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PROGRESSIVE INCREMENTALISM: U.S. FOREIGN ECONOMIC POLICY OVER THE NEXT FOUR YEARS*

John M. Curtis

As we look ahead following last year's U.S. presidential and congressional elections, Canadians — and Canadian business in particular — will want to have a better sense of the economic prospects, as well as the context, of U.S. foreign economic policy over the coming half-decade or so. For, notwithstanding all the talk, debates, op-ed articles, think-tank-pieces and even books in recent years suggesting or asserting the decline of American economic power, Canada's ever-present integration and interdependence with our southern neighbour is both a reality and now, again, an important, medium-term asset. Over the coming four years and likely beyond, and once it has completed sorting out its "fiscal cliff" matter, the U.S. is positioned to be the source of increasing economic growth. The American economy has strengths: its high productivity and innovation compared to most other countries, massive piles of private sector cash leading to all sorts of investment potential, a devalued currency, and a relatively young workforce compared to the European Union, Japan, and even Canada. Therefore, although the U.S. economy continues to face large challenges related to fiscal imbalances, there are reasons to expect increasing economic growth over the medium term.

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Les communiqués de l'École de politique publique sont de courts articles portant sur une question particulière de politique publique et visent à fournir au lecteur une analyse concise, critique et ciblée.

L'Université de Calgary regroupe des chercheurs dans 16 facultés (et proposent plus de 80 programmes d'études) et 36 instituts et centres de recherche, notamment l'École de politique publique. Sous la direction de Jack Mintz, titulaire de la chaire Palmer d'études des politiques publiques, et avec la collaboration de plus de 100 enseignants et chercheurs, les travaux de l'École de politique publique et de ses étudiants contribuent à un débat public étayé sur les questions financières, sociales, énergétiques, environnementales et internationales, pour améliorer le rendement économique et social du Canada et de l'Alberta.

LE GRADUALISME: LA POLITIQUE ÉCONOMIQUE ÉTRANGÈRE DES É.-U. AU COURS DES QUATRE PROCHAINES ANNÉES*

John M. Curtis

RÉSUMÉ

Dans la foulée des élections présidentielles et au Congrès des États-Unis l'année dernière, les Canadiens — et en particulier les gens d'affaires — voudraient être en mesure de mieux cerner les perspectives économiques ainsi que le contexte de la politique économique étrangère des États-Unis pour les cinq prochaines années, plus ou moins. Car peu importe les discussions et les débats, les éditoriaux, les articles d'experts et même les livres parus récemment et qui suggèrent, ou même affirment le déclin de la puissance économique américaine, l'intégration et l'interdépendance du Canada avec son voisin du sud constitue encore et toujours une réalité et demeure pour l'instant un atout à moyen terme. Au cours des quatre prochaines années, et probablement au-delà, et une fois que les États-Unis auront trouvé une solution à leur problème de « précipice budgétaire », le pays sera en position de relancer la croissance économique. L'économie américaine a des forces : sa vigueur sur le plan de la productivité et de l'innovation, comparativement à la plupart des pays, des réserves imposantes d'argent dans le secteur privé pouvant déboucher sur des investissements de toutes sortes, une monnaie dévaluée et une main-d'œuvre relativement jeune par rapport à celle de l'Union européenne, du Japon et même du Canada. Par conséquent, bien que l'économie des États-Unis demeure confrontée à des défis de taille en ce qui a trait aux déséquilibres fiscaux, on peut s'attendre à une croissance économique à moyen terme.

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Canada, along with its strengthening trade and economic relationships with other parts of the world, faces an increasingly positive external environment, notwithstanding the European Union's current debt and banking issues, as well as the slowing of growth in several key emerging markets. The global economic environment directly affecting Canada, that is, will neither be spectacular, nor historically strong, but will be one on which to build an even stronger foundation for future job growth and prosperity. At a minimum, given the coming U.S. economic strength, Canada will be sheltered to a large extent from the downturn that economies largely comparable to ours — such as Australia — will likely endure in the months ahead.

Within this broader context, and attempting to anticipate, if not predict, probable U.S. foreign economic policy directions over the coming four years or so, several "stylized facts," or premises, should be made clear:

> **FIRST:** The "fiscal cliff"[1] alluded to above will get resolved more definitively by the new Congress during the first half of 2013.
>
> **SECOND:** While the foreign economic policy of many countries is a subset of foreign policy, in the case of the United States, this is certainly the case. For example, even while shaping the postwar economic order with the broad foreign policy objective of ensuring peace and stability, the United States insisted, from 1947 onward, that the new, global international trade rules — which became the General Agreement on Tariffs and Trade (GATT) and after 1995 the World Trade Organization (WTO) — must, in effect, protect the interventions in the (basically) free-market American economy. The postwar trade regime, with its principles of openness, transparency, and non-discrimination, was thus designed to leave plenty of domestic-policy space for pre-existing and prospective U.S. domestic interventionist policies — this latitude extending, of course, to other GATT/WTO members. Similarly, the headquarters of the new international financial and development institutions — the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development (World Bank) — were placed in Washington, D.C. under the careful watch both of the State Department and the Department of the Treasury, with officials from both agencies assigned to the senior level of both international bodies.
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> **THIRD:** On a related point, foreign economic policy everywhere remains a manifestation and extension of domestic economic policy, the politics and economics of which — and the tension between producer interests and consumer interests with respect to every sector and to every issue — are central to every international economic policy initiative considered and/or taken.
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> **FOURTH:** The United States is committed to the rule of law, including its enforcement. This fact — shared by others, but reaching its peak in every aspect of life within the United States, enabled both by its political and its legal system — leads to a predictably inward focus and an innate conservatism in terms of seeking out and encouraging institutional change to meet new realities, or at times, to rectify old ones.

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[1] The "fiscal cliff" refers to the automatic tax increases and drastic spending cuts that were scheduled to take effect on January 1 of this year had the outgoing Congress not intervened.

FIFTH: On the other hand, the United States retains what some call its "exorbitant privilege" by virtue of the fact that its national currency is the world's de facto reserve currency and the primary medium of international exchange. This fact means that there is less discipline on U.S. fiscal and monetary practices than in any other country — both a blessing and a curse, as events over the past decade have demonstrated so clearly.

SIXTH: And finally, the United States remains the world's pre-eminent economic power with the responsibility, in theory and in practice, of providing leadership to protect and shape the international economic regime, and enforcing unilaterally, or through mutually agreed upon procedures, the ground rules for its ongoing operations.

In recent years, and for any number of reasons, neither the United States nor the wider world community has shown much concerted demand for change where foreign economic policy is concerned. While there have been calls from many and varied quarters for change, there has not been effective leadership, or success, in achieving much. For example, there have been calls for a recommitment to the G20; for reform of the International Monetary Fund's governance structure to reflect Asia's growing importance; for more socially and environmentally sensitive assistance programs at the World Bank and various regional banks; for tougher financial regulations; for renewed global trade talks to either complete the 11-year-old Doha round, or to begin a new negotiating round with a more current, business-friendly or relevant agenda; and for a credible post-Kyoto climate-change treaty. All these voices, important as they are, have not led to a clear demand for change within any of the international economic areas cited above. The global uniqueness or exceptionalism of the United States, combined with its inwardness, have not provoked or stimulated any clear manifestation of U.S. leadership, or the leadership of any other country, individuals, or groups of individuals.

In these circumstances, the United States, the traditional economic hegemon and guardian of the system, has only actively attempted to shape international economic discussions where it feels that its direct interests, or those of its "clients," are affected. The status quo, with sufficient "tweaking" to advance the system where absolutely necessary — progressive incrementalism — has characterized the recent past, and will continue to do so, with possibly two exceptions.

One is with respect to the Trans-Pacific Partnership (TPP); the other is the complex matter of Iran, the Middle East more generally, and the price of oil.

With respect to the Trans-Pacific Partnership: this prospective regional trade agreement has evolved into Washington's top international economic policy priority. Although conceived as early as 2005, and promoted over the next couple of years by four countries — New Zealand, Chile, Brunei, and Singapore (the P4) — the United States latched onto this now-expanded pan-Pacific trade initiative several years later, early in the Obama presidency, as part of the U.S. "tilt" towards Asia. Several overlapping, yet important geo-strategic, as well as economic factors, were undoubtedly involved: advancing further trade liberalization and stepped-up regulatory alignment, without the counterweight of the European Union or the demands of developing countries — large and small — as has been the case in the stalled global, World Trade Organization negotiations; the prospect of achieving job growth and future prosperity without (at least for now) involving the world's largest trader, and second largest economy, China; and the ability of the United States, which is by far the largest participating country in the now 12-nation talks, to shape the negotiations — by insisting on a post-NAFTA template — toward a "next generation" agreement for the rest of the world to emulate in due course.

When, and if, the TPP is successfully negotiated — with Canada and Mexico now joining the talks officially in December 2012, and Japan perhaps eventually joining — it will supplement and possibly even replace the Canada-U.S.-Mexico NAFTA, the still-nebulous Pacific Alliance, the Australia-New Zealand Closer Economic Relations (CER) Trade Agreement, and the many other regional and sub-regional agreements and arrangements around the Pacific Rim that have been entered into over the past decade. If successful, it will overshadow the multi-faceted and not-terribly-effective Asia Pacific Economic Cooperation (APEC) forum — the one Pacific institution in which Canada has been most active to date — and become the principal vehicle of economic integration in the region. Moving the TPP initiative along will remain the central international economic focus of the U.S. over the next four years, and it will be a much less controversial issue than other major international economic issues, such as strengthened international financial regulations, or those related to climate change[2].

The United States will also show leadership in a progressively incremental way concerning Iran and oil. Unlike the active and obvious leadership that the U.S. is demonstrating with respect to the TPP, the U.S., in this instance, is proceeding in a very different way, with very different objectives: it is quietly but firmly taking steps to protect its allies and client states in the region and around the world by ensuring that geo-political/strategic decisions do not result in the price of oil being either too high or too low. Oil prices that remain too high by historical standards will hurt the world economy, including the U.S. economy; oil prices that are too low, will seriously diminish revenues of countries reliant on oil exports, many of whom depend on the United States for security. While, as a general matter, oil is not as key an element in the world economy as it was in previous years, it remains important in the case of transportation and the movement of goods and services across borders — the core of the liberal world order.

As noted earlier, in other areas of international economic policy — from the G7/G20; reform of the International Monetary Fund (IMF); strengthening international financial regulations; completing the Doha round with the World Trade Organization (WTO) or developing a new agenda for global trade talks within or outside the WTO; or turning to trade-related climate-change matters — the U.S. will remain an active and interested participant, advancing and defending its own interests. But it will not be seen to, or wish to, take the lead. It undoubtedly will continue to act as the guardian and promoter of each of the many international regimes and practices in place worldwide, and of the institutions that support them. But it will follow the mantra of promoting actively ongoing incremental change only where necessary to keep these international policy frameworks relevant in the contemporary world. It is still clear that nothing can or will get done comprehensively in today's world economy — no substantive reform, no significant operational changes — unless the U.S. is part of the solution. Its importance in all of these bodies and on all of these issues should not be minimized, even in a world of shifting global power; it is simply that the United States, over time, is narrowing its focus to fit its means and taking a less-strident leadership role than that which characterized most of the past half-century.

[2] While estimates of the possible economic impact of a successfully completed TPP vary, some suggest that the impact on growth and jobs will equal that of a completed, worldwide Doha-round trade agreement, if the latter were ever completed.

For Canada, this "steady-as-she-goes" forward movement — with the only real U.S. drive manifested with respect to the TPP and Iran and oil — will mean no dramatic change. At the most general, macro-economic level, the slow, ongoing-but-upward trajectory of the U.S. economy will provide continuing, underpinning support for our economy — for jobs; for investment; for technology transfer; for innovation; for energy; and for involvement in U.S.-led global-value chains serving final markets in both the U.S. itself and U.S. markets abroad. Increased confidence from U.S. consumers and businesses will also flow over the border to Canada, leading to more optimism and thus, a sense of confidence in prospects here. Since economic growth (expanding GDP) in a country's trading partner is the primary factor in influencing the amount and direction of trade and investment with that partner, Canada-U.S. cross-border activity will expand over the coming four years; the currently repressed share of 75 per cent of total Canadian merchandise exports going to the United States — compared to a high of 87 per cent as recently as 2001 — is probably at a cyclical low. Since security will continue to trump trade, particularly from a U.S. perspective, progress on the Beyond the Border joint-security approach and the Regulatory Cooperation Council will remain an important bilateral focus between our two countries.

On the larger questions — the Trans-Pacific Partnership, Iran, G7/G20, financial regulations, IMF reform, and perhaps even climate change — Canada, too, will continue to be a presence. But, like the U.S., it will be at least an active, but not a leading participant. It is at times like this, when little intellectual "heavy lifting" is being done by anyone, that a relatively small country, such as Canada, has an opportunity to punch above its weight and to shine.

About the Author

John M. Curtis is a Senior Fellow at the C.D. Howe Institute (Toronto) and at the Centre for International Trade and Sustainable Development (Geneva) as well as an Adjunct Professor at Queen's University (Kingston). He was the founding Chief Economist in the Department of Foreign Affairs and International Trade and holds a B.A. from the University of British Columbia and a Ph.D. in Economics from Harvard University.