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Constant Ends, Flexible Means: C. Fred Bergsten and the Quest for Open Trade

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Over the past 25 years, C. Fred Bergsten has launched and institutionalized a remarkable think tank. And beyond his role at the Peterson Institute for International Economics, he has established himself as a front-rank public intellectual on a range of international economic policy issues. He has interpreted the past. He has lauded or decried the present. He has prescribed for the future. His voice and his pen have marked out a broad range of policy territory: money, trade, Europe, Japan, American competitiveness, the G-7, APEC—the list goes on.

Central to his work has been the goal of trade liberalization, which he has pursued throughout his professional career. His efforts began as a government official (at State, the National Security Council, and Treasury) and think tank analyst (at the Council on Foreign Relations and Brookings) from the late 1960s through 1980. They multiplied with the creation of the Institute in 1981. They combined recurrent themes with openness to new methods of attaining them as circumstances seemed to dictate.

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Bergsten's work has highlighted both economics and politics, addressing not just the welfare-enhancing benefits of trade expansion but how the political system might bring it about. This chapter summarizes and analyzes this impressive Bergsten record. It begins by highlighting recurrent themes and then moves to the historical record, centering particularly on the Institute and its work. The conclusion asks whether the same emphases are likely to be appropriate during the Institute's next 25 years.

Recurrent Themes

Core Commitment to Trade Liberalization

Central to the Bergsten worldview is the value of open trade. For the most part, trade's goodness is assumed rather than demonstrated, but there are recurrent references to the "welfare benefit of reducing present restrictions" (Bergsten 1973a, footnote 20). Moreover, as discussed later, Bergsten mandated and publicized the work of Gary Hufbauer and his colleagues to generate a "big number" estimate ($1 trillion annually) of trade's benefits to the US economy (Bradford, Grieco, and Hufbauer 2005). There is also recognition of a broad political economy rationale for barrier reduction: "the traditional foreign policy desire to use economic negotiations as a functional means for expanding global cooperation" (Bergsten 1973a). Presumably, he concurs—at least in spirit—with the view of Cordell Hull that "unhampered trade dovetailed with peace" and its opposite, "high tariffs . . . with war" (Hull 1948).

But Bergsten has been much more concerned with means: how to get free trade and how to resist new trade protection. Domestically, the threat comes from producers seeking restricted markets and hurt by foreign competition. The threat is intensified if the dollar becomes overvalued and the trade balance deteriorates, as this increases the range and depth of injury from imports. In recommending policy responses, Bergsten has consistently stressed three:

- international negotiations to reduce trade barriers (the "bicycle theory");
- macroeconomic policy balance and coordination (the overvalued dollar as "leading indicator" of protectionism); and
- compensating the trade losers (adjustment assistance).

And there is a corollary to the first: a theory of "competitive liberalization" holding that bilateral and regional barrier reduction stimulates market opening worldwide.

International Negotiations and the "Bicycle Theory"

Over 30 years ago, Bergsten declared trade policy to be "dynamically unstable," making "maintenance of the status quo . . . untenable. . . . Steady movement toward trade liberalization is necessary to halt the acceleration of the trend toward increasing trade restrictions" (Bergsten 1973a). By the early 1980s, if not earlier, he was giving it a now familiar name.[1]

> The hypothesis of "dynamically unstable trade policy" holds that the trade regime either moves forward toward liberalization or backward toward protection, and an MTN [multilateral trade negotiation] helps the trade policy "bicycle" keep its forward-moving momentum. . . . According to the "bicycle theory," trade policy must move ahead or it will topple. (Bergsten and Cline 1982, 18, 71)

> I'm fond of something called the bicycle theory, which says that trade policy has to either be moving ahead, toward greater liberalization, or it topples in the face of protectionist pressures from individual sectors. . . . To hold back the protectionist slide and curb restrictive pressures from vested parochial interests you need to couch trade policy in the broader context—the national interest in greater welfare for the consumer and the economy as a whole, and the benefits to export interests from opening markets worldwide. That, in turn, seizes the interest of a President, a Congress, a prime minister of another country and gets a political commitment made to proceed in the liberalizing direction. (Bergsten quoted in Cohen 1984, 241)

Once coined, the "bicycle theory" became standard Bergsten parlance:

> History demonstrates the validity of the "bicycle theory": if trade policy does not move toward the greater openness that is in the general interest, it will topple in the face of protectionist pressures. (Bergsten 1988, 137; see also 140 and 155)

> The history of trade policy teaches forcefully that failure to move steadily forward toward liberalization condemns the trading system to topple over or fall backward in the face of protectionist pressures—the "bicycle theory." (Bergsten 1996b, 108)

> The situation is very serious if, like me, you believe in the bicycle theory, which says you either move forward or you fall over. (Bergsten 2000)

As suggested by these quotes (and the more extensive analyses from which they are drawn), the logic of the theory is straightforward. Liberal trade policy is ever vulnerable to protectionist pressures from trade-impacted producers—if the agenda is left to them, the question will be not whether to impose new trade restrictions, but how much and on what. You can't beat something with nothing; there must be a liberalizing alternative. Since large-scale unilateral barrier reduction is seldom viable politically,

1. Concerning the "bicycle theory," Deardorff's "Glossary of International Economics" says, "the idea was suggested by Bergsten and named by Bhagwati (1988)." The latter is incorrect, as documented above. The 1982 quotation above was the earliest use of the term we could find, so it was likely "named by Bergsten."

the alternative must be negotiations with trade partner-competitors in which we offer to reduce our barriers in exchange for their reducing theirs. With them, the trade policy bicycle moves forward. Without them, it falls down. (Remember Smoot-Hawley!)

Negotiations keep the bicycle moving by affecting both *process* and *outcome*. There are at least two process effects. While talks are ongoing, US officials can deny protection to claimants on the grounds that it will undercut US bargaining at Geneva (or wherever).[2] And major negotiations engage the interest of presidents, prime ministers, and protrade members of Congress, adding weight to the antiprotectionist side. The outcome effect is straightforward: Successful negotiations leave the US market (and partner markets) more open than they were before. The bicycle thus moves forward.

The theory contains at least two propositions: first, that the bicycle will fall in the absence of negotiations (protection will increase); second, that during negotiations less protection is in fact provided than would be otherwise. And the latter proposition must prevail over a counterproposition: that successful negotiations require that certain potential opponents (textiles, steel) be "bought off" with protection.

> Every president who has wanted to obtain the domestic authority to conduct new international liberalizing negotiations has had to make concessions to the chief protectionist interests of the day. The entire history of U.S. postwar trade policy can be characterized as "one step backward, two steps forward." (Bergsten 2002, 92–93)

In general, recent US trade history appears to validate the bicycle theory—at least up to the mid-1990s. There were substantial surges in protectionist pressures after both the Kennedy and the Tokyo Rounds.

A Corollary: "Competitive Liberalization"

As the United States moved to negotiate preferential free trade agreements (FTAs) in the 1980s and 1990s, Bergsten embraced these as promoting liberalization overall. One reason was the "bicycle" phenomenon:

> One of the great advantages of the contemporary regional initiatives is that they have kept the bicycle moving after the conclusion of the Uruguay Round. (Bergsten 1996b, 108)

But he moved beyond this to develop a broader argument for "competitive liberalization."

2. As the emphasis shifted from import protection to export promotion in the 1980s, the existence of ongoing multilateral negotiations could be invoked to dissuade export interests from using potentially punitive unilateral measures such as Section 301. This was the case, for example, with respect to the demands for market opening in Japan by the USA Rice Millers' Association during the Uruguay Round negotiations.

> [Why have] so many countries . . . headed in the same direction [of reducing trade barriers?] The overarching force . . . has been the process of competitive liberalization. [There has been a] dynamic interaction between regional and global initiatives to reduce trade barriers. . . . When the [Uruguay] Round faltered in the late 1980s, the three North American countries launched NAFTA and the Asians initiated APEC. When the Round almost failed to meet its final deadline in December 1993, APEC's initial summit in Seattle in November 1993 induced the Community to finally agree because, according to one top European negotiator, it "demonstrated that you had an alternative and we did not." (Bergsten 1996a)

In the George W. Bush administration, US Trade Representative Robert Zoellick embraced this strategy,[3] with Bergsten's strong endorsement.

> US policy has been approaching that ultimate goal [global free trade] via three channels of negotiation: bilateral FTAs with individual countries or small groups thereof, megaregional FTAs with Latin America (and, though only rhetorically so far, with the Asia Pacific), and multilateral reductions to trade barriers at the global level through the WTO (currently via the Doha Round). The strategic underpinning of this threefold approach is the concept of "competitive liberalization," under which negotiations at each level create new incentives and pressures for nonparticipating countries to join the process. (Bergsten and the Institute for International Economics 2005, 32–33)

The case seems strong that US-Canada, NAFTA, and APEC helped spur the initiation and completion of the Uruguay Round. However, the FTAs completed under Bush have not had a comparable effect—both the global Doha Round negotiations and the regional FTA talks have broken down. Arguably, the countries involved in the preferential agreements of the 2000s have been too small. Successful completion of the US-Korea FTA negotiations could have an impact on Japan, however, spurring greater liberalization among the Asia-Pacific nations, if not globally.[4]

Indeed, the global and preferential approaches exist in a kind of symbiosis—as long as the multilateral system remains fundamentally strong, preferential agreements can be used tactically to spur competitive liberalization. The risk, of course, is that they come to be viewed as a genuine alternative to multilateral liberalization and ultimately contribute to a world characterized by greater fragmentation and economic and political rivalry

3. A representative Zoellick statement was an address delivered in Phoenix, Arizona, on April 30, 2002, where he spoke of a US-generated "competition in liberalization": we would "proceed with countries that are ready" to open their markets, and success would "create pressure on others" (Zoellick 2002, 81).

4. In a broadly skeptical critique of the Bush administration's "competitive liberalization" strategy, Simon J. Evenett and Michael Meier characterize Bergsten as "Perhaps the most consistent and high profile analyst in support of Competitive Liberalization." After surveying "literally hundreds of documents, press releases, and statements," they declare that "if there is a ferocious contest for better access to the large U.S. market then many [potential FTA partners] are being very quiet about it." Their "interim assessment" concludes that the policy "is almost certain to fall well short of its goals" (Evenett and Meier 2006).

between competing "blocs" than would have otherwise been the case. We return to this possibility below in the context of the contemporary trade policy agenda.

Trade and Macroeconomics: The Exchange Rate

A second recurrent theme sounded (and plausibly pioneered)[5] by Bergsten is the notion that an overstrong currency is the greatest generator of increased protectionism.

> The postwar history of trade policy in the United States, at least, reveals that the most accurate "leading indicator" of trade policy—on both the liberalizing and protectionist sides—is the degree of equilibrium in the dollar exchange rate. Dollar overvaluation clearly breeds protectionist pressures even when unemployment is low (as in 1970–1972), while dollar equilibrium supports liberalizing measures even in the face of high unemployment (as in 1974). This is because dollar overvaluation adversely affects the competitive position of stronger industries as well as those that are traditionally susceptible to foreign competition, and thus fosters much broader political coalitions in support of restrictive policies. (Bergsten 1981, 13)

> One [major risk] is further escalation of trade protectionism in the United States. Dollar overvaluation and the huge external deficits it spawns have traditionally been the primary precursors of such domestic political swings, which would carry large costs for both the US economy and foreign policy. (Bergsten and the Institute for International Economics 2005, 9)

> The history of U.S. trade policy amply demonstrates that dollar overvaluation, and the huge and growing trade deficits that it spawns, are by far the most accurate predictors of U.S. protectionism. When currency misalignments provide sizable advantages to their competitors, more industries look for relief from imports. When their goods and services are priced out of global markets, meanwhile, fewer exporters are credibly able, or even willing, to fight for liberalization. (Bergsten 2005, 17)

A stronger dollar confers greater price competitiveness to imports, resulting in economic pressure on producers of domestic goods. A stronger dollar demoralizes exporters as well, since it renders them less price competitive overseas. Hence it not only unbalances trade but generates a political imbalance as well.

This critique is typically followed by an argument for greater exchange rate stability, through target zones or some other stabilizing arrangement.

5. Since the authors have not undertaken a comprehensive intellectual history of the field of trade policy analysis, we cannot reach definitive conclusions on whether this or any specific concept *originated* with Bergsten. But we know of no other expert who has given comparable emphasis to this relationship or who highlighted it earlier insofar as US trade is concerned.

> What is needed . . . is some kind of synthesis between the excessive rigidity of the fixed rate regime under Bretton Woods and the excessive flexibility . . . of the past ten years. . . . My own preference is for a target zone system. . . . (Bergsten quoted in Cohen 1984, 234–35)

So stated, this relationship seems elementary, important to stress only because it was long underrecognized. What gives Bergsten's thesis bite, however, is the argument that the strong dollar is a more powerful generator of protectionism than the traditional suspect, high unemployment. And for the 1962–95 period, this argument seems valid. The most intense protectionism came in strong-dollar periods (1969–71, 1981–85), not in the years of deepest recession (1974–75, 1982–83), though there is some obvious overlap between the two.

Compensating the Trade "Losers"

A third constant theme has been the need to respond to the distributional hurt caused by trade with programs to compensate the losers. Bergsten did not originate the idea of trade-related adjustment assistance, of course,[6] but he has been active in developing and promoting the idea. His most detailed exposition came early in his career, when he chaired a Chamber of Commerce Task Force on Adjustment Assistance.

> The Chamber [supports] a program of economic adjustment that will enable the United States to pursue a liberal trade policy in the 1970s. . . . It believes that such a program must compensate those whose skills are rendered unprofitable by trade for their losses and, more importantly, help them adjust into new endeavors. (US Chamber of Commerce 1973)

This introductory language was supported by more than 20 pages detailing the components of such a program. Trade adjustment assistance (TAA) was in fact expanded by the Trade Act of 1974 but then curtailed by the Reagan administration in 1981. Bergsten has continued to advocate strengthened adjustment programs—through that decade and up to the present (building on TAA program reforms enacted in 2002).

> The rapid pace of global economic change will continue to threaten industries in the United States (and elsewhere). . . . The challenge is to achieve adjustment in the most efficient and humane manner, avoiding excessive costs both to the individuals involved and to the economy as a whole.
>
> The basic goal of such a program should be to provide a wide array of financial assistance and adjustment services to displaced workers, thereby reducing the interest of labor in trade protection. (Bergsten 1988, 145)

6. It dates from a Council on Foreign Relations planning paper drafted during World War II and was given prominence by United Steelworkers President David J. McDonald in 1953 (Destler 2005, 23–24).

> When portions of society are harmed by policy choices taken in the general interest, there is a strong case for providing equitable compensation. [Moreover, t]he domestic backlash against globalization has become so powerful, especially over the past decade, that it has severely limited US foreign economic policy throughout that period. The case for mounting an effective program of domestic assistance to workers, and perhaps entire communities, disadvantaged by globalization, is very strong. (Bergsten and the Institute for International Economics 2005, 39)

Politically, TAA has in fact proved useful in deflecting protectionism—in particular, it has given protrade Democrats a rationale for supporting new negotiations *and* helping those who are hurt by the process. And it has aided a modest proportion of those Americans whose jobs have been casualties of trade expansion. The program has yet to fulfill its full substantive or political potential, however, in part because of the reluctance of organized labor to fully support it.

Bergsten as Policy Entrepreneur

In addition to his consistency in substantive themes, Bergsten has been consistent tactically in promoting free trade and global openness. He has been an exponent of "responsible excess," exaggeration of dangers in order to win attention. Thus he predicted that many commodity cartels would follow OPEC (Bergsten 1973b) and that the United States and Europe risked a trade war (Bergsten 1999). He sponsored and endorsed Stephen Marris's (1985) apocalyptic "hard landing" scenario for the world economy and has employed somewhat comparable language about the even greater imbalances that have emerged 20 years later (Bergsten and the Institute for International Economics 2005).

He has also encouraged "responsible apostasy" by others, sponsoring studies that diverged from free trade and proglobalization orthodoxy. Examples are Tyson's (1992) advocacy of aggressive trade activism and Rodrik's (1997) focus on globalization's costs.

When predicted calamities did not occur on schedule, Bergsten has claimed credit for heading them off—"the self-denying prophecy." The threat of Third World–based cartels was averted because Secretary of State Henry A. Kissinger changed policy and responded to Third World concerns. Likewise, a hard landing was averted in the 1980s because—prodded in part by the writings of Marris and Bergsten—Secretary of the Treasury James Baker III mobilized his counterparts at the September 1985 Plaza meeting and drove the dollar downward. Bergsten has recently urged Secretary of the Treasury Henry Paulson to undertake a similar initiative.[7]

Bergsten's promotion of open-trade policies has also been a constant throughout his professional career. It was on display during his work as a

7. C. Fred Bergsten, "What's a Treasury Secretary to Do? An Agenda for Henry Paulson, Here and Abroad," *The Washington Post*, July 26, 2006.

fellow at the Council on Foreign Relations (1967–69, 1971–72) and the Brookings Institution (1972–77). As senior assistant for international economic affairs at the National Security Council (1969–71), he promoted TAA and the launch of new trade negotiations and sought compromise in the festering US-Japan textile dispute that was undermining protrade initiatives. As assistant secretary for international affairs (and acting under secretary) of the Treasury (1977–81), he continued to pursue this agenda. He saw his bicycle and exchange rate theories vindicated as protectionism surged in 1967–71, then receded with dollar decline and the launch of the Tokyo Round.

Most important, however, Bergsten's mix of intellectual and practical skills was such that when the German Marshall Fund of the United States made the landmark strategic decision to launch the Institute, he was a (perhaps *the*) natural choice for its director. And it was there that he found an ideal platform for his substantive, managerial, and promotional talents.

The Institute Years

The Institute for International Economics was formed in 1981, and it soon became evident that the relationship between the institute and its director was symbiotic: Bergsten would have a central influence on the Institute's agenda; at the same time, the work produced by Institute-affiliated analysts would affect his own thinking.

The Institute's founding coincided with the accession to the presidency of Ronald Reagan, whose two administrations would mix continuity with, and departure from, previous practice. From the standpoint of Bergsten and the Institute, the Reagan administration's combination of tight monetary policy and profligate fiscal policy predictably resulted in rising real interest and exchange rates, widening trade and current account deficits, and pressures on trade policy emanating from the resulting squeeze on import competing sectors:

> The sharp tax cuts combined with massive defense expenditures will continue to produce large budget deficits. . . . To fight inflation, which will be promoted by its fiscal stance, the administration is relying solely on monetary policy, thus insuring that interest rates will remain quite high for the indefinite future. This level of interest rates—unprecedented in real terms in modern history and stemming primarily from the faulty policy mix of the administration—has badly distorted and undermined all major components of the world economy . . . the unprecedented overvaluation of the dollar caused by the policy mix will produce huge U.S. trade deficits and retard U.S. growth . . . the policies set in motion seem almost certain to revive strong protectionist efforts. The postwar record reveals that an overvalued dollar is by far the greatest single threat to a liberal trade policy in the United States. (Bergsten 1981, 24–30)

He concluded, "Continued malign neglect of the impact of U.S. economic policy on other countries would devastate U.S. foreign policy and U.S. domestic prosperity" (Bergsten 1981, 36).[8]

In Bergsten's distinctive view, the irresponsible macro policies threatened the gains to trade as well as broader foreign policy interests. Alteration in the macro policy mix could be justified in terms of protecting the gains from trade, domestic prosperity, and ultimately, the United States' standing in the world. In the policy realm, this is an unusual view, subordinating *macroeconomic* policymaking to a political economy imperative of maintaining the sanctity of the liberal, rules-based *microeconomic* international trade regime. Analytically, exchange rate overvaluation and current account deficits are interpreted as leading indicators of subsequent demands for international trade protection—which, once incorporated into law and practice, can have long-lived adverse welfare effects.

Bergsten and the Institute offered a multifaceted response to these challenges during the first half of the 1980s. The centerpiece of the critique of Reagan macroeconomic policies was Stephen Marris's analysis of the possibilities of a dollar crash created by the stresses of the Reagan macroeconomic policy mix, a campaign that culminated in the publication of *Deficits and the Dollar* (Marris 1985), released just after the Plaza Agreement. For the remainder of the decade, the Institute continued to support international initiatives to manage the global process of payments adjustment through the Louvre Agreement (Funabashi 1988), claiming credit for a "self-denying prophecy" with respect to Marris's jeremiad and continuing to warn of the adverse trade policy implications of an overvalued dollar (see also Destler and Henning 1989).

While Marris and others addressed the underlying macroeconomic causes of the worsening trade environment, invoking the "bicycle theory," Bergsten called for a new round of multilateral trade negotiations under the General Agreement on Tariffs and Trade (GATT) (Bergsten 1983, 12). In addition, the Institute strongly supported the launch of what became the Uruguay Round, which was to represent a constructive outlet for political pressures for trade policy activism (e.g., Hufbauer and Schott 1985, Hathaway 1987, and Miner and Smith 1988).

Multilateral trade negotiations are protracted affairs, and the Uruguay Round proved to be no exception. As a consequence, the tactic of offering

8. These expressions were not atypical by any stretch: Later, in congressional testimony, Bergsten would argue that, "The substantial overvaluation of the dollar in the exchange markets . . . is by far the most critical trade problem now faced by the United States" (Bergsten 1982, 1) and that industry and labor groups demanding such protection, however ill advised, "are really asking only for policy intervention to correct the distortions generated by other policy intervention (e.g., loose fiscal policy and very high interest rates) and non-intervention (e.g., in the exchange markets)" (Bergsten 1982, 5). In response Bergsten called for a macroeconomic package that would amount to "a reversal of almost 180 degrees from the approach of the past two years" (Bergsten 1983, 6).

multilateral liberalization as a constructive alternative to protection was only partly successful—it deflected traditional demands for protection more effectively than the growing demands for export activism backed by threats of market closure. Clearly, the results would have been worse had there been no GATT negotiations. Nevertheless, the decade of the 1980s saw increasing pressure in the United States for discriminatory and GATT-inconsistent trade protection such as the "voluntary export restraints" (VERs) on products such as steel, machine tools, and automobiles, negotiated with Japan, South Korea, Taiwan, and other countries (Destler and Odell 1987).

The Institute response was threefold: first, establish the linkage between macroeconomics and the political economy of trade policy; second, make explicit the costs of protectionist measures; and third, support TAA for those adversely affected by international trade. Making the costs of protection explicit initially took the form of analyses of the impact of protection in particular US industries or sectors (Hufbauer, Berliner, and Elliott 1986; Cline 1987), a research program that eventually broadened to produce economywide estimates of the costs of protection in the United States and other major participants in the international trade system (Hufbauer and Elliott 1994; Sazanami, Urata, and Kawai 1995; Kim 1996; Zhang, Zhang, and Wan 1998; Messerlin 2001). And if quantitative nontariff protection was to be granted, it would be better to do it in the form of "auction quotas," which would reduce the attractiveness of quantitative restrictions to both importers and exporters and ensure that the resulting quota rents were captured by the public treasury, not private interests (Bergsten 1975b, Bergsten et al. 1987). At the same time the Institute was making the costs of protection explicit, it was also producing proposals to aid the adjustment of those adversely affected by the expansion of international trade (Hufbauer and Rosen 1986).

In addition to this four-pronged approach—address the underlying macroeconomic issues, provide a constructive multilateral alternative to protection, publicize the costs of protection, and advocate support for those adversely affected by trade—the 1980s saw the launching of a new development that arguably shaped the subsequent evolution of the international trade system profoundly.

Throughout the postwar period, US trade policy, with the GATT as its centerpiece, had been fundamentally global and nondiscriminatory in its orientation. Exceptions were relatively minor: The United States and Canada had a special agreement with respect to automobile trade, the United States maintained a modest program of duty-free access for some developing-country exports (under the GATT's generalized system of preferences), and it had occasionally imposed special, discriminatory protection, most often in textiles and apparel or against Japanese exports.

In the 1980s, however, the US concluded free trade agreements with Israel (1985) and Canada (1988). The Israel agreement was driven primarily by foreign policy considerations (Rosen 1989). The negotiations with Canada were launched in the wake of a failed 1982 GATT ministerial, partly as a gambit to spur the launch of what became the Uruguay Round (Bergsten 1991), and the Institute published studies supportive of the FTA (Wonnacott 1987, Schott and Smith 1988).

Arguably, neither the Israel nor the Canada deals had major systemic implications (though the trade negotiations agenda was expanded with the inclusion of services in the Canadian agreement). The picture began to change, however, when the US-Canada agreement was expanded to include Mexico. The initiative came from the Mexican side, and the receptive US response was justified as much or more by foreign policy interests as by economic considerations per se. Yet the North American Free Trade Agreement (NAFTA) was precedent setting inasmuch as it represented the first free trade agreement between large developed and developing countries, and thereby greatly broadened the realm of possible preferential deals. Again, the Institute published generally positive evaluations of the prospective NAFTA agreement (e.g., Hufbauer and Schott 1992, 1993; Martin 1993) and its subsequent performance (e.g., Hufbauer et al. 2000, 2005). This favorable finding was to be replicated when additional preferential agreements came onto the US trade policy agenda, with Institute studies typically concluding that the free trade agreement under consideration would contribute positively to US and global welfare (Schott 1989a, 1989b, 2004).

On the US side, NAFTA was partly motivated by frustration over the slow pace of the Uruguay Round negotiations (Schott 1990). It was hoped that the demonstration that the US could pursue preferential arrangements as an alternative to the GATT system would encourage a more forthcoming negotiating stance on the part of its Uruguay Round partners, most importantly the European Union. When NAFTA did not have the intended strategic effect, Bergsten seized on the embryonic Asia Pacific Economic Cooperation (APEC) forum as a means of upping the ante. Chosen to head its newly minted "Eminent Persons Group" in 1992, Bergsten presented the group's first report to the region's assembled heads of government at Blake Island, WA, in October 1993 and effectively authored APEC's "Bogor Declaration," establishing a commitment the following year to a phased freeing of trade under the organization's "open regionalism" mantra (Bergsten 1995). The sight of the leaders of countries representing nearly half of world output meeting in the US undoubtedly concentrated European minds, and the Uruguay Round agreement was concluded in December 1993 and signed the following year. APEC has subsequently failed to live up to its initial promise, at least in terms of trade liberalization.[9]

9. Although the members of APEC do not appear likely to achieve the Bogor goals of trade liberalization, the organization has played a useful role in facilitating trade. Among the Institute publications addressing these issues have been Funabashi (1995), Wilson (1996), Bergsten (1997), Dua and Esty (1997), and Mann and Rosen (2002).

The Reagan-era macro policy mix had set in motion the mobilization of protectionist interests in the United States that the Reagan administration and its successors resisted with mixed success, and the repercussions were felt beyond the ambit of traditional trade negotiations, global or preferential. One such development was the increasing transpacific orientation of US trade and investment patterns, primarily centered on Japan but also including economies such as South Korea and Taiwan (together with Hong Kong and Singapore dubbed the newly industrializing countries or NICs). The shift away from the traditional transatlantic focus of US trade policy was important, in that a number of these economies were pursuing distinctive development strategies embodying a high degree of state intervention, conducted in a legal and cultural milieu that presented new challenges to US policymakers used to operating in the more familiar European environment (Noland and Pack 2003).

Bergsten's initial response to the increasingly acrimonious US trade relations with Japan was to emphasize the macroeconomic roots of America's trade deficit, both globally and with Japan, and to resist demands for protection (Bergsten and Cline 1985). But this stance was inadequate to deal with the growing demand for trade policy activism aimed at opening foreign markets—as distinct from import relief—and the growing US-Japan rivalry in a number of high-technology industries. As the decade wore on, Institute studies beginning with Balassa and Noland (1988) started examining Japan's economy in greater depth, highlighting the possible impediments to market access for foreign suppliers that its distinctive institutions might pose and providing some of the intellectual bedrock for the George H. W. Bush administration's Structural Impediments Initiative negotiations with Japan.

This reexamination reached its apotheosis in the early 1990s, with three Institute studies. One was by Laura Tyson (1992), who would head the Council of Economic Advisers and then the National Economic Council in the first Clinton administration, on trade policies for high-technology industries. Then followed the studies of US-Japan relations by Bergsten and Noland (1993) and of the roles of reciprocity and retaliation in US trade policy by Bayard and Elliott (1994). Commissioning the first study could be interpreted as an attempt to reach out to heterodox thinkers in the profession whose ideas, such as voluntary import expansions, while untested, were finding a receptive audience among policymakers, and to subject these analyses to more rigorous examination. The second represented a growing realization that in certain respects the Asian countries did pose new challenges calling for new thinking, while the third attempted to assess in greater specificity US experience with aggressive export promotion, finding resonance in the 1993 Framework Agreement between the United States and Japan. Bergsten himself embraced the old verities (macroeconomic policy adjustment), the emerging new "behind-the-border" orthodoxy (the need for international antitrust policies, harmonization of tax policies), and even the new "managed trade" solutions (infelicitously dubbed in congressional testimony "involuntary import expansions" or IIEs) in a quest to manage the relationship to forestall protection and maintain competitive markets (Bergsten 1990, 1993). As he explained it,

> When neither of the preferred options [removing explicit barriers or applying antitrust policy] is available and it can be demonstrated persuasively that access to the Japanese market is artificially hindered, it may be necessary to seek Japanese agreement to temporary use of quantitative measures of increased penetration—to manage the trade in a way that will unmanage the market. I have no philosophical problem with such efforts: they expand trade, expand the number of participants in the targeted market, increase competition, reduce prices and reduce cartel activity. They bear no resemblance to traditional protection—which closes markets, reduces the availability of the product, raises prices and creates or shores up cartels. (Bergsten 1993, 6–7)

Eight years later, Bergsten, Ito, and Noland (2001) closed this cycle, after a decade of considerable policy reform in both the United States and Japan, a period of strong US and weak Japanese economic performance (in stark contrast to Japan's strong performance during the prior decade of the 1980s), and at least some degree of institutional convergence in the two economies. The title of their book, *No More Bashing*, signaled the abandonment of extraordinary asymmetrical measures to force the opening of Japanese domestic markets. Bergsten would eventually propose a free trade agreement between the two countries (Bergsten 2004).

Although much of the focus was on Japan, during the second half of the 1980s Bergsten and the Institute began to grapple with the NICs, publishing Balassa and Williamson's (1987) examination of their exchange rate policies, followed by Noland (1990) examining the economic prospects not only of the NICs but of the rising economies of Southeast Asia as well. The Institute hosted prominent visitors from South Korea, and the research program began delving more deeply into Asian regional integration, with Bergsten offering a steady stream of commentary (e.g., Bergsten 1989).[10] Since then the Institute has published a multitude of Korea-related publications and easily has the most active Korea-related program of any think tank outside that country.[11]

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10. One of the visiting scholars, Cho Soon, returned to South Korea and became the deputy prime minister and later governor of the central bank; as deputy prime minister he established a government think tank, the Korea Institute for International Economic Policy, modeled on the Institute for International Economics. Another South Korean visitor, Il SaKong, founded a private institution, the Institute for Global Economics, also inspired by the Institute.

11. A partial recitation of this output would include Bayard and Young (1989), SaKong (1993), Cho (1994), Bergsten and SaKong (1995, 1996, 1997), Noland (1998, 2000, 2004), Choi and Schott (2001), Bergsten and Choi (2003), and Graham (2003).

Plus Ça Change, Plus C'est la Même Chose?

A well-known witticism variously attributed to both Karl Marx and Oliver Wendell Holmes (!?) alleges that history repeats itself, first as tragedy, then as farce. In certain respects, the current international economic situation resembles that facing Bergsten during the Institute's early years. The second Clinton administration saw a lapse in presidential "fast-track" trade negotiating authority (Destler 1997) and a surge in antiglobalization sentiment. At the same time, the inclusion of environmental (Esty 1994, Hufbauer et al. 2000) and labor (Elliott and Freeman 2003) considerations, and the option of pursuing trade liberalization on a preferential basis, lengthened and complicated the trade liberalization agenda (Destler and Balint 1999, Destler 2005).

In a number of respects, the reactions of Bergsten and the Institute (Bergsten 2000, Bergsten and the Institute for International Economics 2005) echoed their responses to similar situations two decades earlier. A primary response was once again to get the bicycle rolling, supporting the launch of the Doha Development Round of trade negotiations under the auspices of the World Trade Organization, the successor to the GATT created by the Uruguay Round Agreement (Schott 1998, 2000; Bergsten 2002; Elliott 2006; Hufbauer and Schott 2006). In this connection, to publicize the magnitude of the accomplishments to date, and to flag the potential future gains that remained to be harvested, Bergsten commissioned research by Institute scholars to estimate the impact of globalization on the US economy. This effort yielded an estimate of approximately $1 trillion in annual benefits to the US economy and a "conservative" estimate of another half trillion dollars in potential additional gains (Bradford, Grieco, and Hufbauer 2005). Meanwhile, analyses of globalization in information technology by Catherine L. Mann responded to anxieties about offshoring of jobs (concerns that peaked during the 2004 presidential campaign) and highlighted potential US gains from further liberalization of markets for services (Mann 2005, 2006).

A second response was to focus on the underlying macroeconomic roots of politically sensitive balance of payments disequilibria, as well as the recurrent financial crises of the 1990s that were fueling antiglobalization sentiment in many parts of the world (Bergsten and Williamson 2003, 2004; Cline 2005). As was the case 20 years earlier, these imbalances centered on the United States and a rising Asian power—in this instance, China. In policy terms, addressing the issue required macroeconomic adjustments, including changes in exchange rate policies, and analytically it meant devoting resources to the examination of an institutionally distinct economy (Lardy and Goldstein 2004, Lardy 2005, Bergsten 2006, Bergsten et al. 2006).

A third tack was to again deal constructively with domestic adjustment issues created by trade, this time as part of a broad "globalization balance sheet" project directed by J. David Richardson (Richardson 2005, forthcoming; see also Kletzer 2001, Scheve and Slaughter 2001, Kletzer and Rosen 2005). Another response familiar from the earlier period was to bring heterodox thinkers into the big tent (e.g., Rodrik 1997).

One big difference this time around was the availability of the preferential (and/or regional) alternative to global liberalization. In Bergsten's eyes, the attraction of the preferential alternative was purely instrumental: Such agreements took less time to negotiate and permitted bolder action than obtainable through the global system (Bergsten 1996a). Yet he also acknowledged the "fundamentally superior" nature of the global approach, potential tension between the two alternatives, and the need to harness regionalism to constructive multilateral ends. Used constructively, this "creative tension" and "dynamic interaction" could be used to propel the global system forward. However, without "determined leadership" to move forward on the global front, "then regionalism will not only fill the vacuum . . . but it will take place in the absence of any effective multilateral framework and that could lead to fears that many have expressed over the years that regionalism will drive the world apart rather than move it together" (Bergsten 2000, 5). The Institute would subsequently produce a plethora of mostly supportive analyses of preferential arrangements, while continuing to support the successful completion of the Doha Round.

Echoing the endgame tactics of the previous Uruguay Round, Bergsten argued that credible movement toward "megaregional" integration (probably via APEC) was a necessary catalyst to bring the Doha Round negotiations to a successful close; indeed "it may be the only tool available to bring Doha back to life" (Bergsten 2005, 23).[12] Failing that, the United States could try to force the issue through promiscuous invitations to bilateral preferential integration.[13]

Complementing this expanding substantive agenda were innovations in outreach, principally through the increased use of the Internet and shorter publication forms. In 1998 the Institute inaugurated a "policy brief" series, publishing approximately nine per year, along with a similar number of more technical "working papers." In addition, Institute scholars are widely cited in the press and continue to testify before Congress, as they have throughout the organization's existence. Bergsten himself is perennially the most widely cited think tank economist in the United States, and other Institute scholars regularly place in the upper reaches of the citation counts (Trimbath 2005).

12. A partial listing of these publications would include Feinberg (1997), Frankel (1997), Choi and Schott (2001), Pastor (2001), Schott (2001), Scollay and Gilbert (2001), Lardy and Rosen (2004), Schott (2004), Galal and Lawrence (2005), and Hufbauer and Baldwin (2006).

13. C. Fred Bergsten, "Plan B for World Trade: Go Regional," *The Financial Times*, August 16, 2006.

Looking Ahead: Will the Same Patterns Persist?

As the Institute celebrates its 25th birthday, and Bergsten his 65th, both can look back with pride. The relationship has been serious and comprehensive, both in intellectual and practical terms. The impact has been impressive, indeed enviable.

Will the same themes prove appropriate for the next quarter century? At present, the United States is in the midst of a natural experiment testing Bergsten's two signal theses—the trade bicycle and the exchange rate. The global Doha Round talks have adjourned without agreement and with dubious future prospects. The US trade imbalance (driven in part by exchange rate misalignment) is at an astronomical level, with the nation importing over $9 in goods for every $5 it sells overseas. These should be generating, by the logic set forth here, an enormous protectionist backlash.

Thus far, this backlash has not occurred. There is, to be sure, heightened concern over China—the persistent 6-to-1 bilateral trade imbalance and its undervalued exchange rate. There have been some import safeguards imposed, and a bilateral textile agreement negotiated—both within the framework of that nation's WTO accession agreement. And there is a broad antiglobalization movement. But the latter is rooted in social concerns as much as economic interests. Most important, the business-generated protectionism that characterized the early 1970s and the early and mid-1980s in the United States is conspicuously absent, though organized labor is still as, or even more, protectionist and resistant to globalization.

This could be a long-term change. One of us has argued elsewhere that the globalization of US business has made a pure protectionist position very difficult for the great majority of firms and sectors to sustain—they are simply too dependent on trade (needing imports for inputs as much as or more than exports, in many cases). For example, the once formidable textile-apparel coalition has crumbled as apparel makers moved offshore and cloth producers concluded that they could not build their futures on the US market alone. Rent-seeking demands on trade policy continue to exist, but they have taken different forms. So, for example, the mills shifted from protectionism (the Multi-Fiber Arrangement, which expired in 2005) to bilateral FTAs with rules of origin requiring lower-wage clothing producers in partner nations to use US cloth as a condition for barrier-free access to the US market—in effect a local content requirement for imports (Destler 2005, chapter 9)!

Labor cannot, by definition, globalize to the same degree, and open trade policy remains vulnerable to the charge that the gains have not been broadly shared. Still, it was business firms producing at home with domestic inputs for the home market, not organized labor, that were the backbone of historic US protectionism. The overall movement of US business into the internationalist camp is thus an important, arguably durable structural shift that may render the trade bicycle less unstable and the trade-political balance less vulnerable to exchange rate misalignment. These trends may have been further reinforced by the currency hedging strategy implicit in the global dispersion of production facilities by multinational corporations.

However, this relatively benign outcome is facilitated by two conditions—one political, one economic, and both subject to change. Today's congressional acquiescence on trade policy is a product, in part, of Republican control of both the presidency and both Houses of Congress. If the country were to return to the "divided government" that characterized the 1980s, partisanship could contribute to an intensification of congressional intervention (though it also could drive the administration to take the Democrats' concerns seriously).

The other condition that may well have contributed to the relatively benign outcome observed to date has been the generally robust macroeconomic performance of the US economy. Should the US economy experience a noticeable slowdown or recession—especially if associated with external disruptions such as a hard landing of the dollar—then pressures for trade restrictions could multiply. Once again, Bergsten dramatizes the threat:

> It's not pretty to contemplate US trade policy, and hence the global trading system, in a year or two if US growth slows sharply and joblessness rises while our global trade deficit exceeds $1 trillion and the bilateral imbalance with China rises to $300 billion to $400 billion. The fact is that the US external deficits are unsustainable, and they would be even if the rest of the world were willing to finance us indefinitely. (Bergsten 2006a)

If this scenario eventuates, we will enter terra incognita, political as well as economic.

The potential downside risk embodied in this scenario is reinforced, as earlier noted, by the official July 2006 "suspension" of the Doha Round negotiations and the possibility that it will be the first global trade negotiation since the establishment of the GATT to fail. Such an outcome could lead to an erosion of multilateral discipline, a drift toward greater trade discrimination, and the formation of competing rival blocs.

If the world does move in that direction, we hope Bergsten will conjure up ways to limit the damage.

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