to join the EU and are currently negotiating accession (see *IER*, Nov.-Dec. 2001). They could become members of the EU as early as 2004. Turkey has also applied to join the EU, but is not presently negotiating to join. A customs union between Turkey and the EU entered into effect in January 1996.

With the other nine Mediterranean countries, the EU is negotiating association agreements to replace the first generation bilateral cooperation agreements that the EU negotiated with Mediterranean countries in the 1970s. In the earlier agreements, the EU generally granted unilateral duty-free treatment for industrial products, with limited concessions for agricultural products. The trade-related provisions of the new association agreements are broadly similar and can be distinguished from these past agreements by the greater degree of market access granted to EU products in the Mediterranean countries. Each of the new association agreements calls for bilateral free trade covering industrial products and the progressive liberalization of trade in agricultural products, such as the widening of tariff-rate quotas. Under the new agreements, EU concessions in agriculture remain limited; however, a review of the agricultural situation is provided for at a later time. They also call for the parties to assess the possibility of liberalizing trade in services at a future date. Depending on the agreement, the Mediterranean partner could have up to 15 years to dismantle tariffs on EU exports.

In addition to trade liberalization, the agreements cover cooperation in a range of other areas. The EU will provide technical and financial support to implement the association agreements, including for example, the restructuring of customs administrations, support for standards and technical regulatory bodies, and strengthening of the statistics system. The agreements also commit Mediterranean partners to economic liberalization, including modern legislation on competition and the protection of intellectual

[1] The views expressed in this article are those of the authors. They are not the views of the U.S. International Trade Commission (USITC) as a whole or of any individual Commissioner.

property rights. New institutional structures will be set up to facilitate cooperation on a host of other issues, ranging from education and culture to the fight against crime and terrorism. The European Union established a financial instrument in 1996, known as "MEDA," to provide technical and financial support for economic and social reforms in the Mediterranean partners.[2]

Status of the Association Agreements

Such association agreements with three of the nine Mediterranean countries have been ratified and have entered into force: Tunisia (March 1998), Morocco (March 2000), and Israel (June 2000). The agreement with Jordan was ratified in March and is scheduled to enter into force on May 1, 2002. An interim agreement with the Palestinian Authority has been in effect since July 1997, but implementation to date has been limited. According to the European Commission, Israeli impediments to Palestinian trade and insufficient capacity of the Palestinian economy have constrained progress. Also, the sensitive political situation has prevented the negotiation of a full Association Agreement.[3]

Cooperation agreements continue to govern EU trade with Algeria, Egypt, Lebanon, and Syria. Negotiations with these four countries are at different stages. The agreement with Egypt was signed in June 2001 and awaits ratification. Ratification is required by the European Parliament and the parliaments of each of the 15 EU member states as well as the Mediterranean partner.

The agreement with Algeria was initialed on December 19, 2001, and is expected to be signed later in 2002. The association agreement with Lebanon was initialed on January 10, 2002. Because ratification is often a long process, the EU and Lebanon agreed to conclude an Interim Agreement that would implement the trade aspects of the association agreement, probably in mid-2002. Syria was the last of the Mediterranean partners to begin negotiations for an association agreement with the EU in 1997. Negotiations to dismantle tariffs are underway, but progressing slowly. Syria's economy is highly protected and reforms of the industrial sector are far less advanced than in the other Mediterranean partners.

In May 2001, Euro-Mediterranean trade ministers met for the first time since the Barcelona Process began in 1995. Ministers noted that in the Mediterranean region "the increase in trade and the attraction of investments in the last five years has been insufficient, compared to other areas such as Central and Eastern Europe and Latin America, where trade and investment by the EU has grown faster."[4] To achieve the full potential of a Euro-Mediterranean area, the ministers stressed the importance of concluding association agreements as well as the importance of developing trade between the Mediterranean partners. In 1999, about 52 percent of Mediterranean trade was with the EU, and only 5 percent was among Mediterranean countries.[5] The ministers also noted that although foreign direct investment remains stable in the region, it is low compared to other developing countries. EU officials have pointed out that investors believe the Mediterranean is too "fragmented, split into tiny, separate markets with conflicting standards and rules,"[6] and often has a poor business environment (e.g., inadequate infrastructure and services).[7] To help remedy this situation, the trade ministers set up two working groups. One group aims to improve the efficiency of the service sector by exchanging information and building capacity in Mediterranean partners to prepare them to negotiate liberalization of services trade. The other working group is to harmonize rules of origin with the aim of extending the pan-European system of cumulation to the Mediterranean. Work on rules of origin is likely to first focus on the textiles and apparel sector, an important sector in trade. The ministers also agreed to identify additional areas where a convergence of legislation could help spur trade and investment. In particular, they referred to norms and industrial standards, sanitary and phytosanitary legislation, intellectual and industrial property rights, competition policy, and customs legislation.[8]

[2] Council Regulation (EC) No. 1488/96 of 23 July 1996 on financial and technical measures to accompany (MEDA) the reform of economic and social structures in the framework of the Euro-Mediterranean partnership.

[3] European Commission, "The EU and Gaza West Bank," found at Internet address *http://europa.eu.int/comm/external_relations/gaza/intro/index.htm*, retrieved Nov. 14, 2001.

[4] *Euro-Mediterranean Ministerial Meeting on Trade, Presidency Conclusions*, Brussels, May 29, 2001.

[5] European Commission, *Euromed Special Feature*, Issue No. 22, June 7, 2001, found at Internet address *http://europa.eu.int/comm/external_relations*, retrieved Dec. 6, 2001.

[6] "EU Welcomes Moroccan Economic Reforms," *European Report*, No. 2626, Oct. 13, 2001, p. V-4.

[7] For a good discussion on foreign direct investment in the Mediterranean, see *The Euro-Mediterranean Partnership in the Year 2000, Second FEMISE Report on the Euro-Mediterranean Partnership*, Heba Handoussa, Economic Research Forum, Egypt, and Jean-Louis Reiffers, Institut de la Méditerranée, France, Coordinators, July 2000.

[8] *Euro-Mediterranean Ministerial Meeting on Trade, Presidency Conclusions*, Brussels, May 29, 2001; and European Commission, *Euromed Special Feature*, Issue No. 22, June 7, 2001, found at Internet address *http://europa.eu.int/comm/external_relations*, retrieved Dec. 6, 2001.

On March 19, 2002, in the second ministerial meeting on trade, Euro-Mediterranean trade ministers noted that progress toward the FTA requires substantial efforts to improve "South-South" integration (that is, between the Mediterranean countries themselves) and that "in terms of regional integration, the experience of the past years clearly showed that tariff dismantling alone was not enough to ensure rapid development of trade and a significant rise in direct investment."[9] Therefore, the ministers agreed to establish a Working Group on Trade Measures Relevant for Regional Integration. The working group is charged with developing an Action Plan on Trade and Investment Facilitation, which will address customs procedures, standardization issues and conformity assessment, the regulatory framework for investment, and the protection of intellectual property rights.

EU-Mediterranean Trade

In 2000, the Mediterranean partners together accounted for 6 percent of the EU's imports and 9 percent of its exports, or about 8 percent of extra-EU trade, ahead of EU trade with Japan and China. This percentage was about the same as in 1991. Turkey, Israel, and Algeria were the EU's top three partners among the twelve and accounted for almost two-thirds of EU-Mediterranean trade.[10] The EU has traditionally registered a trade surplus with the region, despite a significant deficit in the energy sector.

The composition of EU-Mediterranean trade has changed little over the past decade. Over 80 percent of total trade consists of energy, miscellaneous manufactured products (for example, clothing, footwear, and furniture), and machinery and transport equipment. The energy sector accounted for almost 30 percent of EU imports from the region in 2000. In particular, petroleum products accounted for over 20 percent of EU imports. Algeria, Syria, and Egypt accounted for 94 percent of Mediterranean energy exports to the EU in 2000, with Algeria accounting for nearly 70 percent of this amount. The second largest EU import from the region was clothing, which accounted for nearly 18 percent of EU imports from the region in 2000. The largest category of EU exports to the Mediterranean was the machinery and transport sector, which accounted for about 45 percent of EU exports to the region. This trade pattern is typical of trade between industrialized and developing countries. Road vehicles were the largest export, accounting for over 11 percent of EU exports to the area. In general, EU exports to the Mediterranean countries in the machinery and transport sector were capital-intensive goods. Turkey and Israel were the largest traders among the Mediterranean partners in this sector, reflecting Turkey's developing automobile industry and Israel's strong telecommunications equipment exports to the EU.[11]

Potential Effects in Theory and Practice

Empirical research suggests that trade, whether interregional or international, raises income.[12] Larger countries tend to have more interregional trade and thus higher incomes than countries with small domestic markets and closed economies. Recent research supports the hypothesis of exports as a potential engine of growth for small developing countries. For the Mediterranean partners of the European Union–Mediterranean Association Agreements (EU-MAAs), accessing the larger EU market should result in net welfare gains for all members. Under the theory of comparative advantage, when a nation reduces barriers to a trading partner, national resources adjust through specialization toward areas of comparative advantage relative to the trading partner. Theoretically, EU-MAA partners attain higher levels of welfare from specializing in their areas of comparative advantage and exporting to their trade partners. The net welfare position will include losses to factors in those sectors which are declining, especially returns to specialized labor and capital in the industries in decline. For the Mediterranean partners, these would include inefficient state-owned enterprises and protected domestic industries with high levels of inefficiency due to import-substitution policies. Wages to labor and rents to capital will fall in these declining sectors and increase in the growth sectors as the economy adjusts in response to changes in relative prices brought about by the EU-MAAs. Because EU trade with the Mediterranean countries is small relative to total EU trade, individual Mediterranean partners are too small to influence the terms of trade for their export commodities to the EU. This implies the small country model for the Mediterranean partners. Under the small country model, unilateral trade liberalization is superior to regional or multilateral (reciprocal) trade liberalization at improving the welfare of the small

[9] European Commission, "Conclusions of the Presidency–Euro-Mediterranean Ministerial Conference on Trade, Toledo, 19 March 2002," press release IP/02/437, Mar. 19, 2002.

[10] Eurostat, "EU-15 and the 12 Mediterranean Partners: Solid Trade Links," *Statistics in Focus*, External Trade, 7/2001.

[11] Eurostat, "EU-15 and the 12 Mediterranean Partners: Solid Trade Links," *Statistics in Focus*, External Trade, 7/200; and European Commission, "World Trade Organization Ministerial Conference, The EU Figures for the Doha Conference," Nov. 8, 2001.

[12] Frankel, Jeffrey A. and David Romer, "Does Trade Cause Growth?" *The American Economic Review,* 1999, Vol. 89(3), pp. 379-399.

country.[13] All Mediterranean partners suffer from asymmetry relative to the EU trade bloc, as their economies are significantly smaller and less-developed.

The EU-MAAs have been nick-named the hub-and-spoke agreements. This system represents a free-trade arrangement between Europe and the Mediterranean partners that indirectly links the Mediterranean economies. The EU acts as the hub for the Mediterranean spokes. Although a Euro-Mediterranean free-trade area is a goal of the Barcelona Declaration establishing the Euro-Mediterranean Partnership, the bilateral hub-and-spoke agreements may slow Mediterranean regional economic integration as the small Mediterranean countries have limited government resources to negotiate agreements. Nonetheless, implementation of the bilateral association agreements will encourage regional integration by improving harmonization of standards and technical efficiency in the Mediterranean countries. Four of the Mediterranean partners–Egypt, Jordan, Morocco, and Tunisia–and initiated negotiations for regional trade liberalization in 2001.

What are the possible consequences of forming a bilateral hub-and-spoke system with the EU as the hub? With a hub-and-spoke system, the hub enjoys free trade with all the participants, while the spokes do not liberalize with respect to one another. Thus, the hub enjoys the maximum benefits of this free-trade system. This means the EU hub has significantly more to gain from the EU-MAAs than the Mediterranean partners. The hub will get a larger share of the welfare gains at the expense of the spokes.[14] For example, under the EU-MAA, EU firms will be able to access markets for exports and obtain least cost inputs from any of the Mediterranean partners, whereas firms in each of the Mediterranean partners will only see trade liberalization relative to the EU. Firms in the Mediterranean partners will lose competitiveness relative to the EU under the hub-and-spoke system. Under the hub-and-spoke system, the EU gains a competitive advantage in each market, not enjoyed by the Mediterranean partners. Some industrial trade that normally takes place directly between Mediterranean partners may be diverted through the EU to take advantage of the EU's preferential position in the system. This can cause trade diversion that reduces the net welfare gains from trade liberalization under the EU-MAAs. This kind of trade diversion would increase demand in the EU services sector (transport, insurance, banking) at the expense of service sectors in the Mediterranean partners. Besides the preferential benefits to EU firms of the special hub status, the EU has concern with slowing the immigration flow from the region. Improved investment and employment opportunities in the Mediterranean partners would improve employment in the growth sectors, with the potential for net reductions in unemployment and reduced pressure for migration to the EU.

The EU is the biggest investor in the Mediterranean partner countries. The EU-MAAs are likely to increase confidence in these economies, encouraging investment from the EU, especially repatriation of capital and remittances from Mediterranean workers in the EU. Although market access under the EU-MAAs is expected to attract investment to the Mediterranean partners, the biggest investment flows may be into the EU. Given the EU's preferential treatment in all the EU-MAA member markets, firms would prefer to locate at the hub. A Mediterranean member would be less attractive because there are no tariff reductions relative to other Mediterranean partners. Production growth would be centered at the hub in this type of trading system. Gains from economies of scale and clustering of industry are more likely for the EU than the Mediterranean partners. EU industrial clusters that might form under the hub-and-spoke EU-MAAs are unlikely to shift to Mediterranean partners upon completion of an EU-Mediterranean FTA proposed for 2010.[15] The Mediterranean partners would have greater opportunities for FDI under a free-trade area than the EU-MAAs, because of the market distortions caused by the hub-and-spoke system.

Nevertheless, the Mediterranean partners face numerous potential gains from the EU-MAAs. First, they will immediately enjoy increased access to the EU market, other than for agricultural products. Second, they will have improved domestic efficiencies from elimination of their tariff barriers over the 12-15 year phase-in periods. Developing countries have the potential for more efficiency gains from implementing free-trade agreements than their industrialized partners due to the high level of trade barriers observed in most developing countries. Gains from trade liberalization include improved efficiency in sectors previously protected by trade barriers and increased transparency for doing business. Reduced tariff and nontariff barriers lower domestic prices and price distortions. For the EU-MAAs, this will only be true in the manufacturing and some service sectors. Agricultural prices will remain high and may even increase in the food importing Mediterranean countries. As a result of improved market access under the EU-MAAs, the Mediterranean partners are expected to attract some

[13] Bernard Hoekman and Simeon Djankov, "Catching up with Eastern Europe? The European Union's Mediterranean free trade initiative," in *Opening Doors to the World*, Raed Safadi (editor), The American University in Cairo Press, 1998.

[14] For a theoretical discussion of the hub-and-spoke system versus free-trade areas, with references to NAFTA, see Ronald Wonnacott, "Trade and Investment in a Hub-and-Spoke System Versus a Free Trade Area," *The World Economy*, 1996, Vol. 19 (3), pp. 237-252.

[15] Ronald Wonnacott, "Trade and Investment in a Hub-and-Spoke System," op. cit.

foreign direct investment, resulting in improved economic growth and industrialization. Management practices, productivity, and technology should improve in the Mediterranean countries as a result of greater association with the higher income, industrialized EU. Trade agreements in general have been shown to stimulate domestic economic reforms in developing countries. This is especially relevant for the Mediterranean partners, who lag behind Latin America and Eastern Europe in reforming their economic policies. However, a stable macro-economy, public institutions, privatization of state monopolies, efficient services sectors, private savings and investment cannot be imported through a free-trade agreement.[16]

It should be noted that the potential welfare gains to the Mediterranean partners would be greater under the proposed EU-Mediterranean FTA than the EU-MAA hub-and-spoke system. Under an FTA, trade barriers are reduced among all members, not just between the EU hub and each of the Mediterranean spokes. Morocco, Tunisia, Egypt, and Jordan agreed in 2001 to move forward in liberalizing regional trade. A free-trade area would have lower overall tariffs and thus greater welfare gains for all members. This should encourage the Mediterranean partners to eliminate regional trade barriers. An FTA would also remove any preferential income gains enjoyed by the EU as the hub of the EU-MAAs. However, the EU would be receiving a smaller share of a much larger income pie. Under an FTA, the Mediterranean partners would have more opportunities to benefit from economies of scale, improved competition, and regional bargaining power. The Mediterranean partners have less bargaining power under the EU-MAAs than they would have had under a free-trade agreement where they could have combined resources in negotiating with the EU in areas of common interest. It is unlikely that the individual Mediterranean partners, which are all small developing countries, were able to exert much negotiating power on the EU. A free-trade area would allow Mediterranean partner firms to have equal access to Mediterranean markets and low-cost inputs, putting them on equal footing with EU firms. If the Mediterranean partners successfully form a regional free-trade area in 2010 that directly eliminates barriers between Mediterranean partners, any trade diversion created by the EU-MAAs would be eliminated. At that time, the EU firms would lose their temporary preferential access to Mediterranean markets under the EU-MAAs.

The EU-MAAs relative to an FTA create more administrative work because the EU agreements with each Mediterranean partner are negotiated separately and contain different features. Firms must comply with rules of origin that would not be as pervasive under a free-trade agreement. Firms will need to familiarize themselves with each separate agreement to conduct business within the hub-and-spoke system. The Mediterranean partners stand to lose a substantial amount of customs revenue under the EU-MAAs, which explains the long phase-in periods allowed for the Mediterranean partners. It is estimated that Morocco will lose approximately two-thirds of its customs revenue under the latest version of its EU-MAA. This negative effect on public finances will reduce the net welfare gains from bilateral trade liberalization with the EU. However, the EU-MAAs include provisions for technical and financial aid from the European Union to assist the Mediterranean countries during the transition from protectionism to liberalized trade. The MEDA program provides for grants to the Mediterranean partners to help reduce the financial pain of lost domestic industry competitiveness and lost tariff revenues.[17]

Conclusions

The newest round of bilateral association agreements between the European Union and Mediterranean countries is an important step at moving the Mediterranean partners toward free trade. Although the EU-MAAs will result in greater welfare gains for the EU hub than the Mediterranean spokes, the goal of eventually forming a Euro-Mediterranean FTA by 2010 will remove any temporary advantages caused by the EU-MAAs. Because the Mediterranean partners will benefit more from regional integration under a Euro-Mediterranean FTA than bilateral arrangements under the EU-MAAs, they should move forward as quickly as possible with negotiations aimed at such a regional FTA.

[16] Bernard Hoekman and Simeon Djankov, "Catching up with Eastern Europe?," op. cit.

[17] *Khaleej Times*, "Lebanon to Sign Euro-Med Deal," found at Internet address *http://www.khaleejtimes.com*, retrieved Dec. 17, 2002.

A WTO Agreement on Competition Policy: Prospects and Pitfalls

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This paper briefly reviews the debate over inclusion of competition policy in the WTO and offers some ideas of where such negotiations might lead. It discusses the main sources of conflict that have precipitated the move to a multilateral agreement and analyses whether the WTO is capable of resolving them. The main conclusion is that the prospects of bringing competition policy into the WTO are rather dim, in part because the current system works fairly well and in part because the machinery of the WTO at present, is not well suited for handling competition issues.

Introduction

The November 2001 declaration of the Fourth WTO Ministerial Conference in Doha, Qatar, provided a contingent mandate for negotiations on a range of subjects previously thought to be outside of the domain of international trade policy. One of the most important and complex of these subjects is competition policy. The core of competition policy is competition law (i.e., antitrust law), the set of rules and disciplines maintained by governments relating either to agreements between firms that restrict competition or to the abuse of a dominant position-including attempts to create a dominant position through merger.[2] Exactly which aspects of competition law might come under negotiation has yet to be determined–that decision has been left for ministers to decide at the Fifth Ministerial in 2003. However, that negotiations might occur at all, and that national competition law might one day become subject to a degree of WTO control, is both remarkable and controversial.

Proponents of including competition law in the WTO argue that globalization has increased the degree to which national competition laws have international effects. To the extent that each nation neglects the interests of its neighbors in making its competition decisions, there is a case for an international agreement. Of particular concern for the WTO is that national governments may come to use competition law as a protectionist device, thereby undoing the very trade liberalization the WTO has worked so hard to achieve.

Opponents of a WTO competition agreement argue that cases of conflict between national competition authorities are empirically unimportant and too small to justify the trouble of negotiating and maintaining an international agreement. Such an agreement, if part of the WTO, would divert attention from more important trade reforms, unnecessarily tax the WTO dispute-settlement system, and strengthen the popular perception of the WTO as a usurper of national sovereignty. Moreover, opponents argue that there is a fundamental incompatibility in objectives between competition and trade laws: competition law seeks to maximize welfare-in which the interests of consumers figure prominently-whereas trade law is generally based on mercantilist principles of import protection and export promotion.

This paper offers a brief review of the debate over inclusion of competition policy in the WTO, along with some ideas about where the proposed negotiations might lead. It begins with some examples of international conflict over competition policy that have led to calls for an international agreement. It then discusses some of the pitfalls that may be encountered when attempting to establish and maintain such an agreement. Finally, we discuss the current institutions and the extent to which they form a basis for multilateral agreement. The main conclusion is that the prospects of bringing competition policy into the WTO are rather dim, in part because the current system works fairly well and in part because the machinery of the WTO, as it currently works, is not well suited for handling competition issues.

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[1] The views expressed in this article are those of the author. They are not the views of the U.S. International Trade Commission (USITC) as a whole or of any individual Commissioner.

[2] Hoekman and Holmes (1999) define competition policy to include both competition law and other policies designed to promote competition in domestic markets–such as deregulation, privatization, and antidumping. This paper focuses on competition law, as these other policies have not been at the center of OECD or WTO discussions on competition policy. Whether antidumping, in particular, should be included in competition policy is a matter of controversy in the WTO.

Archetypes of International Conflict over Competition Policy

In principle, there are many ways in which national competition laws can have international spillovers, and quite a few of them involve direct effects on international trade. In practice, the competition issues that have generated the most conflict between governments–providing the impetus for negotiations–are relatively few. The four main issues that have occupied the attention of policymakers and scholars on this subject are vertical restraints, mergers, parallel imports, and international cartels.

Vertical Restraints

Perhaps the most common complaint by WTO members is about vertical restraints,[3] arrangements between vertically related entities (e.g., manufacturers, wholesalers, and retailers) that exclude competitors. Some regard the use of vertical restraints by domestic firms to exclude foreign competitors as an impediment to international trade. A further concern is that governments may contribute to the exclusion of foreign suppliers through lax or discriminatory application of competition law.

The United States confronted the WTO with this issue in the recent case involving photographic film giants, Kodak and Fuji. Kodak alleged that its access to the Japanese film market had been unlawfully blocked by Fuji, through the latter's control of the local film distribution system. By excluding Kodak from access to film wholesaling networks, Fuji had forced Kodak to sell directly to retailers at higher cost. The key allegation was thus of an anti-competitive vertical relationship between Fuji and its primary distributors. But what started out as a dispute between private firms quickly turned into a spat between governments. In 1996, the United States brought the case to the WTO charging that the Government of Japan had aided Fuji. They brought this case as a so-called non- violation complaint under GATT Article XXIII:1(b). This non-violation provision allows members to challenge government measures that "nullify or impair" trade liberalization commitments even though the measures themselves are not subject to WTO rules (Hoekman and Mavroidis, 1994). Japan responded that the control by Fuji of wholesale networks was irrelevant, since most of the retailers they served also bought imported film and that Kodak's own distribution system amounted to the creation of a wholesale system of its own.

[3] This view is supported by surveys of WTO member governments taken by the WTO Working Group on Trade and Competition Policy. See WTO (1998a).

The WTO dispute panel accepted the U.S. argument that measures taken by Japan, including the Japan Fair Trade Commission's failure to find Fuji's practices anti-competitive, could potentially affect trade. However, it concluded there was no actual impairment of U.S. market-access rights in this case (WTO, 1998b, p. 421). Thus, even though the United States lost its case on the facts, it did establish the principle that vertical restraints may be considered denial of market access to foreigners and that a government's failure to prevent such practices may nullify or impair the benefits of a trade agreement.

Mergers

The last decade or so has seen a major wave of mergers, many of them with cross-border effects. Even when the merging firms themselves are from the same country, competition authorities from different countries can assert jurisdiction if the firms' exports to those jurisdictions constitute a significant market share. If different authorities use different criteria, or the merger is likely to have different effects on different countries, then a merger approved by one country might well be rejected by another. At best, this would be burdensome to the merging firms. At worst, competition authorities may apply standards to such mergers based on protectionist motives.

While the vast majority of global merger cases are handled without interjurisdictional conflict, the recent merger of Boeing and McDonnell Douglas, a case reviewed by both U.S. and EU competition authorities, illustrates the potential for problems. The Boeing–McDonnell Douglas merger involved two U.S.-based firms whose combined sales in the EU were sufficient for the EU to claim right of scrutiny. While the United States approved the merger, the EU refused to grant its approval, unless Boeing agreed to give up certain of its long-term exclusive sale contracts with several airlines, contracts that prevented the airlines from buying aircraft from the EU-based Airbus. The contracts in question pre-dated the merger. Thus, the EU objection was not designed to prevent a merger that would result in higher prices for aircraft buyers. It was to force Boeing to give up market share to Airbus (Hoekman and Holmes, 1999). In the end, the EU approved the merger, but only after Boeing agreed not to enforce the exclusive contracts.

This case illustrates several features of the current merger system that have led to calls for better international cooperation. Different countries may have very different views of the same merger case, and the cost of satisfying these diverging concerns falls squarely on the merging firms. If the firms are foreign, then a national competition authority may have little incentive to take these costs into account. Furthermore, a national competition authority may use its power to protect its domestic firms. In the extreme, a government might even use merger approval as an instrument to achieve objectives entirely unrelated to promoting competition.

Parallel Imports

The control of parallel imports involves both trade and competition law and, in practice, it usually involves intellectual property rights (IPRs) as well. When a firm has a monopoly on a product, say, due to copyright or patent, it normally distributes that product through its own authorized channels. Parallel imports are products that enter a country outside of the firm's authorized channels. Parallel imports interfere with the ability of the monopolist to price-discriminate between different countries.

A recent case involves the United States and New Zealand. In 1998, the Government of New Zealand passed an amendment to its Copyright Act legalizing parallel imports. This prompted U.S. copyright holders in the film, music, software, and publishing industries to complain to the United States Trade Representative that parallel imports would impair their ability to detect and combat piracy and reduce the value of their property rights both in New Zealand and elsewhere. In response the USTR began a Special 301 review and placed New Zealand on its Special 301 "watch list" in 1999. In December of 1999, New Zealand announced that it would impose restrictions on parallel imports, not, it said, to satisfy U.S. demands but to foster the development of its own cultural industries. So far it has not changed its policy (USTR, 2001).

A country's treatment of parallel imports hinges on whether it adopts a principle of international exhaustion or of national exhaustion (or regional exhaustion in the case of the EU). Exhaustion refers to one of the legal limits of IPRs. The right to control the commercial exploitation of an IPR-protected product are said to be "exhausted" once the product has been sold for the first time. Unless otherwise specified by law, subsequent acts of resale, rental, lending or other forms of commercial use by third parties can no longer be controlled by the IPR holder. There is a fairly broad consensus that this rule applies at least within the context of the domestic market (national exhaustion), but there is no consensus as to whether it should apply to the world market (international exhaustion). The treatment of parallel imports is likely to become an important issue in the WTO negotiations on competition law, with small countries pushing for the principle of international exhaustion, and large countries that export branded, copyrighted, or patented products, insisting on the principle of national exhaustion (Cottier, 1998).

International Cartels

The only area in which there appears to be widespread support for reaching a common standard in competition policy is in the prosecution of "hard core" international cartels. Hard core cartels are defined by the Organization for Economic Cooperation and Development (OECD) to be "anti-competitive agreements by competitors to fix prices, restrict output, submit collusive tenders, or divide or share markets" (OECD, 2000). The reason for the convergence on this issue is that the EU and United States already have very strong and quite similar rules against cartels, whether domestic or international. As most of the known cases of international cartels involve firms from industrialized countries, developing countries rarely see any benefits from cartels (other than state trading firms) and thus are willing to support an international agreement to prohibit them.

The magnitude of the problem of international cartels is not known for certain, as the sample of known cartels consists of only those that get caught. During the 1990s, the United States and the EU prosecuted some 39 international cartels on charges of price fixing. According to OECD and World Bank estimates, these cartels cost consumers worldwide tens of billions of dollars in higher prices. The most notorious cases were the global cartels in citric acid, graphite electrodes, lysine and vitamins, the French TGV (*train à grande vitesse* or high speed train) cartel, and Spanish sugar cartel.

Do These Cases Justify a WTO Competition Agreement?

Except in the case of cartels, there has been no serious empirical work to determine the magnitudes of the problems discussed in the previous section. This has led many to dismiss an international competition agreement on the grounds of empirical irrelevance. However, if it is not known how important the various international competition issues are, it may be possible to predict whether they will become more or less important over time, as globalization proceeds. If trade and investment liberalization makes international competition problems more severe, and further liberalization is seen as desirable or inevitable, then this would support the current push to put in place an international competition policy framework.

The simplest argument on the relationship between globalization and competition goes like this: as globalization increases the frequency of international transactions, it increases the likelihood that an anti-competitive practice perpetrated by any firm will harm the residents of another country. Thus, competition policy will increasingly become a global issue. The equally simple counter argument is that globalization itself makes markets more competitive and this decreases the efficacy of anti-competitive practices (which normally require a firm to have a dominant position to begin with). Support for this latter view comes from the considerable empirical evidence that increased international competition reduces price-cost margins (Roberts and Tybout, 1997).[4] Thus, under this view, trade liberalization actually reduces the need for an active competition policy.

A more subtle argument focuses on the effect of trade liberalization, not on firm behavior, but on the regulatory behavior of governments. The concern is that as trade liberalization takes away many of the traditional instruments for trade protection, governments will turn to competition policy as an instrument for giving their firms an advantage over their foreign competitors. Richardson (1999) and Horn and Levinsohn (2001) have examined this proposition for the case of merger policy and found it lacking. While trade liberalization is shown to affect government choices on competition policy, there can be no general presumption that governments will move in a direction that is anti-competitive.

To sum up, there is no good measure of the importance of the types of business practices that give rise to international competition policy conflict. There is also no good reason to suppose that international competition problems are likely to get worse.

But the lack of measurement is itself due to a far deeper problem that plagues efforts to create an international agreement on competition policy, which is that the firm practices at issue are not necessarily anti-competitive. There is a considerable literature on the question of whether vertical restraints are anti-competitive. The answer is highly dependent on the circumstances of the market and the contracting environment (Bernheim and Whinston, 1998). Because of this, competition authorities apply the "rule of reason" (meaning they weigh the facts on a case-by-case basis) instead of banning exclusive contracts outright. The same is true of mergers. Mergers are frequently motivated by potential efficiency gains made possible by consolidated operation. Such efficiency gains may well offset any anti-competitive effects that might come from a more concentrated market. Even the prohibition of parallel imports is not necessarily anti-competitive. While the price discrimination that the prohibition of parallel imports makes possible means higher prices in some markets, it may mean lower prices in other markets. This tailoring of prices often results in greater worldwide sales, even though consumers in the high-price market may not be happy about it.[5]

[4] This is also supported by a preponderance of theoretical work. See the survey by Neven and Seabright (1997).

[5] Malueg and Schwartz (1994) explore the welfare consequences of parallel imports, and find that they may either increase or decrease global welfare.

The difficulty in identifying the anti-competitive effects of many common business practices poses several serious problems for the creation of international competition agreement. First, the identification of anti-competitive effects (as well as remedies for those effects) requires the judgement of a competition authority and, in practice, judgments are often little more than educated guesses. It is simply impossible to write down an international agreement that tells a competition authority how it should rule in every possible contingency that can arise. This means that there will inevitably be disputes in which governments challenge each other's judgements about what constitutes an anti-competitive practice. Many have questioned the wisdom of bringing such complex and subjective issues into the WTO dispute-settlement system, a system that authorizes trade sanctions to be used in the event of an impasse.

Second, although anti-competitive effects may be hard to identify, business practices almost always have redistributive effects that are plainly evident. A vertical restraint that has no negative effect on consumers in the domestic market, for example, may still reduce the market share of foreign firms. In such cases, there is no scope for agreement, as there are no mutual gains from eliminating the practice, but there is plenty of scope for conflict, as each country has an incentive to fight for the market share of its own firms (Bacchetta, Horn, and Mavroidis, 1997). As the previous section documented, these conflicts are driven not by competition authorities interested in protecting consumers interests, but by trade authorities interested typically in pursuing producer interests through export promotion. Many have questioned the wisdom of trying to link together trade and competition policy, given the radically different objectives of trade and competition authorities.

Building on Existing Institutions

The current push to have a WTO competition agreement comes in response to real conflicts that have arisen in the WTO in recent years. However, the previous section suggests that any attempt at a full-blown competition agreement is likely to create more problems than it solves. An awareness of these dangers is probably what accounts for the relatively modest language found in the Doha declaration. That declaration calls for the clarification of the principles of nondiscrimination, transparency and procedural fairness, provisions against hard core cartels, and voluntary cooperation. In essence, it seeks to build on institutions that already exist.

The WTO principle of nondiscrimination (notably most-favored-nation treatment and national treatment) does not impose a uniform international standard for competition policy, but does require that countries avoid applying different standards based on country of origin. In other words, governments would be free to set their merger policies or regulate vertical restraints according to national preferences, so long as they applied them even-handedly. Nondiscrimination is certainly a core principle of the WTO, and it may solve some problems. However, it is not at all clear that this would do anything to solve future vertical restraint cases, such as the Kodak-Fuji dispute. The issue in that dispute was not that the government applied a discriminatory standard but that it was lax in applying its standard, which enabled the domestic firm to discriminate against foreigners. Nondiscrimination, like all WTO principles, applies to governments, not firms. Thus, equality of market access for all firms, regardless of origin, is not guaranteed automatically by a WTO agreement.

The Doha declaration's reference to voluntary cooperation suggests that recent bilateral initiatives on competition policy–most notably the EU and U.S. "positive comity" agreements–will lead the way in any future WTO agreement. In many areas of competition law, especially mergers, the main issue is assertion of jurisdiction. Both the EU and United States rely on the so-called effects doctrine such that a country asserts jurisdiction when it is or likely to be affected by a particular merger, be it an effect on its consumers or its producers, whether at home or abroad. This is an extremely broad use of extraterritorial enforcement of national competition law, which must be contained to avoid conflict. The 1991 "positive comity" agreement between the EU and United States, strengthened in 1998, and extended to numerous other countries thereafter, is an attempt to cooperatively manage extraterritorial enforcement. It establishes various procedures as to timing and information-sharing in antitrust cases, but most notably this bilateral agreement established the idea of positive comity–which is that the initial responsibility for investigating antitrust cases with international effects falls to the jurisdiction where the alleged anticompetitive conduct occurs. (DOJ, 2000).

While the Boeing/McDonnell Douglas merger loomed large as an example of the breakdown of positive comity, critics of a WTO competition agreement point to the vast numbers of international mergers that have occurred without incident as evidence of the success of the current system. However, the important question for the next WTO round is not whether positive comity agreements are problem-free but whether a more ambitious agreement could do any better. This has been the focus of much of the theoretical literature on the subject of international mergers (e.g., Barros and Cabral, 1994; Head and Ries, 1997; and Bond, 1999). Most recently, Neven and Roller (2000) have shown that the current system of overlapping jurisdictions produces almost the same results in merger cases as we might expect from a centralized world competition authority (the ultimate form of international coordination), provided that the centralized authority used the same market definitions and the same market concentration rules as the EU and United States have used traditionally in evaluating merger cases. This does not mean that, under the current decentralized system, countries always agree on which merger should be accepted or rejected. It only means that the mergers rejected by at least one country would also be rejected by a centralized authority, and mergers acceptable to all countries would also be acceptable to a centralized authority. All of this suggests that the current system of decentralization with overlapping jurisdictions is fairly robust and is not likely to be improved upon by a more centralized approach. But there is one important caveat to this result: it is only true if the merger cases are decided on the basis of standard market definition and market concentration rules; if other objectives besides these are inserted into the process (e.g., export promotion), the result breaks down. This suggests that the paramount concern for an international agreement should not be to limit the power of national competition authorities but to *insulate* those competition authorities from possible pressure from trade authorities brought on by trade policy concerns. Whether this can be achieved in a WTO agreement remains to be seen.

Conclusion

The idea of bringing competition policy into the WTO is attractive. Many of the current international frictions over competition policy are directly related to trade, and thus it would appear that they are well within the WTO's domain. Moreover, when it comes to international agreements, few if any institutions have a better system for enforcing compliance and resolving disputes than the WTO. Theoretically, adding competition policy to the WTO may be seen as the inevitable next step in creating a comprehensive and fully integrated regulatory regime for the international flow of goods, services, and factors, thereby realizing the long deferred dream proposed under the 1946-48 negotiations of the Havana Charter for an International Trade Organization.

However, in reality, the current system works surprisingly well. Many of the frictions that do arise are the result of: (a) actions by private firms, over which the WTO has no control; (b) inevitable disagreements about the distribution of gains, which the WTO can do nothing to resolve; or (c) unwarranted intrusions of mercantilist objectives into competition matters, which the WTO would more likely foster than prevent. Thus, it is not at all clear that a WTO regime on competition policy would improve upon the current situation. Alas, it would seem that unless the WTO can muster the foresight and subtlety necessary to tackle an issue as broad and complex as competition policy, the dream of a WTO competition agreement will probably have to be deferred a little longer.

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U.S. Trade Developments

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The U.S. Department of Commerce reported that seasonally adjusted total exports of goods and services of $78.0 billion and imports of $106.5 billion in January 2002 resulted in a goods and services trade deficit of $28.5 billion; this was $3.8 billion more than the $24.7 billion in December 2001.[2] January 2002 imports of goods and services at $106.5 billion were $3.7 billion more than December 2001 imports of 102.8 billion.

January 2002 merchandise exports decreased slightly to $54.8 billion from $55.0 billion in December 2001. Merchandise imports increased to $89.9 billion from $85.9 billion, causing the merchandise trade deficit to increase in January 2002 by $3.1 billion to $34.1 billion from $31.0 billion in December. For services, exports remained essentially constant in January 2002 from the prior month at $23.1 billion, imports of services increased to $17.6 billion from $16.8 billion, resulting in a surplus of $5.6 billion, $0.7 billion lower than $6.3 billion surplus in December. Exports of merchandise goods in the fourth quarter of 2001 reflected decreases in industrial supplies and materials, including petroleum; capital goods, including automotive vehicles, parts, and engines; consumer goods; and the "other goods" statistical category. An increase occurred in exports of foods, feeds, and beverages. Imports of goods reflected foods, feeds, and beverages; industrial supplies and materials, including petroleum; capital goods, including automotive vehicles, parts, and engines; and consumer goods. There were increased imports in the statistical category "other goods" in 2001, fourth quarter. Additional information on U.S. trade developments in agriculture and specified manufacturing sectors are highlighted in tables 1 and 2 and figures 1 and 2. Services trade developments are highlighted in table 3.

[1] The views expressed in this article are those of the author. They are not the views of the U.S. International Trade Commission (USITC) as a whole or of any individual Commissioner.

[2] Data for this article were taken largely from U.S. Department of Commerce, Bureau of Economic Analysis, "U.S. International Trade in Goods and Services," *Commerce News*, FT-900, Mar. 19, 2002, found at *http://www.census.gov/foreign-trade/www/press.html#current*, retrieved Mar. 20, 2002, as well as at Internet address *http://www.bea.doc.gov/bea/newsrel/*.

In January 2002, exports of advanced technology products were $13.5 billion and imports of the same were $14.8 billion, resulting in a deficit of $1.3 billion, following a slight surplus of $0.1 billion in December 2001. The export of goods and services during January-December 2001 was $1,004.6 billion, down from $1,065.7 billion during January-December 2000. Imports of goods and services decreased to $1,352.1 billion, from $1,441.4 billion during the same period. As a consequence, the trade deficit on goods and services decreased to $347.5 billion for the January-December 2001 period, from $375.7 billion during January-December 2000.

The export of goods during January-December 2001 decreased to $720.8 billion from $772.2 billion during the same 2001 period, a decrease of $51.4 billion, and imports of goods were $1,147.1 billion, down from $1,224.4 billion in January-December 2000. Consequently, the merchandise trade deficit declined to $426.3 billion from $452.2 billion. Regarding trade in services, exports in January-December 2001 decreased to $283.8 billion, from $293.5 billion in the same period of 2001, a decrease of $9.7 billion. Imports of services decreased to $205.0 billion from $217.0 billion, a decrease of $12.0 billion.

The January-December 2001 exports of advanced technology products declined to $200.1 billion from $227.4 billion in January-December 2000. Imports declined to $195.3 billion in January-December 2001 from $222.1 billion in the same period of 2000. The trade surplus decreased to $4.8 billion in January-December 2001 down from $5.3 billion in January-December 2000.

Trade data for goods and services showed trade deficits in January 2002 with Canada, Mexico, Western Europe, the Euro area (EU-12), the European Union (EU-15), EFTA, Eastern Europe, China, Japan, Korea, Taiwan, Latin America, and the OPEC countries. Trade surpluses were recorded with Belgium, the Netherlands, Spain, Australia, Hong Kong, Singapore, and Egypt. U.S. trade developments with major trading partners are highlighted in table 4.

Table 1
U.S. trade in goods and services, seasonally adjusted, Dec. 2001-Jan. 2002

(Billion dollars)

Item	Exports Jan. 2002	Exports Dec. 2001	Imports Jan. 2002	Imports Dec. 2001	Trade balance Jan. 2002	Trade balance Dec. 2001
Trade in goods[1] (see note)						
Including oil	54.836	54.954	88.916	85.937	-34.080	-30.983
Excluding oil	54.742	54.791	82.226	79.934	-27.484	-25.143
Trade in services[1]	23.132	23.089	17.570	16.819	5.562	6.270
Trade in goods and services[1] . .	77.968	78.043	106.486	102.756	-28.518	-24.713
Trade in goods[2]	61.241	61.620	101.598	97.507	-40.357	-35.887
Advanced technology products[3]	13.491	15.160	14.805	15.038	-1.314	0.122

[1] Current dollars, presented on a balance-of-payments basis.
[2] Constant 1996 dollars, presented on a Census Bureau basis.
[3] Not seasonally adjusted.

Note.—Data on trade in goods in current dollars are presented on a balance-of-payments (BOP) basis that reflects adjustments for timing, coverage, and valuation of data compiled by the Census Bureau. The major adjustments on a BOP basis exclude military trade, but include nonmonetary gold transactions and estimates of inland freight in Canada and Mexico that are not included in the Census Bureau data. Data may not add to totals due to rounding.

Source: Calculated from official data of the U.S. Department of Commerce, Exhibits 1, 9, 10, and 16, FT-900 release of Mar. 19, 2002, found at Internet address *http://www.census.gov/foreign-trade/www/press.html#current.*

Table 2
Nominal U.S. exports, imports, and trade balances, agriculture and specified manufacturing sectors, Jan. 2001-Jan. 2002

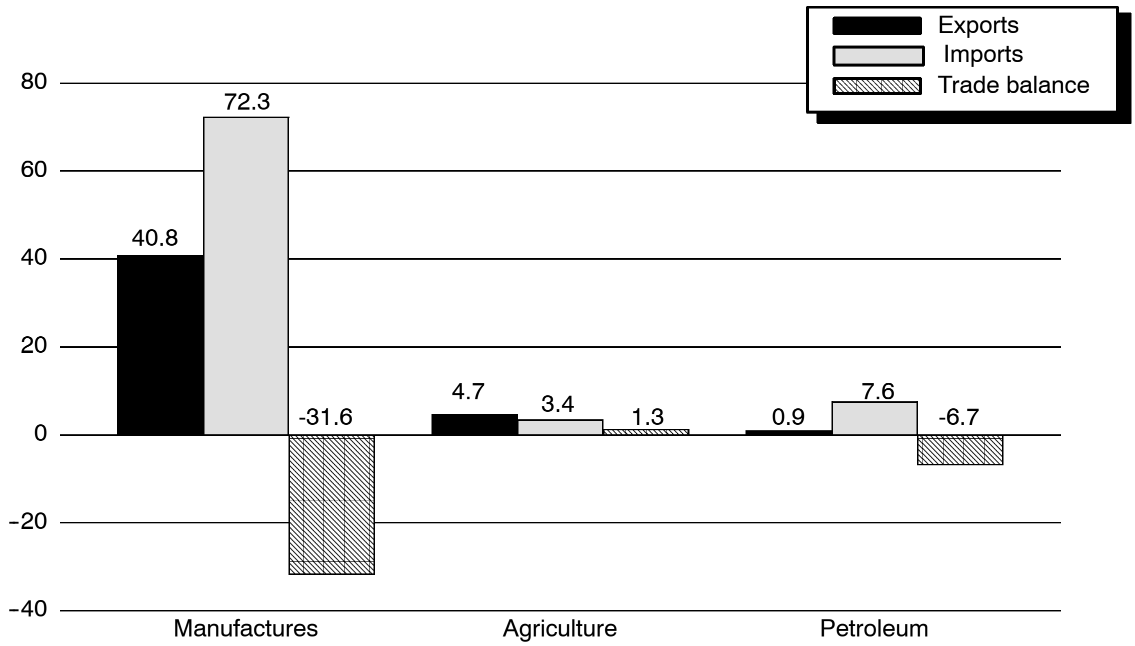
Manufacture sector	Exports		Imports		Trade balance		Change in exports, Jan. 2002 over Jan. 2001	Change in imports, Jan. 2002 over Jan. 2001	Share of total exports, Jan. 2002
	Jan. 2002	Jan. 2001	Jan. 2002	Jan. 2001	Jan. 2002	Jan. 2001			
	(Billion dollars)						*(Percent)*		
ADP equip. & office machinery	2.353	3.729	6.020	6.582	-3.667	-2.853	-36.9	-8.5	4.5
Airplane parts	1.074	1.354	0.428	0.557	0.646	0.797	-20.7	-23.2	2.1
Airplanes	1.747	1.392	1.492	1.033	0.255	0.359	25.5	44.4	3.4
Chemicals - inorganic	0.442	0.429	0.508	0.664	-0.066	-0.235	3.0	-23.5	0.9
Chemicals - organic	1.189	1.508	2.413	3.004	-1.224	-1.496	-21.2	-19.7	2.3
Electrical machinery	5.289	7.332	5.785	8.536	-0.496	-1.204	-27.9	-32.2	10.2
General industrial machinery	2.313	2.752	2.606	2.921	-0.293	-0.169	-16.0	-10.8	4.5
Iron & steel mill products	0.423	0.493	1.062	1.056	-0.639	-0.563	-14.2	0.6	0.8
Power-generating machinery	2.540	2.693	2.767	2.858	-0.227	-0.165	-5.7	-3.2	4.9
Scientific instruments	1.995	2.563	1.527	1.790	0.468	0.773	-22.2	-14.7	3.8
Specialized industrial machinery	1.711	2.733	1.370	1.893	0.341	0.840	-37.4	-27.6	3.3
Televisions, VCRs, etc.	1.584	2.107	4.156	5.270	-2.572	-3.163	-24.8	-21.1	3.1
Textile yarn and fabric	0.742	0.822	1.235	1.300	-0.493	-0.478	-9.7	-5.0	1.4
Vehicles	3.761	3.832	11.496	12.481	-7.735	-8.649	-1.9	-7.9	7.3
Other manufactures exports[1]	13.619	15.750	29.480	32.240	-15.861	-16.490	-13.5	-8.6	26.3
Manufactures	40.782	49.489	72.345	82.185	-31.563	-32.696	-17.6	-12.0	78.7
Agriculture	4.686	4.373	3.358	3.412	1.328	0.961	7.2	-1.6	9.0
Other exports[1]	6.357	7.636	9.955	16.087	-3.598	-8.451	-16.8	-38.1	12.3
Total exports of goods	51.825	61.498	85.658	101.684	-33.833	-40.186	-15.7	-15.8	100.0

[1] Not included above.

Note.—Data may not add due to rounding. Data are presented on a Census Bureau basis.

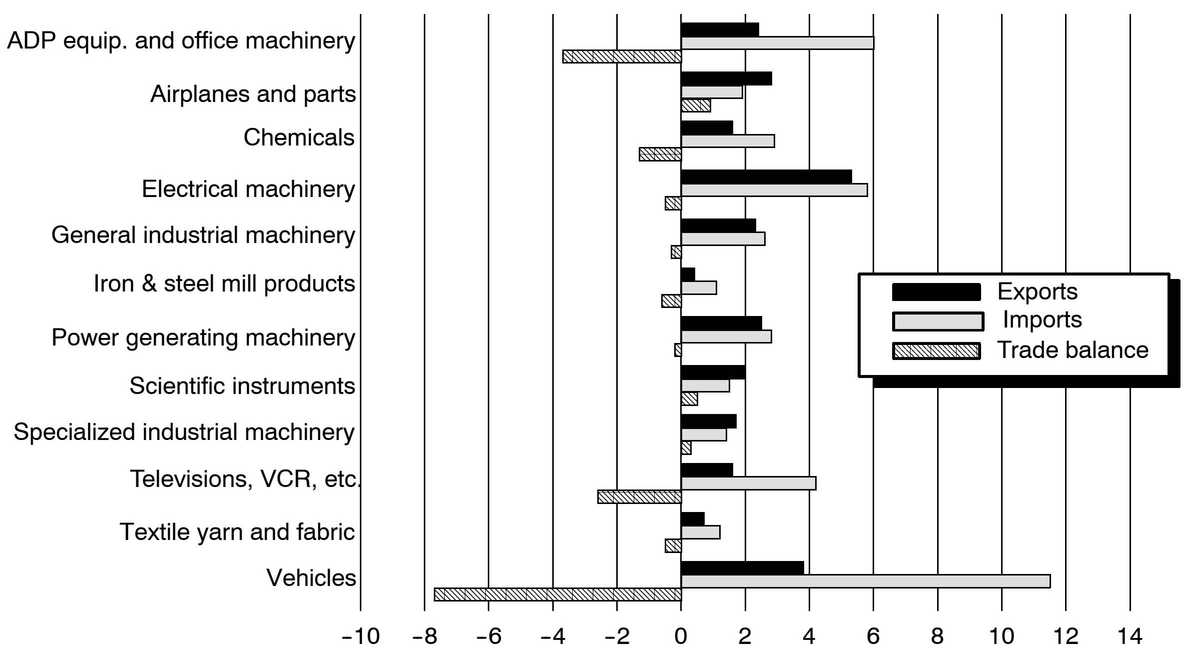
Source: Calculated from official data of the U.S. Department of Commerce, Exhibit 15, FT-900 release of Mar. 19, 2002, found at Internet address *http://www.census.gov/foreign-trade/www/press.html#current*.

Figure 1
U.S. trade by major commodity, billion dollars, Jan. 2002



Source: Calculated from official data of the U.S. Department of Commerce, FT-900 release of Mar. 19, 2002.

Figure 2
U.S. trade in principal goods, billion dollars, Jan. 2002



Source: Calculated from official data of the U.S. Department of Commerce, FT-900 release of Mar. 19, 2002.

Table 3

Nominal U.S. exports and trade balances of services, by sectors, Jan. 2000-Dec. 2001, seasonally adjusted

Service sector	Exports		Imports		Trade balance		Change in exports Jan.-Dec. 2001 over Jan.-Dec. 2000	Change in imports Jan.-Dec. 2001 over Jan.-Dec. 2000
	Jan.-Dec. 2001	Jan.-Dec. 2000	Jan.-Dec. 2001	Jan.-Dec. 2000	Jan.-Dec. 2001	Jan.-Dec. 2000		
	(Billion dollars)						*(Percent)*	
Travel	72.295	82.042	58.921	64.537	13.374	17.505	-11.9	-8.7
Passenger fares	17.734	20.745	23.407	24.197	-5.673	-3.452	-14.5	-3.3
Other transportation services	28.292	30.185	38.230	41.058	-9.938	-10.873	-6.3	-6.9
Royalties and license fees	38.875	38.030	16.399	16.106	22.476	21.924	2.2	1.8
Other private sales	112.892	107.568	50.289	54.687	62.603	52.881	4.9	-8.0
Transfers under U.S. military sales contracts	12.813	14.060	14.775	13.560	-1.962	0.500	-8.9	9.0
U.S. Government misc. services	0.857	0.862	2.932	2.879	-2.075	-2.017	-0.6	1.8
Total exports of services	283.758	293.492	204.953	217.024	78.805	76.468	-3.3	-5.6

Note.—Data on trade in services are presented on a balance-of-payments basis. Data may not add to totals due to rounding and seasonal adjustments.

Source: Compiled from official data of the U.S. Department of Commerce, Exhibits 3 and 4, FT-900 release of Mar. 19, 2002, found at Internet address *http://www.census.gov/foreign-trade/www/press.html#current*.

Table 4
U.S. exports and imports of goods with major trading partners, Jan. 2001-Jan. 2002

Country/areas	Exports Jan. 2002	Exports Jan. 2001	Imports Jan. 2002	Imports Jan. 2001	Trade balance Jan. 2002	Trade balance Jan. 2001	Change in exports, Jan. 2002-Jan. 2001	Change in imports, Jan. 2002-Jan. 2001
	(Billion dollars)						*(Percent)*	
Total	52.458	62.340	85.421	101.106	-32.963	-38.766	-15.9	-15.5
North America	19.753	22.310	26.457	30.288	-6.704	-7.978	-11.5	-12.6
Canada	12.033	13.658	16.467	19.534	-4.434	-5.876	-11.9	-15.7
Mexico	7.720	8.651	9.991	10.753	-2.271	-2.102	-10.8	-7.1
Western Europe	12.331	15.157	17.310	20.777	-4.979	-5.620	-18.6	-16.7
Euro Area	8.288	9.995	12.179	14.204	-3.891	-4.209	-17.1	-14.3
European Union (EU-15)	11.436	13.841	16.065	19.044	-4.629	-5.203	-17.4	-15.6
France	1.551	1.643	2.428	2.548	-0.877	-0.905	-5.6	-4.7
Germany	2.023	2.601	4.005	4.898	-1.982	-2.297	-22.2	-18.2
Italy	0.729	0.923	1.787	2.102	-1.058	-1.179	-21.0	-15.0
Netherlands	1.471	1.821	0.685	0.833	0.786	0.988	-19.2	-17.8
United Kingdom	2.755	3.402	3.057	3.883	-0.302	-0.481	-19.0	-21.3
Other EU	0.930	1.122	1.934	2.025	-1.004	-0.903	-17.1	-4.5
EFTA[1]	0.603	1.052	0.948	1.341	-0.345	-0.289	-42.7	-29.3
Eastern Europe/FSR[2]	0.432	0.619	0.784	1.370	-0.352	-0.751	-30.2	-42.8
Russia	0.185	0.198	0.312	0.694	-0.127	-0.496	-6.6	-55.0
Pacific Rim Countries	13.216	15.808	28.594	33.435	-15.378	-17.627	-16.4	-14.5
Australia	0.945	0.863	0.534	0.542	0.411	0.321	9.5	-1.5
China	1.566	1.188	8.423	8.419	-6.857	-7.231	31.8	0.0
Japan	3.918	5.272	8.670	11.144	-4.752	-5.872	-25.7	-22.2
NICs[3]	5.186	6.461	7.295	9.051	-2.109	-2.590	-19.7	-19.4
Latin America	3.835	4.751	4.917	6.571	-1.082	-1.820	-19.3	-25.2
Argentina	0.110	0.392	0.267	0.278	-0.157	0.114	-71.9	-4.0
Brazil	1.010	1.280	1.097	1.318	-0.087	-0.038	-21.1	-16.8
OPEC	1.234	1.608	3.797	5.819	-2.563	-4.211	-23.3	-34.7
Other Countries	2.182	2.725	5.265	5.642	-3.083	-2.917	-19.9	-6.7
Egypt	0.157	0.184	0.068	0.073	0.089	0.111	-14.7	-6.8
South Africa	0.159	0.237	0.377	0.475	-0.218	-0.238	-32.9	-20.6
Other	1.866	2.304	4.820	5.093	-2.954	-2.789	-19.0	-5.4

[1] The European Free Trade Area (EFTA) includes Iceland, Liechtenstein, Norway, and Switzerland.
[2] FSR = Former Soviet Republics.
[3] The newly industrializing countries (NICs) include Hong Kong, Republic of Korea, Singapore, and Taiwan.

Note.—Country/area figures may not add to totals due to rounding. Exports of certain grains, oilseeds, and satellites are excluded from country/area exports but included in total export table. Also, some countries are included in more than one area. Data are presented on a Census Bureau basis.

Source: Calculated from official data of the U.S. Department of Commerce, Exhibits14 and 14a, FT-900 release of Mar. 19, 2002, found at Internet address *http://www.census.gov/foreign-trade/www/press.html#current.*

International Economic Comparisons

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U.S. Economic Performance Relative to Other Group of Seven (G-7) Members

Economic Growth

The real gross domestic product (GDP) of the United States–the output of goods and services produced in the United States measured in 1996 prices–increased at an annual rate of 1.7 percent in the fourth quarter of 2001. In the third quarter, real GDP decreased at an annual rate of 1.3 percent, according to estimates by the U.S. Bureau of Economic Analysis.[2] For the year 2000, real GDP grew by 4.1 percent and for the year 2001 GDP increased by 1.2 percent.

The annualized rate of real GDP growth in the first quarter of 2002 was 2.0 percent in Canada, -0.6 percent in France, -1.0 percent in Germany, -0.9 percent in Italy, -2.1 percent in Japan, and 0.1 percent in the United Kingdom. The annualized rate of real GDP growth in the first quarter of 2002 was 0.4 percent for EU members linked by the Euro currency, the Euro area (EU-12).

Industrial Production

The Federal Reserve Board reported that U.S. industrial production rose 0.7 percent in March 2002 for a third consecutive monthly increase. Output in March 2002 was 2.9 percent below its level in March 2001. Utilities production increased by 1.6 percent, whereas the output of mines fell by 1.6 percent. The rate of capacity utilization for total industry rose 0.5 percent in March 2002, to 75.4 percent of its 1992 index base of 100, a level still below its 1967-2001 average of 81.9 percent. Due to weak investment, capacity growth expanded only 1.1 percent in the 12 months to February 2002.

By market groups, the output of consumer goods rose 0.6 percent in March, with widespread gains in both durable and nondurable manufacturing. The production of both durable and nondurable materials continued strong, advancing 0.9 percent in March 2002. The production of business equipment rose slightly in March by 0.1 percent. Gains in the output of information processing equipment and in other industrial equipment were largely offset by a 3.2 percent drop in the manufacturing output of transit equipment, notably reflecting continued curtailment of commercial aircraft production. The production of defense and space equipment climbed 1.1 percent.

Other G-7 member countries reported the following growth rates of industrial production for the year that ended in December 2001: Canada reported a decrease of 5.5 percent; France, a decrease of 1.7 percent; Germany, a decrease of 5.1 percent; Italy, a decrease of 4.1 percent; and the United Kingdom reported a decrease of 4.6 percent. For the year ended January 2002, Japan reported a decrease of 11.1 percent. The Euro area reported a decrease of 4.1 percent for the year that ended in December 2001.

Prices

The seasonally adjusted U.S. Consumer Price Index (CPI) rose 0.3 percent in March 2002, following increases of 0.2 percent in both January and February 2002, according to the U.S. Department of Labor. For the year ending in the first quarter of 2002, consumer prices increased at an annual rate of 3.0 percent.

During the 1-year period that ended in January 2002, prices increased by 1.3 percent in Canada, 2.2

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[2] Data for this article were taken largely from the following sources: U.S. Department of Commerce, Bureau of Economic Analysis, "Gross Domestic Product," *BEA News Release*, found at Internet address *http://www.bea.doc.gov/bea/newsrel/gdp401f.htm*; Federal Reserve Board, "Industrial Production and Capacity Utilization," G.17 (419) Release, found at Internet address *http://www.federalreserve.gov/releases/G17/Current/*; U.S. Department of Labor, Bureau of Labor Statistics, "Consumer Price Index," *USDL-01*, found at Internet address *http://www.bls.gov/news.release/cpi.nr0.htm*; U.S. Department of Labor, Bureau of Labor Statistics, "The Employment Situation," *USDL-01*, found at Internet address *http://www.bls.gov/news.release/empsit.nr0.htm*; and the Conference Board, Consumer Research Center, "Forecasters' Forecasts," facsimile transmission, used with permission.

percent in France, and 1.3 percent in the United Kingdom; prices decreased by 1.4 percent in Japan. In the year to February 2002, prices increased by 2.4 percent in Germany, and by 2.5 percent in Italy. Prices increased by 2.7 percent in the Euro area in the year that ended in January 2002.

Employment

The Bureau of Labor Statistics reported that the total U.S. unemployment rate was little changed at 5.7 percent in March 2002. Non-farm payroll employment was also little changed in March, up by 58,000 to 131.3 million, contrasting with an average monthly loss of 144,000 during the 12 months to February 2002. Manufacturing employment continued to decline, although at a much slower rate.

In other G-7 countries, the latest unemployment rates were reported to be: 7.9 percent in Canada, 9.0 percent in France, 9.6 percent in Germany, 9.3 percent in Italy, 5.3 percent in Japan, and 5.2 percent in the United Kingdom. The unemployment rate in the Euro area was 8.4 percent.

Forecasts

The events of 2001 brought new challenges for the U.S. economy and for economic policy. The Council of Economic Advisers projects real GDP to pick up early in 2002. The economy continues to display characteristics favorable to long term growth; productivity growth remains strong, and inflation remains low and stable. The pace is expected to be slow initially, followed by an acceleration thereafter; over the four quarters of 2002 real GDP is expected to grow by 2.7 percent. The unemployment rate is projected to continue rising through the middle of 2002 when it is expected to peak around 6 percent.

In addition, economic prospects improved despite the September 11 terrorist attacks, with raising private forecasters their economic growth projections. Seven major U.S. forecasters expect real GDP growth in the United States during the first quarter of 2002 to reach an average annualized rate of 2.2 percent, but to increase in the second to 3.4 percent, 3.9 percent in the third and 3.7 percent in the fourth. The overall growth rate for the year 2002 is expected to average about 1.9 percent. In the first quarter of 2003, GDP is projected to grow at 3.9 percent. Table 1 shows macroeconomic projections for the U.S. economy from January to December 2002, and the first quarter of 2003, and the simple average of these forecasts. Forecasts of all the economic indicators, except unemployment, are presented as percentage changes from the preceding quarter, on an annualized basis. The forecasts of the unemployment rate are averages for the quarter.

The average of the forecasts points to an unemployment rate of 5.8 percent in the first quarter of 2002, and to the likelihood of remaining around this rate for the rest of the year. For the first quarter of 2003, the unemployment rate is projected to continue essentially unchanged around 5.7 to 5.8 percent. Inflation, as measured by the GDP deflator, is expected to remain subdued, reaching an average of about 1.7 percent in the first two quarters of 2002, and then declining slightly in the third and fourth quarters of 2002 to 1.5 to 1.6 percent, before returning in the first quarter of 2003 to around 1.8 percent. For the whole year inflation is projected to recede to 1.3 percent. (See table 1).

Table 1
Projected changes of selected U.S. economic indicators, by quarters, Jan. 2002-Mar. 2003

(Percent)

	Conference Board	Macro-economic Advisers	E.I. Dupont	UCLA	Northern Trust Co.	Merrill Lynch Capital Markets	Eaton Corp.	Mean of forecasts
GDP, constant dollars								
2002								
Jan.-Mar.	2.6	2.4	3.0	-0.6	1.0	3.5	3.2	2.2
Apr.-June	2.1	3.4	4.0	2.5	3.6	3.5	4.4	3.4
July-Sept.	2.4	3.4	4.0	3.2	3.9	5.0	5.1	3.9
Oct.-Dec.	3.1	3.2	3.5	3.5	3.3	5.0	4.5	3.7
Annual 2002	1.6	1.7	2.3	1.0	1.5	2.6	2.7	1.9
2003								
Jan.-Mar.	4.2	3.8	3.0	3.7		4.2	4.6	3.9
GDP price deflator								
2002								
Jan.-Mar.	2.1	1.7	0.7	2.6	2.1	0.8	1.9	1.7
Apr.-June	2.2	1.5	1.5	2.4	2.3	0.9	1.3	1.7
July-Sept.	0.9	1.4	1.5	2.5	2.5	1.1	0.7	1.5
Oct.-Dec.	1.4	1.7	1.5	2.2	2.5	0.8	1.1	1.6
Annual 2002	1.5	1.3	1.1	1.1	1.8	0.9	1.2	1.3
2003								
Jan.-Mar.	1.8	2.2	1.8	2.3		1.2	1.4	1.8
Unemployment, average rate								
2002								
Jan.-Mar.	5.7	5.8	5.6	5.8	5.8	5.8	5.8	5.8
Apr.-June	6.0	5.8	5.6	6.0	5.9	6.1	5.8	5.9
July-Sept.	6.2	5.7	5.5	5.9	5.8	6.2	5.7	5.9
Oct.-Dec.	6.3	5.7	5.4	5.9	5.7	6.0	5.6	5.8
Annual 2002	6.0	5.7	5.5	5.9	5.8	6.0	5.7	5.8
2003								
Jan.-Mar.	6.3	5.6	5.3	5.8		5.9	5.3	5.7

Note.—Except for the unemployment rate, changes in the forecast represent annualized percentage rates of change from the preceding period. Quarterly data are seasonally adjusted.

Source: Calculated from data from the Conference Board. Used with permission. Forecast date, Feb. 2002.

U.S. Productivity and Costs: Preliminary Fourth-Quarter and Annual Averages for 2001

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Improvements in productivity growth matter most in sustaining and improving long-term economic growth. Productivity growth in the United States accelerated during the second half of the 1990s, and most economists believe that much of that productivity growth resulted from improved ways of doing things and the destruction of old or obsolete methods. Economists expect that productivity growth will remain the propeller of long-term economic growth and help maintain muted rates of inflation.

The Bureau of Labor Statistics of the U.S. Department of Labor reported preliminary productivity data–measured as output per hour of all persons–for the fourth quarter and for the full year 2001. It also provided annual data for the period extending from 1992 to 2001.[2]

Productivity gains in the fourth quarter of 2001 were measured in the business sector as increasing by 3.4 percent and in the non-farm business sector by 3.5 percent, at seasonally adjusted annual rates. Productivity measures gained 1.8 percent on average in calendar 2001, over 2000, in both sectors. Productivity advanced 3.4 percent in the business sector as output declined 0.3 percent and hours worked fell 3.6 percent, at seasonally adjusted annual rates. In the non-farm business sector, productivity rose 3.5 percent, as output decreased 0.4 percent and hours dropped 3.7 percent. On an average annual basis, productivity in both the business and non-farm business rose 1.8 percent in 2001 over 2000, the smallest increase since 1995 when output per hour increased 0.7 and 0.9 percent in the business and non-farm business sectors, respectively. Fourth quarter productivity and related measures are summarized in table 1.

In the manufacturing sector, increases in productivity in the fourth quarter were: 3.5 percent in the manufacturing sector, 2.3 percent in durable goods manufacturing, and 4.3 percent in non-durable goods manufacturing. On an annual basis, productivity gains in 2001 averaged 1.0 percent in the manufacturing sector, 0.5 percent in durable goods manufacturing, and 1.5 percent in nondurable goods manufacturing.

It is worth noting, however, that the data sources and methods used in the preparation of the manufacturing series differ from those used in preparing the business and non-farm business series, and these measures are not directly comparable. Output measures for business and non-farm business are based on measures of gross domestic product prepared by the Bureau of Economic Analysis of the U.S. Department of Commerce. Quarterly output measures for manufacturing reflect indexes of industrial production independently prepared by the Board of Governors of the Federal Reserve Board.

[1] The views expressed in this article are those of the author. They are not the views of the U.S. International Trade Commission (USITC) as a whole or of any individual Commissioner.

[2] Data for this article were taken largely from U.S. Department of Labor, Bureau of Labor Statistics, "Productivity and Costs," *USDL 02-64*, found at Internet address *http://www.bls.gov/news.release/prod2.nr0.htm*, retrieved on Mar. 21, 2002.

Table 1
Productivity and costs: Preliminary fourth quarter 2001 measures, at seasonally adjusted annual rates

Sector	Productivity	Output	Hours	Hourly compen-sation	Real hourly compen-sation	Unit labor costs
	(Percentage change, from preceding quarter)					
Business	3.4	-0.3	-3.6	2.3	2.7	-1.1
Nonfarm business . . .	3.5	-0.4	-3.7	2.3	2.8	-1.1
Manufacturing	3.5	-7.2	-10.4	2.6	3.0	-0.9
Durable	2.3	-10.3	-12.3	3.6	4.0	1.3
Nondurable	4.3	-3.3	-7.3	1.4	1.8	-2.8
	(Percentage change, from same quarter a year ago)					
Business	1.5	-0.5	-2.0	4.0	2.1	2.4
Nonfarm business . . .	1.6	-0.5	-2.1	3.9	2.0	2.2
Manufacturing	0.7	-6.4	-7.0	4.5	2.6	3.8
Durable	0.0	-8.5	-8.5	5.1	3.2	5.1
Nondurable	1.1	-3.6	-4.7	3.9	2.1	2.8

Source: Compiled from official statistics of the Bureau of Labor Statistics, U.S. Department of Labor, found at Internet address *http://www.bls.gov/news.release/prod2.toc.htm*, retrieved on Mar. 21, 2002.

STATISTICAL TABLES

Table 1
Unemployment rates in G-7 countries, by specified periods, 1999-Jan. 2002[1]

(Percent)

	1999				2000						2001	2002
Country		**Q:I**	**Q:II**	**Q:III**	**Q:IV**	**Q:I**	**Q:II**	**Q:III**	**Oct.**	**Nov.**	**Dec.**	**Jan.**
United States	4.2	4.0	4.0	4.1	4.0	4.2	4.5	4.8	5.4	5.6	5.8	5.6
Canada	7.0	6.1	6.1	6.1	6.1	6.2	6.3	6.4	6.5	6.7	7.2	7.3
Japan	4.7	4.8	4.7	4.7	4.8	4.8	4.9	5.2	5.4	5.5	5.5	5.3
France	11.2	9.9	9.4	9.3	9.0	8.6	8.5	8.7	8.8	8.9	8.9	9.0
Germany	8.6	8.3	8.1	8.0	7.8	7.9	8.0	8.0	8.1	8.2	8.2	8.2
Italy	11.5	11.2	10.9	10.5	10.1	10.0	9.7	9.5	9.3			
United Kingdom	6.1	5.8	5.5	5.4	5.3	5.1	5.0	5.1	5.1	5.2		

[1] Rates presented on a civilian labor force basis, seasonally adjusted. Rates for foreign countries adjusted to be comparable to the U.S. rate.

Source: U.S. Department of Labor, Bureau of Labor Statistics, "Unemployment Rates in Nine Countries, Civilian Labor Force Basis, Approximating U.S. Concepts, Seasonally Adjusted, 1990-2001," release of Mar. 8, 2002, found at Internet address *ftp://ftp.bls.gov/pub/special.requests/ForeignLabor/flsjec.txt.*

Table 2
Consumer prices of G-7 countries, by specified periods, 1999-Jan. 2002

(Percent, change from same period of previous year)

	1999				2000						2001	2002
Country		**Q:I**	**Q:II**	**Q:III**	**Q:IV**	**Q:I**	**Q:II**	**Q:III**	**Oct.**	**Nov.**	**Dec.**	**Jan.**
United States	2.2	3.2	3.3	3.5	3.4	3.4	3.4	2.7	2.1	1.9	1.6	1.1
Canada	1.7	2.7	2.4	2.7	3.1	2.8	3.6	2.7	1.9	0.7	0.7	1.3
Japan	-0.3	-0.7	-0.7	-0.7	-0.5	-0.4	-0.7	-0.8	-0.8	-1.0	-1.2	-1.4
France	0.5	1.5	1.5	1.9	1.9	1.3	2.0	1.8	1.8	1.2	1.4	2.2
Germany	0.6	1.8	1.6	2.1	2.3	2.5	3.2	2.5	2.0	1.7	1.7	2.1
Italy	1.7	2.4	2.5	2.6	2.7	2.9	3.1	2.8	2.5	2.4	2.4	2.4
United Kingdom	1.5	2.3	3.1	3.2	3.1	2.5	1.9	1.8	1.6	0.9	0.7	1.3

Source: U.S. Department of Labor, Bureau of Labor Statistics, "Consumer Prices in Nine Countries, Percent Change from Same Period of Previous Year, 1990-2001," release of Mar. 8, 2002, found at Internet address *ftp://ftp.bls.gov/pub/special.requests/ForeignLabor/flscpim.txt.*

Table 3
U.S. trade balances by major commodity categories and by specified periods, Jan. 2001-Jan. 2002[1]

(Billion dollars)

Commodity categories	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	2001 Dec.	2002 Jan.
Manufactures	-32.696	-25.220	-30.321	-29.452	-27.396	-28.402	-35.026	-33.165	-31.535	-38.591	-32.870	-26.797	-31.563
Agriculture	0.961	1.452	1.422	0.897	0.790	0.848	0.692	1.257	0.825	1.746	1.855	1.512	1.328
Petroleum[2]	-12.099	-9.738	-9.844	-10.605	-10.900	-9.957	-9.718	-8.978	-8.233	-8.040	-6.442	-5.768	-6.712
Dollar unit price of U.S. petroleum imports[2]	23.13	23.76	22.76	21.65	22.62	23.09	22.34	22.15	22.99	19.94	17.13	15.51	16.31

[1] Exports, f.a.s. value, not seasonally adjusted. Imports, customs value, not seasonally adjusted.

[2] Petroleum and selected products, not seasonally adjusted.

Source: Calculated from official data of the U.S. Department of Commerce, Exhibits 15 and 17, FT-900 release of Mar. 19, 2002, found at Internet address *http://www.census.gov/foreign-trade/www/press.html#current*.