

ONE ISSUE TWO VOICES

BUY AMERICAN / BUY CANADIAN: The New Protectionism?

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INTRODUCTION Drawing on expertise from both sides of the Canada-U.S. border, the *One Issue, Two Voices* series is designed to stimulate dialogue on policy issues that have a significant impact on the bilateral relationship. This twelfth issue in the series examines the impact of the U.S. economic stimulus measures designed to generate employment stability in the aftermath of the greatest financial crisis since the Great Depression. Authors Robert Baugh, executive director of the AFL-CIO Industrial Union Council, and William Robson, president and CEO of the C.D. Howe Institute, are leading international public policy experts. Together they weigh in on the debate over the Buy American procurement provisions included in the 2008 *American Recovery and Reinvestment Act*. Each author expresses starkly different opinions on the accusations of protectionism triggered by Buy America. Baugh argues that Buy America is not protectionist but a response in part to global demands for U.S. stimulus investments and carbon emission reductions. He maintains that, while recent bilateral negotiations have addressed



immediate concerns about protectionism, the spat over Buy America has much wider implications. The unregulated free market / free trade policies have failed American workers and their communities, just as they have undermined U.S. industrial and innovation capacity. Baugh also contends that Buy America has a much larger context directly related to climate change. The response to the U.S. effort to achieve environmental and economic goals portends the difficulties ahead, as all countries seek to invest in their economies to create jobs and to cut carbon emissions. Baugh says it is time to drop the “win-win-free trade hype” that has proved to be false and to face the reality that current trade policy has become a vehicle to offshore and outsource good jobs. He stresses that urgent action is needed for a rebalancing of trade, as the United States and Canada find themselves stumbling toward an industrial and manufacturing strategy in a world where all our competitors have one.

In contrast to Baugh’s position that protectionism in the form of Buy America is vital to foster economic growth and promote job creation, William Robson makes the classic case for freer trade. He explains how the pro-free trade view turns the language of winners and losers on its head, with taxpayers and consumers of public services benefiting when their governments source the best and best-priced products wherever they originate. His main argument is that discrimination in government procurement policies

in the name of Buy America or Buy Canada, like all other protectionism, hurts those who raise the barriers. Robson maintains that his rationale for open borders holds true in both booms and busts. Confidence and macroeconomic management, not barriers or subsidies to trade, determine the level of output and jobs. He says that the same argument applies to discrimination against foreign or out-of-state / out-of-province suppliers. In the struggle to maintain open borders, he says, the most crucial battle may be the one at home. Both authors agree that the recently negotiated Canada-U.S. deal on procurement has addressed immediate concerns about Buy America, but they also concur that hard times foster economic nationalism and that, despite recent signs of growth, myriad challenges to prosperity lie ahead.

The Canada Institute thanks the authors for their provocative and cogent analyses of a contentious issue in the ongoing bilateral dialogue. We are grateful to the late C. Warren Goldring and AGF Management for their support for this series, and to *Canadian Business* magazine for its support of this issue.

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ECONOMIC REALITY AND ALARMIST RHETORIC: GETTING REAL ABOUT BUY AMERICA

In the midst of the greatest financial crisis since the Great Depression, the U.S. Congress passed the \$787 billion *American Recovery and Reinvestment Act (ARRA)*, and President Barack Obama signed it into law. The Buy America provisions contained within the *ARRA* drew an immediate response from Canada, the European Union, China, and other countries that condemned the provisions as “protectionist,” claiming they would “lead to retaliatory measures” and even “trade wars.” These alarmist reactions need to be seen for what they really are—warning signs about everything that has gone wrong with trade and economic policy. It is time to step back and use this response as a learning moment—to come to grips with the manufacturing crisis, a dangerously unbalanced trading system that is out of step with economic and political reality, and the potential conflict over climate change.

THE RECOVERY ACT AND BUY AMERICA

As both the U.S. and the international economy imploded in 2008, the American Federation of Labor and Congress of Industrial Organizations (AFL-CIO) and the Canadian Labour Congress joined unions across the world to urge their governments to move aggressively on economic stimulus measures designed to generate employment stability. In the United States the AFL-CIO worked with Congress and the Bush and Obama administrations to support the largest stimulus investment in our history. The *ARRA* investments are designed to be the leading edge of a new environmental economic development policy designed to reduce carbon emissions and create good jobs. To ensure, as U.S. taxpayers have every right to expect, that public dollars are recycled to maximum effect in the U.S. economy, Congress included Buy America language in the Act.

The language reaffirms and strengthens existing well-established legal precedents, dating back to the *Buy*

American Act of 1933. The Department of Defense has had Buy America provisions since 1941, and the Federal Highway Administration, Federal Transit Administration, and Federal Railroad Administration all have long-standing provisions. The *ARRA* Buy America requirement simply states that, for the publicly funded projects, “all of the iron, steel, and manufactured goods used in the project[s] are produced in the United States.” It also allows for reasonable waivers.

Most notably, the *ARRA* requires that the Buy America provision be “applied in a manner consistent with U.S. obligations under international agreements.” It is important to note that negotiated trade agreements allow for domestic preferences under a number of circumstances. These preferences were negotiated for a reason, and they are all perfectly legal. The United States would be irresponsible not to use them to the fullest extent possible, just as Canada and our other trading partners do.

THE POT CALLING THE KETTLE BLACK

While Canada, the European Union, and China have been vociferous critics of the Buy America provision, each one of them has its own far-reaching domestic preferences. China, which is not a member of the World Trade Organization (WTO) Government Procurement Agreement (GPA), can discriminate against imported products in its \$586 billion economic stimulus package, and, in addition, it has imposed an 80 percent domestic content requirement. The EU and its member states are GPA members but have excluded significant sectors from coverage, including all federal and sub-federal transportation, telecommunications, and energy contracts. They are therefore free to discriminate against imported goods in these government projects.

Canada is also a GPA member, and it has excluded significant sectors from coverage—even broader exceptions

than those claimed by the United States. For example, Canada excluded shipbuilding and repair, urban rail and urban transportation equipment systems and the components and material incorporated therein, as well as all project-related materials made of iron and steel; all contracts for communications equipment; and, at the provincial level, all procurement of steel, motor vehicles, and coal. With regard to the procurement of construction services, Canada also excluded dredging and all construction service contracts tendered on behalf of the Department of Transport.¹

So, what is all the fuss about? The Buy America and the EU and Canadian provisions are all legal and covered under the GPA. In fact, the Buy America policy rewards other nations with reciprocal government procurement agreements by exempting them from certain restrictions. Ironically, Canada did not have a reciprocal relationship with the United States because it had failed to bind its provincial procurement under the GPA. When the crisis hit, it was obliged to enter into negotiations to find a solution.

What is more telling is the reaction that the U.S. provision elicited from our trading partners. Why does an economically and politically sensible action generate such heat, and, if it is legal under the precepts of a negotiated trading system, why is it branded “protectionist”?

PROTECTIONISM AS A PEJORATIVE

The charge of “protectionist / protectionism” has become a pejorative label applied by free-market / free-trade advocates against any contradictory view. It is used to cut off debate by defining an opponent’s point of view in a negative light. U.S. and Canadian trade unionists, businesses, and economists know well what it feels to be stigmatized in this way. It does not matter that we believe in fair, balanced, and smart trade. Every time an objection or a question is raised about trade policies or agreements pursued by government, multinational corporations, and financial interests which undermine labor, economic, environmental, and other standards, the labeling begins. At times it borders on the absurd. The barrage of protectionist accusations in response to a decision in a trade case filed by the United Steelworkers Union is a good example.

In this case, a Chinese government representative charged at an international meeting held by the Carnegie Institution in Washington, D.C., that the decision imposing tariffs on its tires was protectionist. A number of diplomats present made similar comments. A U.S. union representative responded by pointing out that the decision was based on the illegal actions of the Chinese government—as determined by the independent U.S. International Trade Commission. He explained that the Chinese government’s own testimony revealed how it required a new Cooper tire plant in China to export all its first five years’ production, with the U.S. market as its primary target. The diplomats at the meeting then agreed that the Chinese actions violated WTO rules, though many of them still insisted that the United States was somehow being protectionist. The reactions to Buy America provisions are only the latest example of labeling without supporting facts or context.

The *ARRA* is not protectionist. In part, it is a response to worldwide demands for U.S. stimulus investments and carbon emission reductions. It included spending \$150 billion over two years on infrastructure projects. Excluding construction and other costs, the actual figure spent on U.S. manufactured goods as a result of Buy America will be much smaller. This amount pales in comparison to the total two-way U.S. trade in goods and services in 2008 of \$4.4 trillion, or the \$2.5 trillion worth of goods and services that the U.S. purchased from the rest of the world. It also pales in comparison to the \$600 billion of trade in 2008 between the United States and our number one trading partner, Canada.²

When the United States runs a goods balance of payments deficit of \$840 billion (including a \$144 billion deficit with Canada and Mexico), as it did in 2008, any charge of protectionism rings hollow.³ Chinese accusations of U.S. protectionism seem Orwellian given the 80 percent domestic content requirement in their own stimulus investments and their recently instituted “indigenous innovation” rules designed to capture foreign technology.⁴

What should raise far more concern on both sides of the U.S.-Canadian border are the state of U.S. manufacturing, the trade deficit, and the behavior of the Chinese government. The implications of each of these factors are far more important than Buy America to the future of our mutual economies.

American manufacturing jobs and capacity are being lost at an alarming rate. Between 1998 and 2009, more than 57,000 manufacturing establishments closed. Since 1998, the United States has lost one-third of its manufacturing jobs—more than 6 million in all.

A CROSS-BORDER CRISIS

The economic integration of the United States and Canada and their shared policy interests can be seen in the level of two-way trade between them—most obviously in the automotive sector. More than 20 percent of U.S. manufacturing is tied to an industry where capacity crashed from 17 million cars to 10 million in annual sales in less than two years. As a result, Michigan and Ontario's cross-border trade (half auto-related), which peaked at \$8 billion in September 2007, plummeted to \$3 billion by June 2009, and unemployment skyrocketed.⁵ With GM and Chrysler in bankruptcy, the U.S. and Canadian governments were faced with a tough choice: Do we still want an automotive industry?

Thankfully, for millions of workers and communities, the United States, Canada, the United Auto Workers (UAW), and the Canadian Auto Workers (CAW) all stepped up, ignoring the free-market fundamentalists who said, "Let them fail." Today General Motors is a public corporation owned by the U.S. Treasury (60.8%), the employees' agent (17.5%), the Canadian government (11.7%), and the old GM's bondholders (10%). The restructured Chrysler (not a public company) has four owners: the U.S. Treasury (9.9%), the employees' agent (67.7%), Fiat (20%), and the Canadian government (2.5%).⁶

Other countries around the world also made similar "protectionist" choices, but they have been making comparable strategic policy choices in support of a manufacturing strategy for decades. While the auto sector serves as a specific example of our cross-border integration and crisis-driven industrial policy decision-making, it is just the tip of the iceberg.

The United States and Canada are both nations without clear industrial development policies or manufacturing

strategies in a world where all our other competitors have one. The consequences have been wage stagnation, spiraling trade deficits, and job loss. Canada is not immune from the contagion. The economic crisis has created a situation that finds both countries stumbling toward an industrial policy. The dire situation in American manufacturing is bad news for both countries.

THE CRISIS IN AMERICAN MANUFACTURING

American manufacturing jobs and capacity are being lost at an alarming rate. Between 1998 and 2009, more than 57,000 manufacturing establishments closed.⁷ Since 1998, the United States has lost one-third of its manufacturing jobs—more than 6 million in all. Two million of those jobs were lost in the current recession that began in December 2007. At the end of 2009, U.S. manufacturing employment hit 11.63 million, the lowest figure since 1941.⁸ Two-thirds of those who lost their jobs were skilled production workers, and a significant portion of the rest were engineers, scientists, designers, managers, software specialists, and industrial machine installation/repair workers—all in occupations critical not only to the operation of production systems but to product and production innovation.

Manufacturing has declined in real terms. Between 2000 and 2009, manufacturing's share of GDP fell from 14.5 percent to 11.5 percent. Machine tools, the heart of a vibrant industrial base, has seen U.S. consumption decline by 30 percent since 1998.⁹ The greatest economic downturn since the 1930s accelerated a decade-long freefall in manufacturing.

This recession drove manufacturing output down 16.7 percent. The 46.1 percent decline in real automotive

output is a big part of the problem, but it runs across the spectrum. Real output during this period is down, 47.4 percent in primary metals (including steel), 27.3 percent in machinery, while information technology (IT), hardware, and chemicals are all down significantly. IT hardware (semiconductors, computers, and telecom equipment) is down 15.8 percent, and chemicals are down by 21.4 percent.¹⁰

Massive job losses and the offshoring of technical capacity are a threat to innovation as an engine for the nation's growth. With few exceptions, product development cannot be geographically separated from production without threatening a firm's long-run ability to innovate, and innovation in high-tech services depends heavily on innovation in high-tech manufacturing.¹¹ The loss of research, design, engineering, and development capacity, along with skilled production workers, means that future investments and innovations are more likely to be made in the economy of another country.

The decline is occurring even in industries that are not labor intensive and in which other highly developed, high-wage countries such as Germany, Japan, and Finland are doing well. The complete loss of U.S.-based industries and U.S. market share makes it clear that the explanation for loss of employment is much more than simple increases in productivity.

The U.S. manufacturing crisis runs in tandem with a decade of deepening trade deficits that have contributed to the decline in manufacturing jobs and wages. The offshoring of jobs, technical capacity, and innovation are a threat to the future of the U.S. and the Canadian economies alike. The continuing failure to address the practices of the Chinese government in world trade imperils both our countries.

TRADING JOBS AWAY

In 2008 the U.S. goods trade deficit grew to a staggering \$821 billion, or \$2.2 billion a day. A \$266 billion deficit with China accounted for 68.6 percent of the manufactured goods deficit. In 2009 the United States ran a \$240.1 billion "all manufacturing" deficit with China. From 2002 to 2009, the United States ran a \$3.7 trillion trade deficit for all manufacturing, including a \$1.6

trillion deficit with China. In all manufacturing, China's share of the U.S. trade deficit rose continually from 28.5 percent in 2002 to 75.2 percent in 2009.¹²

According to the Economic Policy Institute, the growth of trade with China since it entered the WTO in 2001 has had a devastating effect on U.S. workers and the domestic economy.¹³ Between 2001 and 2007, 2.3 million jobs were lost or displaced, including 366,000 in 2007 alone.¹⁴ Research shows that, even when re-employed in non-traded industries, these workers lost an average \$8,146 per worker per year.¹⁵ In 2007 these losses totaled \$19.4 billion.

Canada and Mexico are not immune from the China factor. In 2007 Mexico reported a \$34 billion trade deficit and the closure of thousands of manufacturing facilities. Parts once made in Mexico are now produced in China, then imported for assembly and export. Canada reported a \$32.6 billion deficit with China in 2008, based on a trade profile of raw materials exports and finished goods imports.¹⁶

With an explicit export strategy targeting key industries, sectors, and technologies, China has captured a growing share of U.S. and world markets. It has used a wide array of unfair trade practices, including currency manipulation, export subsidies, widespread suppression of worker rights and wages, and tariff and non-tariff barriers to exports, to support this strategy. The Chinese government has purchased massive volumes of foreign exchange in order to suppress the value of its currency. The unsustainable trade imbalances with the United States and other nations allowed the Chinese government to increase its total foreign exchange reserves by \$453 billion last year, to a total of \$2.4 trillion. The financial crisis has proved to be another opportunity for China to take advantage of the rest of the world by increasing its share of U.S. and other markets for manufactured products.

The United States cannot continue to run trade deficits with the rest of the world and, in the process, destroy its own manufacturing base. There must be a rebalancing, and that requires a vibrant American manufacturing sector producing goods for a domestic and world market. The Buy America provision is a small tactical step in that direction, though it foreshadows much larger concerns.

COMMON PROBLEMS, COMMON SENSE

The economic and environmental challenges the world faces are compounded by trade distortions and market failure. The 2006 *Economics of Climate Change* report by the British government's Stern Commission stated that "Climate Change presents a unique challenge for economics: it is the greatest and widest-ranging market failure ever seen." The 2008 worldwide economic meltdown is another market failure driven by the reckless, unregulated behavior of financial markets and speculation which rewards short-term gain to the detriment of long-term investments in manufacturing. The "win-win free-trade hype" has proved untrue—the hard, cold reality is that current trade policy has become a vehicle for offshoring and outsourcing good jobs.

It is time to drop the free-market and free-trade fundamentalism and to find ways to end global imbalances. The United States and Canada need to focus on how best to revitalize manufacturing, which is responsible for a large share of our innovation and production. Moreover, we must begin fostering jobs again in this difficult business environment.

These concerns are not unique to North America. Workers and governments across the world are focused on the same issues, especially when it comes to climate change. The AFL-CIO and the Canadian Labour Congress are working at home and internationally with the International Trade Union Confederation to promote an environmentally sound economic development agenda—a just transition—in domestic legislation and within an international climate agreement.

A just transition to a greener economy requires an aggressive, sustained commitment of national resources to create and retain good jobs, increase per capita income, modernize industry, develop and deploy technology, and educate and train workers. It requires assistance for any workers, families, or communities that may be adversely affected by the transition, and a democratic voice for workers in their workplaces and their communities.

These are important goals for every country. And it is exactly what they are doing—investing in their

own economies to reduce carbon and create jobs. It is a straightforward economic, political, and environmental common-sense decision. But here's the rub: in the world of free-trade fundamentalism, one nation's investment becomes another's accusation of illegal subsidy and protectionism. As nations move toward massive climate change investments, the reaction to Buy America portends a coming conflict among international environmental, economic, and trade policy.

INVESTING IN OUR FUTURE

The United States faces critical investment decisions on energy and carbon reduction and on infrastructure. The American Society of Civil Engineers estimates that \$2.2 trillion is needed in the next five years to bring aging infrastructure up to date. In the coming decades, climate concerns will drive additional trillions of public and private investment into energy efficiency, carbon reduction, and new energy technologies. Buy America provisions will be part of a fundamental strategic discussion about how we invest in America and the public policies needed to rebalance trade, revitalize manufacturing, develop new industry and technology, and create good jobs. Unions in the United States and Canada know that all these issues are critical.

Ken Neumann, the national director for Canada of the United Steelworkers Union, made this point in an opinion piece published in the *Toronto Star*. He wrote: "Instead of lecturing Americans about the merits of unregulated global trade, Canada should have its own 'Buy Canadian' policy and recognize that, due to the integrated nature of the Canadian and U.S. economies, this current debate in the U.S. is really an opportunity for Canada ... We believe the current challenge for Canada is to develop meaningful policies to support Canadian manufacturing while continuing to be part of an integrated and co-operative North American market. This is an approach that will work for both Canadian and U.S. workers and their economies."¹⁷

The obsession with American protectionism serves as nothing more than a diversion from the real questions that need to be answered. Our workers and communities deserve less rhetoric, more respect, and real answers.

BUY AMERICA PROVISION FROM *THE AMERICAN RECOVERY AND REINVESTMENT ACT*

SEC. 1605. USE OF AMERICAN IRON, STEEL, AND MANUFACTURED GOODS

- (a) None of the funds appropriated or otherwise made available by this Act may be used for a project for the construction, alteration, maintenance, or repair of a public building or public work unless all of the iron, steel, and manufactured goods used in the project are produced in the United States.
- (b) Subsection (a) shall not apply in any case or category of cases in which the head of the Federal department or agency involved finds that—
 - (1) applying subsection (a) would be inconsistent with the public interest;
 - (2) iron, steel, and the relevant manufactured goods are not produced in the United States in sufficient and reasonably available quantities and of a satisfactory quality; or
 - (3) inclusion of iron, steel, and manufactured goods produced in the United States will increase the cost of the overall project by more than 25 percent.
- (c) If the head of a Federal department or agency determines that it is necessary to waive the application of subsection (a) based on a finding under subsection (b), the head of the department or agency shall publish in the Federal Register a detailed written justification as to why the provision is being waived.
- (d) This section shall be applied in a manner consistent with United States obligations under international agreements.

NOTES

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William Robson

BUY THE BEST! THE MESSAGE CANADIANS AND AMERICANS AND THEIR GOVERNMENTS ALL NEED TO HEAR

Canadians and Americans alike must be relieved by recent signs that the 2008–2009 crisis will not precipitate a 1930s-style depression.¹ Both countries' central banks, like their key counterparts abroad, moved aggressively to avert a financial collapse and prop up spending. Crucially, the surge of protectionism that sent the world economy into a tailspin after 1929—the original *Buy American Act* in 1933 being a salient example—had only a muted echo in 2009.

However, as stories about Canadian-made pipes being ripped from the ground in California revealed that same year, advocates of open borders have their work cut out for them.² Government procurement that discriminates against out-of-jurisdiction suppliers is one of the toughest types of protectionism to contain through intergovernmental agreements. Hard times foster economic nationalism, and, despite recent signs of growth, myriad challenges to prosperity lie ahead.

Traditional negotiations and legal arguments alone will not lower barriers and keep borders open to the friendly flow of goods, services, people, and capital. It is also vital to marshal users and consumers on both sides of every border as allies against protectionism. Most important, opinion leaders must remind their compatriots that discrimination in procurement, like all protectionism, hurts those who raise barriers. As taxpayers and consumers of public goods and services, citizens throughout North America should insist that their governments buy the best and the best-priced products wherever they originate.

THE COMPELLING CASE FOR FREE TRADE

Supporters of domestic content rules and other barriers view the arguments in favor of free trade as perverse. They support old-style mercantilism—promoting exports and discouraging imports—and argue that the best way to bolster domestic demand and tide local industries through a slump

is to impede the import of products made elsewhere.

Advocates of free trade, in contrast, say we all do better exchanging with each other rather than each growing our own food, making our own clothing, building our own houses, and doing our own surgery. More subtly, the idea of comparative advantage explains why people do better when they exchange, even if they are more (or less) efficient than their trading partners across the board. Countries will have surpluses in things they are “more better” at, and deficits in things they are “less better” at, as exchange rates adjust to balance overall flows of trade and investment.

This argument holds true in both booms and busts. Confidence and macroeconomic management, not barriers or subsidies to trade, determine the level of output and jobs. A comparison of the list of sick industries in 2010 to those ailing in the recessions of the early 1980s and early 1990s shows just how ineffective temporary prop-ups turn out to be.³

THE EVIDENCE SUPPORTING THE CASE

The case for open borders, which catastrophically failed to carry the day in the 1930s, largely prevailed after the Second World War. Believing that international economic harmony fosters international political harmony, the United States and Canada led multilateral reductions in tariffs and quantitative trade barriers under the General Agreement on Tariffs and Trade (GATT) and the World Trade Organization (WTO). That success supported the arguments for free trade. The world prospered and living standards in outward-oriented regions such as East Asia outpaced those in more closed economies such as South America.

On the Canada-U.S. front, the Canada-U.S. Free Trade Agreement (CUSFTA) of 1988 and the North American Free Trade Agreement (NAFTA) of 1994 marked major successes for the advocates of open borders. Before the slump-induced setback of 2009, Canada-U.S. merchandise trade grew from C\$187 billion in 1988 to C\$603 billion

in 2008, handily outpacing overall economic growth over the period. Scaled to Canadian gross domestic product (GDP), two-way trade rose from 30 to 38 percent.⁴

Complemented by falling transportation and communication costs, this openness changed economic activity in ways that made the flaws of mercantilism and the wisdom of liberalized trade even more obvious. The “imports bad / exports good” mentality is more persuasive when finished goods are being bought and sold—a complete car for cash, say. It is less persuasive when production is increasingly integrated across borders—automotive design and engineering, for example, and components such as engines, doors, and seats.⁵ In the modern world, exchanges of intermediate goods, often within companies, dominate trade: one study estimates that two-fifths of world trade is in intermediate goods; similarly, a recent tally of major Canadian trade commodities put the share of finished goods in imports at less than half, and their share in exports at less than 40 percent.⁶ When so much trade consists of inputs to domestic production, it is clear that protectionist barriers hurt domestic production. Countries that do not block imports of primary and intermediate goods, or capital equipment and business services, are more attractive places in which to invest.

PROCUREMENT: A TOUGHER NUT FOR FREE TRADERS

Despite these successes, free-exchange arguments have by no means triumphed. The dynamic of trade negotiations is still mercantilist.⁷ The language of “defending interests” and “concessions” reflects and reinforces the illusion that a jurisdiction which lets its citizens buy better things for less has lost, and one that blocks such access has won.

In the case of government procurement, an agency problem makes things worse. When governments block access to or raise the price of a desired product, buyers know whom to blame and press for relief. With government procurement, by contrast, the buyer will not directly experience the pain of paying too much or getting too little. Taxpayers and consumer interests are typically not consulted or informed about the alternatives. Inevitably they have little influence compared with the organized pressure from domestic producers. The use

of tax revenue furthermore makes mixed mandates—furthering domestic interests, including political objectives of the government—seem natural or even beneficial. International agreements have therefore made less progress in limiting discriminatory procurement: the various multilateral negotiations included no constraints on government procurement until the GATT Tokyo Round concluded in 1979.

Another reason why it is hard to limit discriminatory procurement is because subnational governments and their agencies are major buyers in many countries, Canada and the United States among them. Federal governments cannot and should not infringe on subnational governments (provinces or states) that are sovereign in their own spheres. It is even more challenging to bring the diffuse interests of taxpayers and consumers of public services to bear on subnational governments when those governments are not at the table during international talks. Not surprisingly, the Tokyo Round procurement code applied only to national governments. The CUSFTA likewise applied only to national governments, as did its successor, the NAFTA.

The Uruguay Round of multilateral negotiations that produced the WTO made efforts to extend the scope of disciplines on procurement. The result was the 1994 Government Procurement Agreement (GPA). The GPA, which applies to 40 WTO members, provides for disciplines on procurement by some subnational governments, such as some U.S. states and their agencies, though not by others, such as municipalities and utilities.⁸ The U.S. appendix to the GPA covers procurements by various departments and agencies in 37 states, but Canada declined to provide equivalent coverage—indeed, it declined to provide *any* coverage—of its provinces. Not surprisingly, the United States took a mercantilist stance in response and expressly excluded Canadian suppliers from the access it granted to other GPA signatories to the state entities in its appendices.⁹

RECENT CANADA-U.S. DEALINGS ON PROCUREMENT

These problems—consumer/taxpayer interests that are diffuse and unrepresented at the subnational level—stymied progress on government procurement disciplines

after the mid-1990s. NAFTA committed its partners to negotiations on voluntary, reciprocal coverage of state and provincial procurement by 1998, but nothing happened. Although some states and provinces have undertaken their own reciprocal agreements in government procurement in recent years,¹⁰ the U.S. government continues to cite discrimination in this area as an impediment to binational commercial relations;¹¹ in return, Canadian critics fault U.S. states for requiring domestic content in specific products and for steering procurement toward small, locally registered businesses.¹²

Canadian discussion of this issue tends to focus on Canada as a victim of U.S. protectionism, but, in truth, Canadian procurement practices at all levels are no less perverse. Federal industrial offsets in defense purchases,¹³ provincial content requirements (such as Ontario's 10 percent price preference for construction tenders using Canadian structural steel),¹⁴ and new local content requirements for subsidized energy investments in both Quebec and Ontario are just a few examples. The damage such measures do to producers outside each province, and to the producers on the other side of the Canada-U.S. border, is less than the harm they cause for domestic taxpayers and consumers, who pay higher taxes and electricity rates or get lower quality or less than they otherwise could.

Tension over procurement rose sharply following the 2008–2009 crisis and slump, as economic anxiety and fiscal activism created new protectionist temptations and tools. Despite an early commitment by the G20 countries to avoid them,¹⁵ and specific measures such as Canada's current cuts of tariffs on capital goods,¹⁶ tallies of protectionist measures suggest that the slump and the consequent government interventions have made national borders generally less permeable to commerce and investment.¹⁷

A salient event in the Canada-U.S. context was the *American Recovery and Reinvestment Act (ARRA)*, passed by Congress in February 2009. Section 1605(a) of the *ARRA* applies a Buy America requirement covering iron, steel, and manufactured goods to the projects it funds. Although this provision respected existing international agreements, it sparked alarm in Canada, where business leaders, policymakers, and trade experts predicted damage to Canadian export opportunities and warned about actual or potential movements of production from Canada to the United States.¹⁸

After a flurry of negotiations, the United States and Canada announced an agreement to address some of these concerns. The agreement, which came into force on February 16, 2010,¹⁹ has two main elements. One provides mutual access for procurement at the subnational level under the GPA. It gives Canadian suppliers access to procurement covered by the current U.S. GPA appendix, while U.S. suppliers gain access to provincial procurement as set out in a new Canadian GPA appendix. The second element expands access on both sides of the border—for Canadian suppliers to a range of state and local public works funded by the *ARRA*, and for U.S. suppliers to a range of construction contracts across provinces, territories, and some municipalities. This expanded access related to *ARRA* and Canadian construction contracts is temporary, however, running through to the end of September 2011. The agreement also commits both countries to further discussions within a year to explore another agreement that would expand market access for government procurement.

WHO WON? THE RHETORIC AND THE REALITY

Not surprisingly, given the different sizes and exposures to trade of the two economies, the procurement agreement got more attention on the Canadian than the U.S. side of the border. Also predictable was the mercantilist, adversarial language of much of the commentary. Official statements from both sides led with the export opportunities now open to firms in their own country.²⁰ Some commentators in the Canadian media hailed Canada's "victory"—tempered by concern that the bulk of the *ARRA*'s stimulus money had already been committed and that Canadian exporters' opportunities under the temporary provisions of the agreement were limited.²¹

This unique emphasis on export opportunities is misplaced, as are related references to gains and losses. Granted, to the extent that the agreement has material effects, U.S. and Canadian producers who needed a tilted playing field to get their products to market will feel pain. The real winners, however, will be U.S. and Canadian taxpayers and consumers. For the duration of the agreement, with more bids to choose among, U.S.

taxpayers who are funding the *ARRA* could potentially pay less, and U.S. citizens who are benefiting from the infrastructure and other projects it funds could get better quality than they could previously with a more restricted field. The same argument applies to Canadians who are funding and benefiting from their own governments' infrastructure spending. Extending the temporary elements of the agreement after 2011, or delivering on the promise of further negotiations, would make these benefits more generally available to taxpayers and consumers of public services.

THE NEED TO RECAST THE LANGUAGE AND FOCUS OF CANADA-U.S. BUY-LOCAL DEALINGS

The focus on the domestic benefits of more open government procurement adds key dimensions to the work plan of anyone interested in building on the February 2010 agreement and ensuring that it is a stepping stone to something more comprehensive and durable.

The clear first priority is to engage at the negotiating table. Both federal governments must take the lead, talking to each other and representing or involving the provincial and state governments. Each side should seek to cement the gains that have been made to date and to ensure that the elements of the GPA governing bilateral relations are the most liberal available.²² In pursuing the usual mercantilist aim of increasing access to the other country's markets, both governments have plenty to do. In the United States, defense and surface transportation are two major sectors where discriminatory procurement is rife. "Set-aside" contracts for small or minority-owned businesses have distorted purchases by U.S. federal agencies for more than half a century, and they are also widespread at the state level. Neither NAFTA nor the GPA constrains these programs, and the February 2010 agreement specifically excludes them. If they were subjected to some thresholds or other disciplines, Canadian suppliers would have the potential for more business across the border. On the Canadian side, the permanent elements of the February agreement contain a long list of exemptions, including shipbuilding and repair, highway construction, much of mass transit, and Crown corporations²³—all economically significant areas that would offer opportunities to U.S. suppliers.

Content rules and set-asides that discriminate not only against foreign but against out-of-state or out-of-province suppliers hurt citizens' interests.

Complementary to the negotiations, moreover, each side should increase its efforts to reach out to users of intermediate goods and the people who pay for and use publicly funded products on the other side of the border. Statistics and stories of existing sales and opportunities to export to Canada are now standard kit for Canadian diplomats and commercial officers in the United States. U.S. producers who use Canadian inputs—such as homebuilders concerned about supplies of softwood lumber—have long been important allies for Canadian exporters. The impediments that Buy America provisions created for U.S. contractors and municipalities as they tried to invest *ARRA* money must have factored in the U.S. government's decision to conclude the February agreement. Similarly in Canada, U.S. intermediate goods are critical to Canadian infrastructure and other publicly funded goods and services, and tax-weary citizens will likely welcome U.S. suppliers who offer better prices and favorable deals.

At least as important as these two thrusts, however, is the less-frequently noticed campaign at home: repeating the key message that liberalized procurement is about benefits to taxpayers and users of public services. That message applies just as much to the lowering of barriers between U.S. states and between Canadian provinces as it does to the lowering of barriers between the two countries. Indeed, one major potential benefit of further negotiations on a more comprehensive Canada-U.S. agreement covering subnational procurement is the leverage it can give Canada's federal government in working to limit inter-provincial discrimination. And a major potential benefit of an actual agreement is the possibility that it may result in situations where U.S. suppliers have better access than compatriots—always an awkward situation for defenders

of protection. Content rules and set-asides that discriminate not only against foreign but against out-of-state or out-of-province suppliers hurt citizens' interests.

In Canada, the procurement provisions of the Trade, Investment and Labour Mobility Agreement recently concluded between the provinces of Alberta and British Columbia mark an important step forward, with lower thresholds, fewer exceptions, and more effective dispute resolution than the existing national Agreement on Internal Trade. They also provide a wider range of covered entities, including Crown corporations, municipalities, and educational and health institutions.²⁴ When subnational governments buy from each other's producers, they not only open side doors to transactions that might be blocked directly but further integrate supply chains in ways that make protectionism less practical and less attractive.

Moreover, by revealing these benefits to taxpayers and consumers, these deals demonstrate that this same approach is just as applicable to international agreements as to agreements within countries. Canada is at the beginning of free-trade negotiations with the European Union. It would be simpler and smarter for the Canadian government to proclaim the virtues of procurement discipline to Canadians and to make the same concessions to the Europeans as it has to the Americans, rather than muddying the message with mercantilist language as it fights the same fight all over again. In the struggle to maintain open markets, the most important battle may be the one at home.

SURMOUNTING THE CHALLENGE

Mercantilist language resonates strongly when unemployment is high, just as temporary relief through trade barriers is more compelling when demand is clearly in a slump. An adversarial mindset comes easily when partners in economic relations are themselves misbehaving and embracing protectionist policies. As the North American economies recover, however, the realities of an aging population and slower workforce growth, combined with the need to overcome the legacy of higher interest payments and taxes incurred through fiscal excess, will sharpen the focus on meeting public needs more efficiently.

Government procurement is big business: in Canada and the United States, non-wage spending by governments

amounts to 12–14 percent of GDP. In 2009 Canada's procurement was almost half as big as the average value of national exports and imports, while U.S. procurement was as big as those totals.²⁵ Governments have many fiscal and monetary tools to cushion a slump and promote growth; discriminatory procurement need not and should not be among them. Erecting barriers between states, provinces, and countries is no more sensible than seeking self-sufficiency person by person, household by household, city block by city block. Even if it appears an affordable indulgence in good times, it is emphatically not one when times are tough.

Those who urge discriminatory procurement to support sick or dying industries should remember that consumption and investment, along with saving and borrowing, will determine the U.S. and Canadian balances of trade and payments in the future, just as they have in the past. Propping up one industry or sector, such as steel or manufacturing, can create a more favorable trade balance in those items, but the gain will come at the expense of others—including biotech materials or medical services, for example—that offer better jobs and higher incomes in the long run. The Canadian federal government, despite its minority status in Parliament and the recent severe slump, is unilaterally cutting tariffs on capital goods to make investment easier for cash-strapped firms. That understanding—that liberalizing benefits the liberalizer—should motivate Canadians and Americans alike to rethink their government procurement policies.

So far, the world has avoided the 1930s-scale economic disaster that appeared all too possible in late 2008. A key reason for optimism about recovery and expansion is that protectionist reactions have been muted. Canada and the United States deserve credit for working separately and together, as in the February 2010 agreement, to keep borders open.

In building on this recent agreement, the two countries cannot avoid an element of mercantilist, adversarial engagement at the negotiating table. As they talk, however, the negotiators, their political masters, and opinion leaders generally need to keep their eyes on the true objective—ensuring that taxpayers and consumers of public goods and services get a better bang for their buck. Each side needs to engage with allies on the other side of the border—those they know already, and those they have yet to meet. And each needs to make the case to its own

people that every time their country, province, or state makes a concession, they—as taxpayers and consumers—are the winners.

NOTES

1. I thank Philippe Bergevin for extensive collaboration on this article, and Alyson Henry for research assistance. Larry Herman, Jon Johnson, and several anonymous reviewers provided valuable comments on an earlier draft.
2. See Natalie Stechyson, “Buy America Horror Stories Building,” *Financial Post*, November 6, 2009. <http://www.financialpost.com/news-sectors/story.html?id=2193885>.
3. Arguments in favor of barriers to tide industries through a slump are much like the older argument for protecting “infant industries” until they grow up. As the experience of global trade and development discussed in the next section demonstrates, countries that promoted inward and outward trade, exposing all industries to more competition at home and abroad, have tended to be more successful. Selective protection, whether from downturns or more established competitors, runs into a classic problem: diversion of effort from pleasing customers to pleasing policymakers undermines attention to quality improvement and cost reduction.
4. Statistics Canada, CANSIM, tables 228-0003 and 380-0016.
5. The chief executive officer of IPEX, one of the companies whose pipes were dug back up in California, reported that 90 percent of the materials in the excavated pipes had come from Texas. Stechyson, “Buy America Horror Stories Building.”
6. See WTO, International Trade Statistics, 2009, chart 1.3; Doris Chu and Danielle Goldfarb, “Stuck in Neutral: Canada’s Engagement in Regional and Global Supply Chains,” Conference Board of Canada, May 2008, table 2.
7. See, for example, Bill Dymond and Michael Hart, *Navigating New Trade Routes: The Rise of Value Chains, and the Challenges for Canadian Trade Policy* (C.D. Howe Institute, Commentary, no. 259, March 2008).
8. A layperson’s guide is available at www.wto.org/english/tratop_E/gproc_e/gpa_overview_e.htm.
9. Jon Johnson, “Buy America: Canada Plays Catch-up,” *Canadian International Lawyer* (forthcoming), underlines the extent to which the federal government’s unwillingness or inability to commit the provinces to procurement disciplines has deprived Canadian exporters of U.S. opportunities that are open to other U.S. trading partners.
10. See, for example, British Columbia and Washington in 2009: “B.C., Washington State Partner on Cross-Border Opportunities,” Office of the Premier of British Columbia and Office of the Governor of Washington, October 9, 2009, www2.news.gov.bc.ca/news_releases_2009-2013/2009PREM0045-000458.htm.
11. Office of the United States Trade Representative, “National Trade Estimate Report on Foreign Trade Barriers,” 2009.
12. Scott Sinclair, “Buy American Sell-Out: Giving away Canadian Procurement Sovereignty,” Canadian Centre for Policy Alternatives, November 2009.
13. U.S. Department of Commerce, Bureau of Industry and Security, “Offsets in Defense Trade: Fourteenth Study,” December 2009.
14. Ontario Ministry of Government Services, “Procurement Policies and Practices,” 2008, www.doingbusiness.mgs.gov.on.ca/mbs/psb/psb.nsf/English/procurement.html.
15. The G20 Washington declaration of November 15, 2008, stated: “We underscore the critical importance of rejecting protectionism and not turning inward in times of financial uncertainty. In this regard, within the next 12 months, we will refrain from raising new barriers to investment or to trade in goods and services, imposing new export restrictions, or implementing World Trade Organization (WTO) inconsistent measures to stimulate exports.” See www.g20.org/Documents/g20_summit_declaration.pdf.
16. A first round of tariff cuts on capital equipment announced in the 2009 federal budget was followed by a larger round in the 2010 budget. The budget projected a reduction in customs revenue of C\$300 million by the time the tariffs are fully phased out—equal to about 7½ percent of the customs revenue of C\$4 billion in fiscal year 2008/2009. Public Works and Government Services Canada, *Budget 2010*, March 2010, p. 89; Receiver General for Canada Public Accounts of Canada, 2008–2009, October 2009, 1.6.
17. As of March 2009 the World Bank had tallied 47 measures to restrict trade at the expense of other countries which had been implemented since the beginning of the financial crisis. Seventeen of the G20 countries had implemented such measures. Elisa Gamberoni and Richard Newfarmer, “Trade Protection: Incipient but Worrisome Trends,” World Bank, *Trade Notes*, no. 37, March 2009.
18. See, for example, www.ceocouncil.ca/en/view/?document_id=1372.
19. The text of the agreement is available at [www.international.gc.ca/trade-agreements-accords-commerciaux/assets/pdfs/ENG-Canada-USA%20Government%20Procurement%20\(clean%2011%20Feb%202010%20printed\).pdf](http://www.international.gc.ca/trade-agreements-accords-commerciaux/assets/pdfs/ENG-Canada-USA%20Government%20Procurement%20(clean%2011%20Feb%202010%20printed).pdf).
20. See www.international.gc.ca/media_commerce/comm/news-communications/2010/069.aspx?lang=eng for the Canadian statement, and www.ustr.gov/countries-regions/americas/canada for the U.S. statement.
21. Paul Viera, “Protectionism ‘Breakthrough’ Reached: Canadian Victory,” *Financial Post*, February 5, 2010, www.financialpost.com/news-sectors/economy/story.html?id=2523659. To critics who focus on the limited amounts of U.S. stimulus money still available to Canadian sellers, it seems apt to retort that, had Canada provided the same subnational coverage when it originally adhered to the GPA as it has now, Canadian suppliers would have been able to bid from the beginning.
22. The February agreement makes reference to the 2007 revisions to the text of the 1994 GPA (still formally in force), which improve in many respects on the 1994 version.
23. Many Crown corporations are included in the temporary agreement, which underlines the fact that no fundamental principles or practical considerations dictate this exclusion.
24. See www.tilma.ca/faq_vendor_contractor.asp.
25. National accounts figures from Statistics Canada put non-wage spending by Canadian governments on goods and services of C\$216 billion in 2009; the U.S. Commerce Department figure for the United States was US\$1,749 billion. The average of Canadian exports and imports of goods and services was C\$451 billion; the comparable U.S. figure was US\$1,760 billion.

ROBERT BAUGH'S RESPONSE TO WILLIAM ROBSON

In reading William Robson's essay, "Buy the Best! The Message Canadians and Americans and Their Governments All Need to Hear," it is obvious that we have very different messages we would like our audience to read. While we both agree that trade is critical to each nation's economy and that negotiations have served to address the immediate concerns about Buy America, our paths soon diverge, with fundamental differences over theory, economic policy, and real world experience.

Robson repeatedly raises a set of assertions in defense of free trade. They include comparative advantage, consumers as the winners, procurement used as a prop for dying industries at the expense of other industries with better jobs, exchange rates that adjust to balance overall flows of trade and investment, and labeling any action that is perceived to interfere with free trade as "mercantilist" or "protectionist"—even those actions that have been negotiated and adjudicated. Robson's essay also suggests that the failure to legislate open borders was one cause of the Great Depression. These myths need to be dispelled.

The holy grail of trade theory—comparative advantage—is used to sell free trade as a win-win proposition. In David Ricardo's 1817 theory, barriers to trade defeat efficiency because, if one country is better at making wine and another at making wool, it makes no sense for each one to produce both—they should each do what they do best and trade their excess production. And, as the economist Robert Kuttner once observed, "add some algebra, and that is how trade theory continues to be taught today."¹ But, 19th-century assumptions do not hold up to 21st-century reality. The theory assumes, for example, that factors of production (especially capital) are not mobile between nations and that there is always a full output economy—or that trade has no effect on its output. Experience undermines these and other Ricardian assumptions.²

Ricardo's perfectly balanced competitive markets do not exist. Paul Krugman, the 2008 Nobel Prize laure-

ate in economics, long ago observed that this theory had serious flaws. Although he recognized the importance of a nation's natural endowments, he also realized that much of global trade had little connection with basic advantages. "Instead," Krugman wrote, "trade seems to reflect arbitrary or temporary advantages resulting from economies of scale or shifting leads in close technological races."³ He also acknowledged that comparative advantage could be created by interventions targeted at particular industries and technologies for a nation's benefit. China, Japan, Korea, Germany, and other countries have repeatedly demonstrated the truth of this observation.

The idea that free trade does not increase income inequality among nations and that everything will balance out has been thoroughly debunked. The groundbreaking research by the esteemed economists Ralph Gomory and William Blau in their book, *Global Trade and Conflicting National Interests*, shattered the illusion. Like Krugman, they recognized economies of scale and their role in economic growth. They warned that highly capitalized and knowledge-intensive industries defy Ricardian economics, and that advanced industrial nations can lose if they do not manage trade and industrial policy trade well.⁴ Paul Samuelson, the godfather of modern economics, lent further credence to their findings when he weighed in against academic proponents of free trade purveying "polemical untruth." He recognized that "free trade is not always a win-win situation," because large low-wage countries can capture advanced industries and, inevitably, those conditions will have an impact.⁵ One consequence is that international wage, tax, and regulatory arbitrage is a reality, as companies look around for the most favorable economic environment in which to locate. The other is that trade has played a major role in a decade of loss: in the United States, that loss translates into one-third of manufacturing jobs, the closure of tens of thousands of facilities, wage stagnation, and massive unsustainable trade deficits.

The notion that exchange rates will correct trade imbalances has proved to be laughable. For a decade, the Chinese currency (RMB) has been undervalued (by 30 to 40 percent), and a number of other leading economies have emulated that behavior. That has been a leading factor in a decade of record U.S. trade deficits. The concern over China's currency has become a worldwide problem, but the international trade institutions—the World Trade Organization (WTO) and the International Monetary Fund—have proved incapable of action or of crafting a multilateral solution.⁶

One of the most perverse free-trade arguments is the one that takes the consumer as the arbiter for the structure of an entire economy. It trumpets consumption over production by dismissing manufacturing as a *laissez-faire* afterthought—as though it does not matter what we make or even if we make anything at all. It ignores the opportunity costs and the opportunities lost, such as future innovation, employment, income, and the growth in gross domestic product (GDP). It also ignores the economic reality that, to achieve balanced trade, countries must be making things of value to trade. Moreover, it has led to an erosion of the working middle class. That is why, for most countries, it is not consumers who are the driving force of economic policies, but employment, income, and investment. In North America we have lost sight of that fact—a key part of the post-1945 policies that led to prosperity.

Robson suggests that free trade is the primary reason for economic growth in the postwar era. In holding this position, he misses the foundational investment and empowerment drivers that were at work in those years. The Allies' development approach was a Keynesian one that rebuilt economies and provided constitutional guarantees of workers' rights to organize and bargain collectively. This private-sector market approach—that workers with legal rights would raise their own wages, benefits, and working conditions over time—clearly succeeded. The economies of Germany, Italy, and Japan prospered, as did their labor force. The same was true for Canada and the United States. Twenty years ago the European Union had a similar debate about its first expansion, and, over time, it chose to invest and to raise the environmental and labor standards

of Spain, Portugal, and Greece rather than lower those in the more prosperous member countries. Today, these balanced approaches are missing at the WTO, in the current Doha Development Round of talks, in trade deals such as NAFTA, and in trade negotiations with China.

The message policy makers need to hear is simple: there is a better way. We cannot base 21st-century policies on 19th-century assumptions. It is time for both of our nations to get real about smarter, fairer, more-balanced trade. They must also develop domestic investment policies, along with labor and environmental standards, that will result in a vibrant economy and a thriving manufacturing sector that generates good jobs.⁷ Let Buy American and Buy Canadian open the door to this much-needed strategic discussion.

NOTES

1. Robert Kuttner, "The Free-Trade Fallacy," *The New Republic* 188 (12), March 28, 1983.
2. For a detailed critique of comparative advantage, see Ian Fletcher, *Free Trade Doesn't Work: What Should Replace It and Why* (Washington D.C.: U.S. Business and Industry Council, 2010). Over the years, Robert Kuttner has written extensively of comparative advantage and free trade. John Cassidy, "Winners and Losers: The Truth about Free Trade," *The New Yorker*, August 2, 2004.
3. Kuttner, "The Free-Trade Fallacy."
4. Ralph Gomory and William Baumol, *Global Trade and Conflicting National Interests* (Boston: MIT Press, 2001).
5. Paul Samuelson, "Where Ricardo and Mill Rebut and Confirm Arguments of Mainstream Economists Supporting Globalization," *Journal of Economic Perspectives* 18 (September 2004): 135–46.
6. A wealth of information is available on this subject from the U.S. Treasury Biannual Currency Reports; see <http://www.ustreas.gov/offices/international-affairs/economic-exchange-rates>. Economic studies and legal information are also available from the Fair Currency Coalition, <http://www.faircurrency.org/index.html>, and the Peterson Institute for International Economics, <http://piie.com/research/researcharea.cfm?ResearchTopicID=48&ParentTopicID=7#china>.
7. Several new works that provide a broad view of trade and domestic investment policies have helped inform my essay and rebuttal published here. They include Richard McCormack, ed., *Manufacturing: A Better Future for America* (Washington, D.C.: Alliance for American Manufacturing, 2010); "Made in America: Reviving American Manufacturing," *The American Prospect*, November–December 2010; Pat Choate, *Saving Capitalism* (New York: Vintage Books / Random House Press, 2009); Clyde Prestowitz, *The Betrayal of American Prosperity* (New York: Free Press / Simon and Schuster, 2010).



WILLIAM ROBSON'S RESPONSE TO ROBERT BAUGH

Robert Baugh's aggressive defense of discriminatory procurement and interventionism generally makes two things plain. First, those advocating open borders and avoidance of the mistakes of the 1930s have plenty of work to do. Second, effective engagement on the core issues in this debate is hard to get.

The case for openness is about letting people buy the best quality and the best value available—either through their governments or directly. Baugh, however, never talks about that. He mentions taxpayers only tangentially. And he never mentions consumers at all.

PRIMACY OF CONSUMER AND TAXPAYER INTERESTS

This gap in Baugh's essay is a shame. His views on taxpayer and consumer interests would be good to hear, partly because his heavy reliance on legalistic and tit-for-tat justifications suggests he is not fully at ease with his own case.

There is no question that today's discriminatory procurement measures have many legal antecedents and accommodations in international agreements.¹ Similarly, there is no doubt that trade law frowns on Chinese-style export promotion.² But saying that legality or illegality proves that something is right or wrong offers many hostages to fortune—as Baugh would doubtless agree regarding, for instance, laws mandating secret ballots for union certification. As the Canada-U.S. deal in February 2010 testifies, existing trade agreements can be improved. Current laws are largely products of mercantilist thinking, and making them friendlier to the interests of the average citizen is a key ongoing task.

No more convincing is the “we should because they do” defense. I fault Canadians for the same protectionism Baugh does, and I agree that excluding provinces from the Government Procurement Agreement in 1994 was a failure that Canada should not have needed a crisis to fix.³ Free traders, however, are not black pots denigrating black

kettles: they condemn discriminatory procurement on both sides. The irony is not, as Baugh says, that Canada is being forced to do what it *could* have done before, but that Canada is being forced to do what it *should* have done before—for the sake of the majority of Canadians. Canada's mistakes are a shabby justification for U.S. actions that will hurt the majority of Americans.

PERILS OF MIXED MANDATES

Not being sure where Baugh would rank quality and value for taxpayers and consumers in government procurement decisions, I will repeat my contention that those interests should be front and center. The agency problem in government procurement—when the people doing the buying have little personal incentive to seek the best quality and the most competitive price—is no small issue. The buyers may purchase second best or pay too much, believing they serve the public interest, but they may also do so because of laziness, pork-barreling, or corruption. Modern governments are big and strong, and the crisis has made them even bigger and stronger. To protect citizens' interests, policymakers should be given mandates that are clear and transparent.

Baugh's essay points the opposite way. He lauds the *American Recovery and Reinvestment Act (ARRA)* not just for its discriminatory procurement but as “the leading edge of a new environmental economic development policy.” He celebrates the government ownership of car makers. He urges “an aggressive, sustained commitment of national

As the Canada-U.S. deal in February 2010 testifies, existing trade agreements can be improved.

resources to create and retain good jobs, increase per capita income, modernize industry, develop and deploy technology, and educate and train workers” with “assistance for any workers, families, or communities that may be adversely affected ... and a democratic voice for workers in their workplaces and their communities.”

This wish list says nothing about how to reconcile inevitable conflicts—when buying local conflicts with buying clean, when communities dependent on dying industries resist innovation, or when the surge of government spending to pay for it all runs out. You don’t have to be a radical free trader to see this muddle of mandates as an accountability-defying jumble—welcome, perhaps, to some legislators, bureaucrats, and pressure groups, but hostile to the interests of most Americans.

MERCANTILIST ILLUSIONS

Accountability matters all the more because these exhortations cannot deliver one of Baugh’s core ambitions—a U.S. trade surplus. Macroeconomic conditions, not barriers to and subsidies for cars, manufactures, or all goods, determine the trade balance. As the more than one thousand U.S. economists who petitioned—unsuccessfully, to the world’s misfortune—against the Smoot-Hawley tariff of 1930 pointed out, blocking the rest of the world’s ability to sell to the United States will correspondingly hurt the rest of the world’s ability to buy from the United States.⁴ For as long as the United States depends on foreigners to supplement its own meager saving, it must and will run current-account deficits.

Although propping up Baugh’s favored industries cannot produce a trade surplus, it can hinder adjustment and growth. The decline in manufacturing’s share of the North American economies is no more regrettable than the decline in agriculture over the past century. The more developed countries of the world are increasingly specializing in higher-value sectors—typically with support from inputs purchased abroad. If the United States followed Canada in cutting tariffs, North America’s future position as a favored place to work and invest would be more secure.

MAKING THE RIGHT CHOICES TOGETHER

It is disappointing that Baugh’s contribution to this binational discussion of government procurement contains no constructive advice for Canada-U.S. negotiations. He does, however, make a forecast: “As nations move toward massive climate change investments, the reaction to Buy America portends a coming conflict among international environmental, economic, and trade policy.” This glum prediction should inspire action. Economic distress has made myriad interventions to serve mixed and particularist interests seem more acceptable. A breakdown of international cooperation in trade and investment, however eloquently rationalized by legalistic and tit-for-tat rhetoric, could yet trigger a 1930s-style collapse.

Happily, however, the *ARRA*’s respect for international agreements and the Canada-U.S. deal in February show that policymakers are alive to this threat. Further progress toward openness in bilateral and multilateral negotiations, and relentless focus on consumer and taxpayer interests in words and in deeds, can better foster continued recovery and durable expansion in the years ahead.

NOTES

1. The reference is to the passage in Baugh’s opinion essay that reads: “The Department of Defense has had Buy America provisions since 1941, and the Federal Highway Administration, Federal Transit Administration, and Federal Railroad Administration all have long-standing provisions ... Most notably, the *ARRA* requires that the Buy America provision be ‘applied in a manner consistent with U.S. obligations under international agreements.’”
2. Baugh devotes a long paragraph to the U.S. tariff against Chinese tires without once considering what a free trader would see as the most salient point: that the U.S. government forced its own citizens to pay more for tires.
3. The reference is to Baugh’s passage: “Canada is also a GPA member, and it has excluded significant sectors from coverage—even broader exceptions than those claimed by the United States ... Ironically, Canada did not have a reciprocal relationship with the United States because it had failed to bind its provincial procurement under the GPA. When the crisis hit, it was obliged to enter into negotiations to find a solution.”
4. See “Economists against Smoot-Hawley,” *Econ Journal Watch* 4 (September 2007): 345–58, available at <http://econjwatch.org/articles/economists-against-smoot-hawley>, for the petition and commentary on its creation, its failure to sway Congress and President Hoover, and the dismal consequences of that failure.



About the Authors

1 **BOB BAUGH** was appointed executive director of the AFL-CIO Industrial Union Council in January 2003. The Council, comprised of the nation's leading industrial unions, is the coordinating body for the federation's manufacturing policy and legislative initiatives. He is the co-chair of the AFL-CIO Energy Task Force and has served as the leader of the U.S. labor delegations to the United Nations climate change conference negotiations in Bali, Poznan, Bonn, and Copenhagen. He regularly testifies before Congress, is a spokesperson with the media, and writes about manufacturing, trade, globalization, energy, and the economy. His publications include *Changing Work: A Union Guide to Workplace Change* and *Greening the Economy: A Climate Change and Jobs Strategy That Works for All*.

2 **WILLIAM ROBSON** took office as president and CEO of the C.D. Howe Institute in Toronto in July 2006, after serving previously as senior vice-president and director of research. A graduate of both the University of Toronto and the Norman Paterson School of International Affairs at Carleton University, he has written extensively on government budgets, pensions, and inflation and currency issues. His work on demographic change and healthcare financing won an award from the federal Policy Research Secretariat, and his work on monetary policy with David Laidler won prizes from the Canadian Economics Association and the Donner Canadian Foundation. He has also been a regular columnist for the *Globe and Mail* and is a familiar commentator on economic issues in the media.

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