



# Rebuilding the Global Economy

*A series outlining policy priorities and solutions*

MEMORANDUM ON

## THE FUTURE OF EUROPEAN TRADE POLICY

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**To: The European Commissioner for Trade**

**From: Robert Z. Lawrence**

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**Background:** The announced intention of President-elect Joe Biden to strengthen US alliances and participate in international institutions offers an opportunity for the European Union to set its global trading strategy on a new path by reinvigorating the US-EU trade relationship, revitalizing the World Trade Organization (WTO), and implementing a coordinated response to the systemic problems presented by Chinese policies.

The European Commissioner for Trade should not, however, naively expect that the new administration will place trade policies at the top of its agenda and automatically eliminate the bilateral conflicts caused by the Trump administration. Nonetheless, the European Union has an opening to encourage the Biden team to move in that direction.

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### KEY PRIORITIES

#### **PRIORITY 1: Restore the US-EU trade relationship**

The European Union should try to rapidly restore the status quo ante-Trump on a group of issues, consistent with broader Biden administration goals, rather than seeking big wins that challenge US principles.

- A standstill agreement on authorized retaliations in the Boeing-Airbus subsidy cases could permit the United States and the European Union to negotiate an agreement patterned after the Organization for Economic Cooperation and Development (OECD) code for export subsidies that would allow subsidies for aircraft development but within defined limits. An exception would be no limits on subsidies for green fuels and technologies for aircraft.
- The US-EU frictions over steel and aluminum should concentrate on problems of excess capacity rather than alleged national security concerns between allies. The administration should be ready to remove steel and aluminum national security tariffs on EU products and simultaneously announce new steel and aluminum procurement plans for infrastructure and clean energy programs. In return, the European Union should eliminate its retaliatory tariffs and increase its NATO contributions. Both sides should use the WTO subsidies code to challenge practices leading to excess capacity emanating from China and other countries.
- Europe and the United States should relaunch their initiative to cooperate on regulations and standards, including mutual recognition of those deemed to be

equivalent, with emphasis on transportation, health, and renewable energy. The new EU-US Trade and Technology Council should be equipped to deal with challenges in quantum computing, 5G and 6G broadband cellular networks, artificial intelligence (AI), big data analytics, biotechnology, and nanotechnology.

- Setting compatible standards should also involve international standard-setting bodies, with a goal of opposing efforts by China and others to use standard setting to gain a competitive advantage. Agreements to bolster supply chains in health and strategic minerals should also be negotiated, with the goal of preserving open trade rather than self-sufficiency. Bilateral understandings on rules for ecommerce can pave the way for new agreements on data use, cybersecurity, nonlocalization, and privacy rules.
- Both parties should avoid taxes on internet transactions by agreeing to OECD rules. In light of the incoming Biden administration's proposals for minimum taxes on corporations and a US return to the OECD negotiations on base erosion and profit shifting (BEPS), France should postpone its planned digital tax measures.
- Implementing climate policies should not violate WTO rules. Border adjustments could be justified by GATT Article XX as necessary to protect "human, animal or plant life." But such adjustments would not be necessary if countries apply market-based climate policies such as taxes or tradable CO<sub>2</sub>-emissions permits. Under the principle of national treatment, foreign firms could be given offsetting credits for permits they have purchased or taxes they have paid in their home countries.
- Any overly ambitious goal such as the Transatlantic Trade and Investment Partnership (TTIP) should be placed on the back burner.

## **PRIORITY 2: Revitalize the WTO with Appellate Body reform, plurilateral agreements, and new rules**

The European Union should lead efforts to reform the WTO to strengthen its role in dispute settlement and rules setting. A first step would be persuading the United States to join the consensus in appointing Ngozi Okonjo-Iweala as the next WTO Director-General.

- **Reform the Appellate Body (AB).** The European Union has led by establishing a temporary alternative to the AB, but the impasse over the US refusal to fill vacancies at the AB remains unresolved, making an effective alliance to challenge unfair foreign practices difficult to achieve. The Biden administration should therefore accept reform proposals responsive to US concerns over AB overreach, intrusion in administration of trade remedies, and inefficiency.
- **Allow plurilateral agreements.** The WTO should be a forum with a variable geometry that can accommodate the wishes of members who seek deeper trade agreements that not all members wish to join. Members should all have the right to negotiate and join such agreements, but to prevent free riding, these agreements should not automatically be extended to all members on a most favored nation basis. The European Union should help launch plurilateral agreements on issues that are standard in US and EU regional agreements, such as investment, services, ecommerce, and labor standards. Agreements on environmental goods, pharmaceuticals, and medical supplies should also be pursued.
- **Reform safeguards.** Safeguard protections, which allow countries to impose temporary trade barriers when injury can be proven, can play a vital role as a buffer that prevents finger-pointing about unfair trading practices. Both the United States and the European Union have been unable to implement safeguards that can survive WTO challenge,

however. A new more workable safeguards agreement would eliminate ambiguous language and allow selective responses in cases where injury is caused by imports from one country.

- **Reform subsidies.** Some of the groundwork for expanded WTO rules on subsidies has been laid out in the agreement reached by the European Union, the United States, and Japan. After resolving their remaining differences, this agreement should form the basis of an expanded WTO subsidies negotiation. If these negotiations fail, an enhanced plurilateral subsidies agreement can be negotiated.

### **PRIORITY 3: Coordinate policies toward China**

A joint US-EU approach to China should steer realistically between the extreme decoupling sought by the Trump administration and the inadequate responses to harmful Chinese practices in the past. Efforts to prevent China's rise are likely to fail and prove counterproductive. Similarly, China is very unlikely to abandon its successful state-led system. In addition, China will continue to increase in importance as a market for many foreign firms and to be a key participant in global value chains. Although excessive Western dependence on China raises risks of opening opportunities for technological and trade blackmail, mutual interdependence is a better cement for peaceful interactions than acrimonious efforts at extreme separation.

- China's trading partners should use improved WTO rules and a restored Appellate Body to challenge China's practices of violating intellectual property rights, forcing technology transfers, employing poorly disclosed subsidies, and generating excess capacity in international markets.
- China's market remains largely closed to foreign investors in key areas, despite long inconclusive negotiations over bilateral investment treaties. A joint US-EU policy should deny China foreign investment and technology acquisition opportunities in industries and technologies in which they do not provide reciprocal benefits to foreign firms.
- Where there are genuine national security and strategic threats, the European Union should also work with other countries to strengthen procurement restrictions and implement coordinated export controls on sales of products and technologies to China. The European Union should promote the selective approach it used with Huawei, which involved avoiding purchases of network products that pose national security risks but buying other products that do not.

### **NOTES OF CAUTION**

Both the United States and the European Union will need to bolster domestic support for trade policy. President-elect Biden will be hindered by the legacy of the unilateral measures undertaken by the Trump administration that gained considerable support domestically. Before rolling back tariffs, he will need to point to offsetting benefits. The EU challenge is achieving a unified strategy to resist China's efforts to employ tariffs and incentives (infrastructure projects) to dilute common EU policies. The European Union also needs to monitor the actions of the Biden administration and be willing to challenge US "Buy American" measures that are not WTO-consistent. The same would apply to proposed US tax policies, especially those that discriminate in favor of domestic manufacturing production.