Much more than bananas at stake in US-Europe trade conflict

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An emergency meeting of the World Trade Organisation, which began in Geneva on Monday, appears to have failed to resolve the trade conflict between the United States and the European Union over the EU's banana imports policy. The US insists that despite rulings from the WTO, the Europeans are still favouring producers in the former European colonies in the Caribbean over the US producers, Dole and Chiquita, operating out of Latin America.

WTO director-general Renato Ruggiero said before the meeting that no-one should expect any decisions from it.

"This meeting has been called because the Europeans want to say they do not like the trade measures taken by the United States. And the United States, they will explain their point of view is a meeting in which there is nothing to decide," he said.

The emergency session was convened at the request of the EU which accused the US of "irresponsible unilateral action" following its decision last week requiring importers to post bonds equivalent to a 100 percent tariff on $520 million worth of luxury exports to America in advance of a WTO ruling on the disputed EU banana imports policy.

In a letter to the WTO general council the EU accused the US of "blatant disregard" for the WTO's disputes settlement procedures "based on the rule of law."

The US action prompted a flurry of diplomatic activity and statements of condemnation. In London the British government called in the US ambassador twice within 24 hours and Prime Minister Tony Blair telephoned US president Bill Clinton urging that he intervene to defuse the dispute. British officials estimate that as many as 2,000 jobs could be threatened by the US action.

A statement by the French Foreign Ministry said that France deplored the US action and called on the administration to "show good faith and reverse an unacceptable decision."

The European condemnation was also joined by Japan. It said the US sanctions were deeply regrettable, a flouting of global trade rules and "an equivalent effect to the United States taking a unilateral action, despite the fact that the WTO has not authorised it to suspend concessions."

The involvement of leading trade and financial bodies of all the major capitalist powers indicates that the trade tensions extend well beyond bananas. The US has already launched action against imports of cheap steel from Japan and a conflict is brewing with Europe over aircraft and genetically modified agricultural exports. And behind the immediate issue of exports are US concerns over the widening trade imbalances and what it considers to be the failure of both Japan and the European powers to sufficiently stimulate their economies to absorb the flow of exports from the depressed Asian region.

In addition there are tensions over policies to deal with the global financial crisis. The European nations, supported by Japan, are calling for a re-regulation of currency exchange rates to ensure "controlled flexibility" containing fluctuations to between 20 and 30 per cent, together with action to control the huge flows of capital through global financial markets. The United States, however, is insisting that such measures are largely unworkable and only impede the operations of the "free market."

The underlying causes of the conflicts can be clearly seen in the latest figures on the US trade account. The US merchandise trade deficit rose by 25 percent in 1998 to its highest level on record, reaching $248 billion, an increase of $50 billion over 1997. The goods and services deficit jumped by 53 percent to $169 billion, also an all-time record. Furthermore it is predicted that the deficit in the US balance of payments on current account will increase by an additional $57 billion, or 25 percent in 1999.

Speaking at the World Economic Forum meeting held in Davos, Switzerland, at the end of January, influential American economist C. Fred Bergsten predicted that America's current account deficit would reach the equivalent of 3.5 percent of gross domestic product in 1999. This would be the same level it achieved in the mid-1980s, after which there was a 50 percent fall of the dollar against the deutsche mark and the yen. The net foreign debt, he predicted, would rise to $2 trillion, roughly equivalent to 25 percent of GDP.

Bergsten warned that the rise in the US deficit would intensify "a wide range of protectionist trade pressures in the United States." "The steel industry is already seeking comprehensive relief. Machine tools, semiconductors, shipbuilding, textiles and several agricultural sectors may not be far behind. If American economic growth slows enough to push unemployment up by even a modest amount, as seems likely, the trade deficit will be blamed for 'exporting jobs' and the pressure on trade policy will become intense."

There have been warnings in the British financial press that the banana war could lead to a breakdown of the WTO disputes settling procedures with far-reaching implications for the world economy.

According to an editorial comment in *The Economist* of March 6: "The immediate worry is that hostilities will break out on other fronts too. America is fuming about the EU's ban on hormone-treated beef. It is unhappy with Europe's reluctance to embrace genetically modified food. It is angry over European subsidies for Airbus, Boeing's rival in aerospace. It is concerned that an EU directive on data-privacy and proposed rules on aircraft noise discriminate against American firms. It is peeved that the EU has asked the WTO to rule against its sanctioning imposing 'Section 301' legislation. In the background, there is huge resentment that the EU is doing so little to stimulate demand, leaving America as the sole locomotive of the world economy and chief bearer of the 'burden' of imports from struggling emerging economies."

In the longer term a "worse fear" was that the WTO might not be able to enforce its own rules.

"If countries feel that the WTO does not work, they will be tempted to bypass or ignore it. Big powers such as America and the EU may prefer to act unilaterally. Smaller ones might gang up, or curry favour with bigger powers to pursue their claims. The predictability and fairness of a rules-based system could be lost. In its place would be an arbitrary one based on power. Almost inevitably, there would be more protection and more trade wars."

The *Financial Times*, in an editorial of March 5, called on both sides to "pull back before more damage is done."

"This is a plain, old-fashioned trade row, aggravated by weak leadership on either side. But far more difficult disputes are looming, which do not simply involve business lobbies, but deep differences in social and cultural attitudes across the Atlantic. They include issues like hormones in beef, antibiotics in food, and trade in all genetically modified products."

It said the dispute had been aggravated by "US concerns at the soaring trade deficit, and at the perceived unwillingness of Europe to share that burden. Things will only get worse if the two sides cannot deal with individual trade disputes in a more coherent way."

Fearful of the consequences of a trade war between the major powers, the *Australian Financial Review* warned in an editorial that the dispute had "fundamental and far-reaching implications for the effective functioning of a rules-based global trading system, on which medium-sized nations like Australia depend."

"The bananas dispute threatens to undermine the crowning achievement of the last round of multilateral negotiations--a binding mechanism for settling disputes over breaches of agreed trade rules."

If the "fragile bargaining" underpinning the system were to fail and rulings were "routinely ignored, or subverted by replacement measures" then the system would fall into "disrepair and disrepute."

"Powerful players like the US and EU will revert to the use of unilateral measures, to the disadvantage of smaller players like Australia. A crucial pillar of the rules-based trading system will collapse."

The rapid entry of Japan into the dispute on the side of the EU is also significant. Besides the immediate conflict over steel exports, there is growing resentment in Japanese ruling circles over the continuing American claims that the government is not doing enough to resolve the country's financial crisis.

According to a report in the *Australian Financial Review*, the well-known Japanese author Kenichi Ohmae insists that the reason for what he calls American "micro-management" is to keep Japan doing what really needs to be done: liquidating its holdings of US treasury bonds and using the proceeds to refinance the banking system without increasing government debt. Such a measure, which has been previously threatened by government spokesmen during periods of tensions over trade issues and currency values, would have major implications for US bond prices, interest rates and stock market values.

The US-Japan differences extend to the global financial regime, with the Japanese government favouring European proposals for coordination of exchange rates and controls on the movement of capital.

Last week in a speech delivered on his behalf to a World Bank symposium in Tokyo, Japanese finance minister Kiichi Miyazawa criticised the IMF's handling of the Asian crisis. The IMF, he claimed, had been established in days when global capital flows were limited and it had not attuned itself to the new situation. If the IMF continued to advise countries to take measures that were appropriate for crises arising from current account deficits, it would not only damage the country's chances of recovery but also the reputation of the IMF.

Miyazawa's speech, delivered in the presence of IMF deputy director Stanley Fischer, called for "market friendly" regulations on the movement of capital--a policy which is opposed by the US.

While the policy disagreements are so far confined to so-called "emerging markets" they could have wider implications.

As the *AFR* article commented: "There is a growing possibility that the resentment of American financial imperialism and the new found friendship with Europe may yet play out into something far more significant than an ideological debate over free markets in emerging nations."