



Cordell Hull Institute

# Trade Policy Analyses

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As part of its project on the Role of the WTO in the World Economy, supported by the Netherlands Ministry of Foreign Affairs and the Berger International Legal Studies Program at Cornell University, the Cordell Hull Institute held a one-day meeting in Washington, DC, on October 20, 2004, on Developing Countries in the WTO System.

The meeting was at Hogan & Hartson, attorneys-at-law, in its Washington office in the Columbia Square Building (pictured above), designed by I.M. Pei.



Attached are the remarks of **Douglas Oberhelman** (above) providing a business perspective.

#### About the Author

Douglas R. Oberhelman is

#### PAUSE FOR REFLECTION...

## On the Direction of U.S. Trade Policy – a Caterpillar View

Douglas Oberhelman

BY WORKING together, the U.S. Administration and Congress can move forward, I believe, with bilateral free trade agreements without necessarily compromising the Doha Round negotiations in the World Trade Organization and efforts to achieve a Free Trade Area of the Americas. At the end of the day, though, success will be measured not by what is done bilaterally, but by what the United States and others do multilaterally. What governments do together, through multilateral cooperation, will strengthen the connection between free markets, international harmony and, ultimately, world stability, peace and prosperity.

Before getting into a discussion of free trade from an international corporate perspective, let me lay out some background on Caterpillar, which will help explain why trade-policy issues are so important to our business. Caterpillar firmly believes that open markets are in the best long-term interests of its customers, business and the global economy. In fact, Caterpillar has advocated access to markets since the 1950s, as conveyed in its annual reports from that time onwards, and we plan to continue advocating free trade in the future. It is vitally important to Caterpillar and other U.S.-based international companies that we maintain an open trade and investment environment.

#### Summary of Caterpillar's Business

Caterpillar is the world's largest manufacturer of construction and mining equipment, diesel and natural gas engines and industrial gas turbines. In 2004 the business was 79 years old, celebrated its 75th anniversary on the New York Stock Exchange and marked the 100th anniversary of its signature product, the track-type tractor.

Caterpillar is a Fortune 100 company and a member of the Dow 30 with projected sales and revenues in 2005 of more than \$30

the Group President of Caterpillar Inc., Peoria, for worldwide manufacturing, marketing and sales of the group's diesel power system business and for the corporate financial and legal divisions.

He is also a director of the Ameron Corporation, the South Side Bank and the National Association of Manufacturers.

### Other Speakers

The meeting was attended by 55 trade-policy and law specialists, mostly from the Washington, DC, area.

Besides Mr Oberhelman, the other speakers were: **Hugh Corbet**, president of the Cordell Hull Institute; **Carlos Primo Braga**, **Richard Newfarmer** and **Alan Winters**, economic advisers at the World Bank; and **John Barcelo**, of the Cornell Law School.

The meeting was chaired by **Clayton Yeutter**, of Hogan & Hartson, and **Harald Malmgren**, of Malmgren O'Donnell, financial advisers, London and Washington, DC.

### About the Meeting

In August 2004, after the WTO General Council's "July package" of framework agreements – without detailed negotiating plans – on agriculture and non-agricultural market access, the prospects for the Doha Round negotiations began to look better.

It looked as if the next problem to be overcome in the negotiations would be the development dimension, for there are serious divisions over special-and-differential treatment, with the many of developing-country proposals on the

billion. Its products range from the small skid steer loader to the 797 truck – the largest mining truck in the world. And it is not just a product company either – services businesses like Cat Financial, Cat Logistics, Cat Remanufacturing Services and OEM Solutions contribute significantly toward the group's bottom line.

Caterpillar's headquarters are in Peoria, Illinois, but it operates nearly 300 other facilities in twenty countries on six continents. Just half of its 74,000 employees are located in the United States. Its 200-plus independent Cat dealers employ more than 90,000 and operate 3,000 branch and rental stores worldwide – and that doesn't include the 400 distributors of FG Wilson, MaK, Perkins and Solar products, all subsidiaries of Caterpillar. Collectively, these dealers give our multinational enterprise a local presence in virtually every corner of the world.

All told, the group offers more than 300 different products sold in 200 countries. We are, indeed, a global enterprise – and not just in terms of people and locations. Caterpillar has consistently been one of the United States' top ten exporters. In 2003 it exported \$5.8 billion worth of product.

About half of the products made in the United States are exported to countries around the world. And most of its manufacturing operations are globally integrated – in that they import *and* export materials, components and products.

This worldwide reach came about in large part because of the need to manage around foreign trade barriers. To put it simply, selling to a given country often required establishing a manufacturing presence there.

But even with the group's investments in place and market position assured, Caterpillar continues to support the elimination of tariffs and other import barriers. It competes best in a free trade environment. When trade barriers are removed, we can meet our customers' needs more efficiently and grow more easily. Free trade also promotes economic growth, higher standards of living and better human understanding – and thus a more peaceful world – ideals we can all be proud of promoting.

In the United States today, exports account for approximately 12 percent of the gross domestic product; and they account for one of every seven jobs. Developing countries are America's fastest-growing export markets and they will soon account for 40 percent of world trade.

That's why it is so important to further open the U.S. market to products made in the developing countries. It's important not only for U.S. business success but also for the success of people and nations around the world. By trading and investing in the world community, we help improve the quality of life for those in

subject bearing on agricultural trade.

On the one hand, the developing countries are pressing for special-and-differential treatment through (i) preferential access to markets, (ii) relief from reciprocating fully in market-access negotiations, (iii) deferrals or exemptions from some WTO rules and (iv) technical assistance in implementing new WTO agreements. Some of the countries are bent on preserving "policy space" for the future and a number of others worry about "preference erosion" with the prospect of MFN tariffs being further reduced or eliminated.

On the other hand, those familiar with the system point out that the WTO is not a development agency, but a framework of contractual agreements, setting out internationally agreed rules that promote transparency, predictability and stability – important to businesses in conducting international trade and planning [trade-related] investments.

But the trouble, some say, is that WTO rules are often asymmetrical, reflecting conditions in industrialized countries, as with those on subsidies, anti-dumping actions and intellectual property rights.

The most intractable Doha Round issues, namely liberalizing agricultural trade and trade in labor-intensive manufactures, essentially arise out of discrimination by country and by product.

Recent studies at the World Bank show that generalized tariff preferences, in place since the early 1970s, have not significantly benefited developing economies and

developing countries, while continuing to raise standards of living in the United States.

## Experience with Trade Liberalization

Today much public discussion centers on the merits of negotiating *new* "free trade agreements", bilateral and regional, while also trying to put the Doha Round negotiations into high gear. Free trade agreements are widely criticized for falling short of free trade among the parties to them, for being preferential trade arrangements, for not satisfying the requirements in WTO rules for departures from the principle of non-discrimination to form free trade areas or customs unions.

The arguments have been drawn together in the papers by Alan Winters and Richard Newfarmer for the Institute's project on developing countries in the WTO system. I have no quarrel with the criticisms that need to be addressed by governments. But businesses have to deal with the world as they find it.

To put things in perspective, let me recall Caterpillar's experience with the negotiations that yielded the North American Free Trade Agreement (NAFTA) and the Uruguay Round agreements.

## Key Benefits of NAFTA

NAFTA is now ten years old, so we've had plenty of time to evaluate its impact on our activities, customers and communities. At Caterpillar, we believe that impact has been enormously positive. From our viewpoint, the only real losers are our competitors who can no longer hide behind high tariff walls. At Caterpillar we've experienced four key benefits due to NAFTA:

- The first and most obvious is this. For an exporter like Caterpillar, *NAFTA not only provides better access to the Mexican market; it actually provides preferential access.* Put another way, NAFTA allows us to sell most of our products in Mexico duty-free, while our competitors who have not established a North American manufacturing presence must still contend with duties. Today our U.S. exports to Mexico are triple what they were before NAFTA went into effect.
- A second and equally important benefit is that *NAFTA provides increased access to the U.S. market.* This is especially important for the parts and components incorporated into our prime products – because it allows us to rationalize some production. For example, assembly work previously performed in Mexico was transferred to the United States, while steel fabrication work moved to Mexico. Today, Caterpillar's U.S. operations are significantly more competitive than they were before NAFTA – and, in turn, we're a more formidable competitor in markets both inside and outside North America.

that today the proliferation of preferential trade arrangements is adversely affecting developing economies as a whole, even if each one may be benefiting the parties directly involved.

The studies were drawn together in the World Bank's Global Economic Prospects 2005, focusing on trade, regionalism and development.

In seeking to

- liberalize trade in agricultural products and light manufactures,
  - make sure WTO rules apply equally to all member countries and
  - integrate developing countries into the world economy,
- the time may have come to restore non-discrimination to its original position as the cornerstone of the multilateral trading system.

#### Trade Policy Roundtable

The Cordell Hull Institute's Trade Policy Roundtable is sponsored by eight international law firms in Washington, DC: Akin Gump Strauss Hauer & Feld, Arnold & Porter, Hogan & Hartson, O'Melveny & Myers, Miller & Chevalier, Sidley Austin Brown & Wood, Steptoe & Johnson and Wilmer Cutler Pickering Hale & Dorr.

- The third benefit is that *NAFTA also promotes non-inflationary economic growth*. What is often forgotten is that a free trade agreement is essentially a permanent tax cut. And as a result, agreements like NAFTA encourage trade, stimulate investment and generate economic growth. For Mexico, more trade translates into the need to build a modern highway system and other infra-structure, generating significant demand for Cat equipment.
- The fourth and perhaps biggest benefit of NAFTA isn't in what it does, but in what it *prevents*. There was a time when the Mexican Government would have reacted to events like the 1995 peso crisis or the 1997 financial crisis by closing its border to trade. Largely because of NAFTA, that didn't happen. In effect, *NAFTA provides the stability and confidence* that allows Mexican leaders to avoid quick-fix, protectionist solutions and weather difficult economic times.

#### Multilateral is More Beneficial

As important as bilateral agreements like NAFTA are, we can't lose sight of the fact that multilateral negotiations, like the Uruguay Round negotiations of 1986-94, are often more important.

For example, Caterpillar's goal during the Uruguay Round marathon was to convince negotiators that Cat customers in the developed world should be able to buy our products without the added burden of duties. We knew that was a tall order. But since rounds of multilateral trade negotiations only happen every ten years or so, it was worth a try. It took considerable effort and a lot of patience, but after five years of negotiations and another five years of implementation, the multilateral process worked. Today, Caterpillar customers in more than twenty developed countries have duty-free access to most of the products it makes.

But that was only the tip of the iceberg. By cutting taxes on trade, the Uruguay Round agreements became, in effect, a massive global tax cut that stimulated economies world-wide. At the same time, increased competition made possible by lower trade barriers helped to tame inflation and keep interest rates low.

We believe that the liberalization of trade made possible by NAFTA, on a regional basis, and made possible on a worldwide basis in successive GATT rounds was a central element in the economic expansion of the 1990s. Today we have an opportunity to restoke the fires of free trade and economic growth. Much of our recent focus has centered on the strategy of "competitive liberalization", promoted by Robert Zoellick, as the U.S. Trade Representative. There are merits in his approach. Negotiating bilateral, regional and multilateral agreements is an ambitious agenda – and, done right, has the potential to be mutually complementary.

For Caterpillar, the key is to make sure that, in our zeal to negotiate bilateral free trade agreements, we don't lose sight of what is truly the *grand prize of trade liberalization* – the Doha Round negotiations and, to a lesser extent, the Free Trade Area of the Americas.

Eliminating trade barriers with a few countries is a *step* in the right direction. But a Free Trade Area of the Americas would be a *leap* forward – with the potential to transform the entire hemisphere by generating economic growth. And the Doha Round agenda could take us further still. By significantly reducing barriers to trade and investment in *all* countries, the WTO negotiations offer a historic opportunity to spread the benefits of an integrating world economy to the developing world – and kick the global economic growth engine into a whole new gear.

With that in mind, I can summarize Caterpillar's views on trade negotiations easily. We believe multilateral negotiations are by far the most efficient and comprehensive way to promote trade liberalization.

As a practical matter, however, we'll take freer trade *whenever and wherever* it can be obtained. That's why we were strong supporters of the free trade agreements with Chile, Singapore, Australia and Morocco – as we are of the agreements with the Dominican Republic/Central America and Bahrain on which we hope the U.S. Congress will soon vote.

We're also excited about the free trade negotiations with Thailand, the South Africa Customs Union and the Andean countries. These agreements should not be taken lightly – especially not by groups like Caterpillar. Unlike previous agreements that eliminated tariffs over as many as fifteen years, these ones eliminate almost all tariffs on manufactured goods on the day they go into effect. The immediate impact is expected to be significant.

In 2004, Caterpillar's U.S. exports to Chile, for example, nearly tripled. To be fair, much of this increase was the result of higher demand for Cat products resulting from high commodity prices. But improved market access resulting from the free trade agreement has also been an important factor.

The potential of the U.S.-Australia free trade agreement is even greater. Australia is already Caterpillar's second largest export market. And when the agreement is put into effect, on January 1, 2005, we calculate the impact for Caterpillar will be equal to that of NAFTA. Together the Chile and Australia free trade agreements will annually reduce the tariffs paid by Caterpillar's customers by more than \$40 million.

Beyond the free trade agreements already being negotiated, we'd like to see the list of new bilateral partners include countries that

are economically meaningful, reform-minded and diplomatically important wherever possible.

### **New Bilateral Free Trade Partners?**

First on that list is **Turkey**, a democracy and large economy, a bridge from the broader Muslim world and a linchpin to our efforts to bring peace and prosperity to the region. Free trade negotiations with the United States would put pressure on the European Union to extend membership to this important NATO ally.

Second are **Egypt** and other Middle East countries. There are compelling diplomatic reasons why the United States has already established free trade agreements with Israel and Jordan. Even though these same reasons also apply to Egypt, the United States has to date avoided the subject. To bring prosperity to the region, we need to do more than rely on foreign aid. We need to promote direct foreign investment, which is what a free trade agreement would do. And we believe the Bush Administration is right to look for other free trade partners in the region.

Third is **New Zealand**. Even though it's a small economy, to a large degree it is already integrated with Australia. Since the United States and Australia are moving forward with a free trade agreement, it only makes sense to negotiate a free trade agreement with New Zealand as well.

### **Doha Round is the Primary Focus**

But the primary focus at Caterpillar has to be the Doha Round agenda. In fact, we believe that the business community, non-governmental organizations and "think tanks" must insist that the United States, the European Union and Japan adopt policies that allow the benefits of an integrating world economy to be extended to the developing countries, particularly those of Africa that are lagging so far behind.

In the industrialized world, we may not want to admit it, but many trade practices that are taken for granted disadvantage the developing world. It is troubling that the United States collects more import duties from Bangladesh than from France, more from Cambodia than from Singapore – and that was before the U.S.-Singapore free trade agreement.

Governments need to reform WTO rules. While anti-dumping remedies are necessary, [they and other safeguards need to be more consistent with one another], so that companies and countries don't use these rules to game the system. As we move toward greater trade liberalization, the last thing we need is for anti-dumping provisions to become the global protectionist weapons of choice in the twenty-first century. [Already there are more anti-dumping actions being taken against American-based



The **mockingbird** is the state bird of Tennessee. Cordell Hull represented a district of Tennessee in the Congress of the United States, and was elected a senator from there, before becoming U.S. Secretary of State (1933-44).

"The mockingbird is known for fighting for the protection of his home – falling, if need be, in its defense. Mockingbirds are not intimidated by animals larger than themselves and

have been known to attack eagles”

– Diana Wells, *100 Birds and How They Got Their Names* (Chapel Hill, NC: Algonquin, 2002)

### **Trade Policy Analyses**

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businesses than there are anti-dumping actions in the United States against businesses based in other countries.]

Earlier this year, the United States extended the Africa Growth and Opportunity Act. It was a step in the right direction – as were, as I said earlier, the free trade agreements with Chile, Singapore, Australia and Morocco.

In the United States, by contrast, the overly generous farm bill and steel decision back in 2002 were steps backwards. The decision to impose steel tariffs was particularly troubling and counter-productive. It weakened America’s leadership position in multilateral trade negotiations – and worse, it harmed an already weak U.S. economy by causing higher prices and lost jobs among America’s steel-using manufacturers.

[Fortunately, the Administration ended the steel tariffs early and since then, through both words and deeds, President Bush has proven to be an unapologetic supporter of trade liberalization. I only wish others who seek the presidency would follow his lead.]

Looking forward, we can’t afford any more missteps. The Doha Round negotiations are a *once-in-a-generation* chance to make the big changes needed to promote trade liberalization and investment throughout the world. The key to success involves tackling an array of agricultural issues ranging from eliminating export subsidies to substantially reducing domestic support to substantially improving market access. And while some progress was made in the “July package” of framework agreements, as a result of the leadership of Ambassador Zoellick, we must work together to make sure that the political clout of a few protectionist agricultural interests doesn’t undermine progress in the Doha Round negotiations.

Whatever it takes, the United States can’t allow the WTO negotiations to fail. Forgoing the benefits of those negotiations would serve no useful purpose. Rather, it would hurt worldwide economic growth and the people of the developing world, especially those in the poorest countries. And it would hurt U.S. companies like Caterpillar whose future depends on economic growth outside the United States.