The Rise of “Free” Trade in the 20th Century

In Western economies, especially in US economic policies were more to support protectionism in international trade. However, by the mid-1930s, a new, more open trade policy began to emerge with the implementation of reciprocal trade agreements. The Open-Door policies was the first examples of free trade agreements. The first examples of these policies were the Great Britain’s Anglo-Chinese of Nanjing (1842) and Wangxia (1844). But, in 1980s major industrial powers started to gain influence on the coastal China, Britain was also one of them, but it abrogated its role of world hegemony. Then US maintained The Open-Door policy—which was based on a series of diplomatic notes written by Secretary of State John Hay—was directed at maintaining equal and nondiscriminatory privileges among the major countries trading with China at the time: the United States, Russia, Germany, France, Japan, and Britain. It was, in other words, a “free” trade policy, albeit for a geographically limited area. The U.S. maintained open-door policies, in large part, because it occupied a disadvantageous position in China (relative to the European countries and Japan), and had little to gain if China became a thoroughly closed market. the Open Door policy marked a significant first step by the U.S. toward assuming the hegemonic mantle. As a fledgling hegemon, the U.S. commitment to maintaining an open system was not entirely consistent. This helps explain why the U.S. continued to follow an ostensibly protectionist line in its trade policy more generally. In 1922 and 1930, two major tariff bills were passed: the Fordney-McCumber Act, and the Smoot-Hawley Tariff Act. Interestingly, earlier in the century, two other tariff bills were passed that lowered tariffs. These were the Payne-Aldrich Act of 1909 (which was nonetheless a protectionist bill) and the Underwood Tariff Act of 1913 (a partly liberal bill, in that it significantly lowered tariffs). Except for the infamous Smoot-Hawley Tariff Act, it is important to note, the various tariff bills were at least partly used as “bargaining tariffs” designed to extend the Open Door policy abroad (Lake 1983, p. 534). More specifically, they contained a provision for “flexible” tariffs that would allow the U.S. to impose higher tariffs on countries that discriminated against American goods.
The Great Depression, the RTAA, and the Emergence of U.S. Hegemony

The decision by the U.S. to erect higher protectionist barriers through the passage of the Smoot-Hawley Tariff Act helped spur a significant worldwide rise in tariff rates and other discriminatory measures; not surprisingly, U.S. goods were a key target (Irwin 1998; also see table 4.5). While it is not at all clear that the Smoot-Hawley Act caused or even significantly contributed to the severity of the Great Depression, it is nonetheless clear that it led to a serious rethinking within the United States about the efficacy of the tariff as the main instrument of trade policy. In this regard, the Great Depression played an important role in pushing the domestic political balance in favor of the democrats, who were then able to use their newfound voting advantage to pursue reciprocal trade agreements (agreements that would reduce tariffs on a bilateral, as opposed to multilateral, basis). The basis for bilateral trade agreements came relatively quickly with the passage of the Reciprocal Trade Agreements Act (RTAA) of 1934. The successful passage and implementation of the RTAA has been intensively studied and debated by both economists and political scientists. The RTAA set in motion a largely virtuous cycle (as liberals would emphasize) that proved to be beneficial to the industrialized world, and especially to the United States. Because of this, the RTAA helped to cement a liberal trend in U.S. trade policy that had not previously existed. The path toward a liberal international trading system was, of course, interrupted by the outbreak of World War II. Significantly, though, World War II interrupted the process, but did not stop it. Indeed, in important ways, it may have ultimately accelerated the process of trade liberalization. As Hiscox (1999) argues, World War II had the effect of radically reducing—although only temporarily—import competition for U.S. manufacturers while simultaneously fueling a tremendous expansion in export demand for U.S.-made products (p. 685). The reason is easy to see: unlike most of the industrialized world, the United States homeland was essentially isolated from the devastation of the war. While other countries had to rebuild, the U.S. was able to build up from a still-intact, and very strong industrial foundation.

After WWII

One of the first priorities of the United States in the postwar period was to create the framework for a more stable international economic system. The Bretton Woods system is most closely associated with the creation of the international monetary or financial system. But another key (and strongly related) aspect of the BWS was the effort to liberalize international or cross-border trade on a sustained, multilateral basis. This effort
was largely successful, as over several decades a new international trade regime was constructed. This almost assuredly could not have been achieved without the exercise of tremendous political will and power, and more specifically without the coordinating and stabilizing efforts of the United States.

After several years of both bilateral and multilateral negotiations, a draft agreement known as the Havana Charter (formally, the Final Act of the United Nations Conference on Trade and Employment) was announced on March 24, 1948. The charter’s main objective was the creation of the International Trade Organization (ITO). Although signed by 53 of the 56 countries participating in the final UN conference on this issue, the ITO failed to materialize. One big reason for this was the unwillingness of the U.S. Congress to ratify the charter, and without U.S. commitment, it was no surprise that other countries likewise refused to move forward. In retrospect, it is not difficult to see why the U.S. Congress refused to approve the charter. Specifically, the ITO was, at the time, an extraordinarily ambitious idea. As Narlikar (2005) explains it, “The ITO envisaged by the Havana Charter had a far-reaching mandate, and an elaborate organization to implement it.... [B]esides covering the obvious areas of commercial policy, the 106 articles of the ITO extended to areas of employment, economic development, restrictive business practices, and commodity agreements. It gave recognition to the importance of ensuring fair labour standards, and also incorporated provisions that allowed governments to address their development and humanitarian concerns” (p. 12). More simply, the ideas behind the ITO were too “radical” and too much to handle for many U.S. congressional free-trade-wary representatives. This points to a larger lesson as well: the failure of the ITO could very well have spelled the failure of the entire push toward trade liberalization in the early postwar period.

Fortunately (but not necessarily fortuitously), the ITO was only one prong of a multi-pronged strategy. Another prong was the General Agreement on Tariffs and Trade (GATT). Originally, the GATT was to be an interim arrangement until the ITO came into force, but it was also pursued by the Truman administration precisely because of fears that the U.S. Congress would oppose the more ambitious provisions of the ITO (Kaplan 1996, p. 53). Unlike the ITO, moreover, the GATT did not require ratification by the Congress (ironically, this was a result of the congressionally approved RTAA). As an interim agreement, the GATT was much less ambitious than the ITO; it focused on trade (or commercial) relations only and revolved around three basic principles:
(1) nondiscrimination—i.e., the concept of most-favored-nation (MFN) status—in trade relations among participating countries; (2) a commitment by all participants to observe the negotiated tariff concessions; and (3) a prohibition of quantitative restrictions (quotas) on exports and imports. Not only was the substantive coverage much narrower, but so too was its legal and institutional basis. The GATT was, in essence, little more than a negotiating forum; it was not an international organization, nor did it even have a membership per se—instead it had “contracting parties” (Narlikar 2005, p. 16). Despite these shortcomings, the GATT not only survived (for 47 years, after which it was formally replaced by the WTO), but it proved to be an effective—albeit far from perfect—means for establishing the necessary groundwork for a significant expansion of cross-border trade.

The main concern is how the GATT negotiations laid the groundwork for the establishment of a liberal international trading regime (or a new socially constructed order for international trade). In this regard the move from item-by-item negotiations to across-the-board negotiations—which was partly related to the growing economic power and influence of the European Economic Community (later the European Community, and finally the European Union)—was an important step. Specifically, it made it more difficult for parochial domestic interests (i.e., special interests) to influence negotiations (Kaplan 1996, p. 68). Also, the successive rounds of multilateral negotiations helped to establish a practical and normative framework for talks and disputes over trade issues in general, not just tariffs. Tariffs, as you know, are not the only barriers to trade. NTBs (nontariff barriers) are equally, and potentially more, corrosive to trade, since they are nontransparent (meaning that it is not always obvious what constitutes an NTB). As tariffs declined, many countries began turning to NTBs. But before this trend could completely undermine the progress made through tariff reductions, talks on nontariff barriers were added to the GATT agenda during the Tokyo Round (1973–79).

The Birth, Significance, and Troubles of the WTO

Discussion about the establishment of WTO took place in the final GATT round, the Uruguay Round (1986-1993). A major reason why the GATT had become unwieldy and ineffectual was its ad hoc nature. The many overlapping negotiations of the GATT had produced a range of agreements and measures, not all of which were consistent with one another. Thus, some sort of coordinating mechanism was required for creating order out of an increasingly chaotic situation. Creating a coordinating mechanism,
however, was (in practical terms) not possible within the existing GATT framework. As a forum rather than an organization, moreover, the GATT could not directly coordinate its activities with international organizations such as the IMF and the World Bank—a function that was becoming increasingly necessary as the global economy had become more complex and interconnected. The GATT had served its purpose, but without a solid institutional basis it might not have been able to sustain the progress that had been made. The significance of the WTO, therefore, would be found in its ability to reinforce the existing international trading system, but also to extend liberalization into the most politically sensitive and divisive areas.

On the first point, the WTO did, in fact, play a key role in reinforcing the existing system. One of the most important new features was the adoption of the single-undertaking principle. This principle required member countries to accept and implement all WTO agreements as a package rather than through a pick-and-choose method, which had been the practice under GATT. For the most part, this also meant that there would be no grandfathering of rights; that is, countries that had previously been exempted from certain agreements and articles because of existing (domestic) legislation were no longer allowed exempt status. This was a major change, in that it compromised the principle of state sovereignty by requiring member countries to change their domestic legislation if there was a conflict with WTO rules. Within the framework of the WTO, it is important to add, this was possible due to a Dispute Settlement Panel (DSP) that had been much strengthened via the Dispute Settlement Understanding (DSU). The new DSU made WTO rules easier to adjudicate, and easier to enforce through the principle of cross-issue retaliation (cross-issue retaliation allows a member country or countries to apply WTO-approved sanctions against a violator of an important area of trade in order to maximize the impact of the punishment). More broadly, the DSU gave the WTO a power that few other international organizations had—a compulsory, legally binding process for resolving conflicts between member states. The compulsory element of the DSU was and is key: unlike the GATT (which had its own dispute-settlement procedures), or other international organizations that have a judicial process, the DSU did not require the consent of both parties to bring or hear a complaint.

The WTO has been far less successful in extending liberalization into the most politically sensitive and divisive areas. This is clearly reflected in the current round of trade negotiations (under the WTO, high-level trade talks take place in ministerial
conferences held every two years), known as the Doha Development Agenda, or the Doha Round for short. The Doha Round began in 2001, and was designed to take up a number of difficult issues, including agriculture, services, intellectual property regulation, environmental agreements, electronic commerce, regional trade agreements, transparency in government procurement, and trade facilitation, among others. The results have not been pretty: after the initial Doha meeting, the next ministerial conference in Cancún (2003) collapsed after just four days, and subsequent meetings in Hong Kong (2005) and Geneva (2009 and 2011) also failed to reach agreement. Things were so bad at one point that the biennial ministerial meeting in 2007 was cancelled (in addition to the ministerial conferences, there were also a number of lower-level, that is, nonministerial, meetings). In December 2013, there finally was a breakthrough in negotiations; although not completely resolved, preliminary agreement was reached on some particularly sticky issues, although it still remains to be seen how far things will move. As suggested above, however, the obstacles are not only related to difficult-to-negotiate issues, but also to (1) a dramatic expansion of membership (by the Doha Round, the WTO had 155 members); (2) a more pronounced division among “developed” and “developing” countries; (3) consensus decision-making; and (4) an all-or-nothing principle (based on the idea of a single undertaking wherein, in effect, “nothing is agreed until everything is agreed”).