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BACKGROUNDER

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New Trade Agenda for Advancing Economic Freedom in the World

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Abstract

Free trade has fueled competition, innovation, and economies of scale, giving people all over the world lower prices and more choices. Yet even the U.S. seems to have "free trade fatigue," and the most recent free trade agreements seem in many respects designed more to regulate trade than to free it. The development of the free-market system has brought about a dramatic and revolutionary improvement in living standards around the world. The Trump Administration should build upon the momentum of recent decades to increase economic freedom and dynamic growth, not disrupt it with protectionist trade policy.

The United States was the first great free trade zone of the modern age, a fact that accounts for the economic efficiency and prosperity that has made it the largest economy in the world. The freedom to trade without hindrance across a continent-spanning market, which has underpinned America's rapid development, has in modern times been emulated by groups of nations such as the European Union and promoted worldwide through multilateral organizations like the World Trade Organization (WTO). Trade freedom has also been extended through a number of bilateral and regional free trade agreements. The globalized economy that has resulted provides historically unprecedented economic freedom for individuals around the world to trade freely in pursuit of better lives for themselves and their families.

The process of economic specialization and trade, which allows individuals to focus on doing the things they do best and exchange the products of their labor with others who are likewise concentrating on their own areas of expertise, leads to higher levels of production

Key Points

- The right to trade freely is properly an individual right that government should act only to secure, not to impede.
- If the rapid economic growth that has done so much in recent decades to reduce poverty around the world is to be sustained, governments everywhere must rededicate themselves to economic openness and the most widespread freedom to trade and invest.
- In the ongoing process of revitalizing America's global competitiveness and economic dynamism, the Trump Administration has the unique opportunity to become an effective advocate for trade freedom and help America reap the rewards of free trade policies.
- In addition to the European Union, Japan, and the United Kingdom, the Administration should take a practical look at the countries that have indicated a willingness to forge closer trade partnerships with the United States: Switzerland, Taiwan, Georgia, and Tunisia.

This paper, in its entirety, can be found at **http://report.heritage.org/bg3369**

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of goods and services as well as the most efficient use of labor and resources. It is this process that creates and sustains the markets of the "free market" system. The development of this system has brought about a dramatic and revolutionary improvement in living standards around the world. Free and open trade has fueled vibrant competition, innovation, and economies of scale, allowing individuals and businesses to take advantage of lower prices and more choices.

The right to trade freely is properly an individual right that governments should act only to secure, not to impede. Yet the freedom to trade, despite its manifold societal and economic benefits, is often under attack.

Tariffs, for example, never lack champions and supporters. Potential restrictions can be far broader, however, and modern trade agreements like the Trans-Pacific Partnership or the United States-Mexico-Canada Agreement are mammoth documents with extensive provisions that can seem in many respects designed more to regulate trade than to free it.

There have always been those who seek to use the power of government to restrict others' freedom to trade in order to enhance or preserve their own economic advantages, pressuring societies to expand the size and weight of government intervention. If the rapid growth that has done so much in recent decades to reduce poverty around the world is to be sustained, however, governments everywhere must rededicate themselves to economic openness and the most widespread freedom to trade and invest.

Diminishing Trade Freedom in the Global Economy

History has proven that trading freely is the most pragmatic economic strategy for people all over the world. No single nation has the natural resources, infrastructure, and human capital in sufficient quantity and quality to realize the standard of living to which developed nations have become accustomed and to which developing nations aspire. And so, people trade.

In recent years, however, opposition to trade agreements has come from both the Left and the Right, casting doubt on whether the old consensus on trade can hold. The impact of free trade has been the regular and intense subject of contentious debate both in politics and in the media.

Context matters in such heated debates, and one needs to acknowledge that the context in which people think about trade has shifted. As tariffs have come down, trade negotiators have turned their attention to a much wider range of issues, such as labor and environmental standards, currency manipulation and investment regulations, and even human rights conventions. Trade agreements are becoming ever more comprehensive, and their regulatory reach has become quite sweeping. Such managed trade could actually make countries less competitive. Good trade agreements, by contrast, can be simple. The only essential component is that they reduce or eliminate trade barriers.

It is notable that in 2017, world trade grew at its fastest pace since the 2008 financial crisis, in both value and volume. However, as the WTO points out, "[w]hile G20 economies continue to implement trade-facilitating measures, the more worrying trend during this period is the increase in trade-restrictive measures which has come at a time of increasing trade tensions and associated rhetoric."

Reflecting this negative trend, the latest rankings of trade freedom around the world, measured by Heritage Foundation analysts for the forthcoming *2019 Index of Economic Freedom*, show that global trade freedom has declined. (See Appendix Table A for the 2019 "trade freedom" scores.)

The WTO's global trade monitoring report on G20 trade measures covering the period from mid-October 2017 to mid-May 2018 documents that new trade-restrictive measures from G20 economies have doubled compared to the previous review period.[1] During the same period of monitoring, the WTO reports that its members "applied 75 new trade-restrictive measures, including tariff increases, quantitative restrictions, imposition of import taxes and stricter customs regulations, amounting to a monthly average of almost 11 new measures per month."[2]

Making markets freer and more open requires that political leaders demonstrate courage, foresight, and sustained commitment. Despite the demonstrable

1. World Trade Organization, "Report on G20 Trade Measures," July 4, 2018, https://www.wto.org/english/news_e/news18_e/g20_wto_report_july18_e.pdf (accessed October 17, 2018).
2. World Trade Organization, "Monitoring Report Shows Increase of New Trade Restrictions from WTO Members," July 25, 2018, https://www.wto.org/english/news_e/news18_e/trdev_25jul18_e.htm (accessed October 17, 2018).

benefits to consumers and business of lower prices and the greater availability of goods and services, opening a domestic economy to increased competition rarely, if ever, garners widespread popular support. There can be near-term costs in terms of the displacement of workers in industries affected by increased competition, and negatively affected individuals or firms are not shy about making their displeasure known to government officials.

Balancing such interests can require real leadership and commitment. Global trade is highly competitive and complex, open trade is a constantly evolving phenomenon and process, and the temptation to seek short-term advantages through the protectionist tactics of higher tariffs, subsidies, and other devices abounds. In such an environment, defending and advancing trade freedom is more important than ever.

Will America Still Lead?

America's engagement with the world through trade and investment has been the framework upon which its prosperity rests, and an engine of growth for the world as a whole. Open trade and investment policies have created economic dynamism that engenders continual innovation and leads to better products, new markets, and greater investment. America and all countries stand to gain from expanding markets and greater trade.

In America today, however, some of the main processes through which trade has historically been liberalized are being questioned. According to the 2017 Executive Order on trade by President Donald Trump, "For many years, the United States has not obtained the full scope of benefits anticipated under a number of international trade agreements or from participating in the World Trade Organization."[3]

That the government should maintain trade agreements only when they benefit Americans is obvious. Open trade, however, is based on the concept of mutual advantage. To paraphrase President Ronald Reagan: The goal of free trade agreements should be to unite people around the world in a bond of mutually beneficial exchange.

It is notable that in its 2017 National Security Strategy, the Trump Administration stated that "the United States will partner with countries as they build their export markets, promote free market competition, and incentivize private sector growth."[4] Furthermore, in its 2018 trade agenda report to Congress, the Trump Administration specified that "the United States remains committed to working with like-minded countries to promote fair market competition around the world."[5]

These statements are welcome, but leave unclear the extent to which the Administration understands that it is free trade that best promotes the fair competition it seeks.

Forging Deeper Trade Relationships

As data in The Heritage Foundation's *Index of Economic Freedom* show, people in countries with low trade barriers are much more prosperous than those in countries with high trade barriers.[6] Therefore, the best approach to ensuring that America continues to reap the benefits of international commerce is to work continuously to lower its own barriers. This can, of course, be done unilaterally, and some of the freest economies in the world, such as Hong Kong, Singapore, and New Zealand, have followed this path effectively. For many countries, however, a more likely path to lower barriers lies in the pursuit of trade agreements with others, particularly with like-minded and willing countries, to advance mutual market openness.

With that in mind, the Trump Administration should consider negotiating trade agreements with additional partners, based on the following guiding principles:

- The primary function of America's 21st-century free trade agreements should be the removal of

3. Executive Office of the President, "Executive Order 13786: Omnibus Report on Significant Trade Deficits," *Federal Register*, Vol. 82 (April 5, 2017), p. 16721, https://www.federalregister.gov/documents/2017/04/05/2017-06968/omnibus-report-on-significant-trade-deficits (accessed October 30, 2018).
4. The White House, "National Security Strategy of the United States of America," December 2017, https://www.whitehouse.gov/wp-content/uploads/2017/12/NSS-Final-12-18-2017-0905.pdf (accessed October 17, 2018).
5. Office of the United States Trade Representative, "The President's 2018 Trade Policy Agenda," April 2018, p. 4, https://ustr.gov/sites/default/files/files/Press/Reports/2018/AR/2018%20Annual%20Report%20I.pdf (accessed October 17, 2018).
6. Terry Miller, Anthony B. Kim, and James M. Roberts, *2018 Index of Economic Freedom* (Washington, DC: The Heritage Foundation, 2018), http://www.heritage.org/index.

pre-existing government restrictions on trade. Free trade agreements need to serve as the pragmatic vehicle through which partner governments agree to mutually remove some or all such restrictions.

- Previous trade agreements have created an environment that allowed policymakers to eliminate trade barriers that would otherwise probably still be in place. Trade negotiators today should not be in a position of defending or erecting new barriers. The United States Trade Representative should work only to reduce both foreign and U.S. protectionism.

- In addition to reducing tariff and non-tariff barriers to trade, new trade pacts should provide ways to mediate trade and investment disputes and prevent costly trade wars.

- The end goal of new U.S. trade agreements must be to enhance Americans' freedom to trade, with exceptions only for the minimum restrictions that may be required by national security concerns. Attempts as in some recent trade agreements to codify regulations in areas like labor and the environment or other areas of social concern are generally unhelpful and tend to reduce, rather than enhance, trade flows.

- At the G7 meetings in Quebec in June 2018, President Trump surprised other leaders with this proposal: "We should at least consider no tariffs, no barriers—scrapping all of it." Indeed, dismantling tariff and non-tariff barriers across the board is good trade policy. Cutting tariffs, which are nothing more than taxes on imports, should not be a controversial issue. Zero tariffs and zero barriers should be the ultimate goal for a new batch of free trade agreements.

- The U.S.'s economic engagement with other countries involves trade in goods and trade in services, as well as U.S. investments in other countries and foreign investments in the U.S. There are massive financial flows into and out of the U.S. The entirety of economic interactions between Americans and foreigners must be taken into account in order to avoid policy mistakes.

On October 16, 2018, United States Trade Representative Robert Lighthizer notified Congress that the Trump Administration intends to negotiate three separate trade agreements with Japan, the European Union, and the United Kingdom.[7] In addition, the Trump Administration is reportedly considering possible trade agreements with a number of African countries (Ghana, Côte d'Ivoire, and Kenya). Along with these countries, the Administration should take a practical look at the following countries that have indicated a willingness to forge closer trade partnerships with the United States.

- **Switzerland.** The United States and Switzerland have a long history of practical partnership. Switzerland, a non-EU country located at the geographic heart of continental Europe, is a competitive and dynamic economy. The Swiss and U.S. economies have advanced and flourished on the foundation of market principles and the effective rule of law. More notably, a possible U.S.–Swiss free trade agreement uniquely presents a tangible and practical opportunity for moving forward President Trump's proposal for zero tariffs and zero barriers. Since December 2017, Switzerland has already removed tariffs on imported industrial goods.[8]

- **Taiwan.** Taiwan is an important free market democracy in the Indo–Pacific region and an active member of the WTO. Disappointingly, the United States and Taiwan have no broad trade pact to date. All that exists is the Trade and Investment Framework Agreement (TIFA)—essentially an agreement to meet on a regular basis to discuss and work toward resolving outstanding trade differences. It is typically held at the Deputy Secretary level by the United States Trade Representative. Furthermore, a TIFA

7. News release, "Trump Administration Announces Intent to Negotiate Trade Agreements with Japan, the European Union and the United Kingdom," Office of the United States Trade Representative, October 31, 2018, https://ustr.gov/about-us/policy-offices/press-office/press-releases/2018/october/trump-administration-announces (accessed October 31, 2018).
8. News release, "Federal Council Adopts Measures to Tackle High Prices in Switzerland," The Federal Council, Switzerland, https://www.admin.ch/gov/en/start/documentation/media-releases.msg-id-69321.html (accessed October 31, 2018).

meeting is long overdue, as there has been no meeting since October 2016. The U.S.–Taiwan relationship deserves far better than that.

- **Georgia.** A free trade agreement would be a win-win for the U.S. and Georgia. It would benefit Georgia by making the country a more attractive destination for international investment. It would also send an additional signal to Russia that Georgia is a strong friend and partner of the United States. Moving in a timely manner to implement a Georgia–U.S. agreement would promote economic freedom and prosperity in both countries and would serve U.S. economic and security goals in Eurasia.

- **Tunisia.** Against the odds, Tunisia has made measurable social progress largely on its own accord. Tunisia's great progress on the political fronts in no way lessens the need for policies that promote inclusive economic growth. The country's ongoing bottom-up democratic transition will not succeed without effective reforms that advance economic freedom for ordinary Tunisians. The U.S. should consider upgrading its current trade and investment relationship with Tunisia to a free trade agreement. Trade flows between the U.S. and Tunisia are relatively modest, and liberalization would bring important benefits with little disruption.

Advancing America's Freedom to Trade

The Trump Administration should build upon the momentum of recent decades to increase economic freedom and dynamic growth, not disrupt it with protectionist trade policy. Reducing the corporate tax rate and reining in abusive regulations were important steps toward freeing the U.S. economy. Protectionist trade policies, by contrast, could do real harm. Changes in trade policy alone are unlikely to reduce the trade deficit and could in fact widen it if other countries respond to U.S. protectionism with trade restrictions of their own. Such a course of events would lead to lower growth and reduced prosperity for Americans, both individuals and businesses.

The freedom to trade must be guarded and enhanced. The main threat to U.S. prosperity in recent years has come not from trade, but from a persistent decline in economic freedom in the U.S. In the ongoing process of revitalizing America's global competitiveness and economic dynamism, the Trump Administration has the unique opportunity to become an effective advocate for trade freedom and help America reap the rewards of free trade policies. It should not let the opportunity pass.

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APPENDIX TABLE A

2019 Trade Freedom Scores

Rank	Country	Score
1	Hong Kong	95.0
2	Singapore	94.8
3	New Zealand	92.4
4	Macau	90.0
5	Chile	88.8
6	Georgia	88.6
7	Mauritius	88.4
8	Albania	87.8
9-t	Australia	87.6
9-t	Eswatini	87.6
11	Switzerland	87.4
12-t	Iceland	87.0
12-t	Oman	87.0
12-t	Taiwan	87.0
15	Canada	86.8
16	**United States**	**86.6**
17	Peru	86.4
18-t	Austria	86.0
18-t	Belgium	86.0
18-t	Bulgaria	86.0
18-t	Croatia	86.0
18-t	Cyprus	86.0
18-t	Czech Republic	86.0
18-t	Denmark	86.0
18-t	Estonia	86.0
18-t	Finland	86.0
18-t	Germany	86.0
18-t	Hungary	86.0
18-t	Ireland	86.0
18-t	Italy	86.0
18-t	Latvia	86.0
18-t	Lithuania	86.0
18-t	Luxembourg	86.0
18-t	Malta	86.0
18-t	Netherlands	86.0
18-t	Poland	86.0
18-t	Portugal	86.0
18-t	Romania	86.0
18-t	Slovakia	86.0
18-t	Slovenia	86.0
18-t	Spain	86.0
18-t	Sweden	86.0
18-t	United Kingdom	86.0
44	Montenegro	84.7
45-t	Israel	84.4
45-t	United Arab Emirates	84.4
47	Brunei	84.0
48-t	Bahrain	83.8
48-t	Botswana	83.8
50-t	Norway	83.2
50-t	Qatar	83.2
52-t	Namibia	83.0
52-t	Thailand	83.0
54	Bosnia and Herzegovina	82.6
55	Guatemala	82.2
56-t	Macedonia	82.0
56-t	Malaysia	82.0
58	Laos	81.8
59-t	Costa Rica	81.4
59-t	El Salvador	81.4
59-t	Jordan	81.4
59-t	Mexico	81.4
59-t	Seychelles	81.4
64-t	France	81.0
64-t	Greece	81.0
64-t	Lesotho	81.0
67	Papua New Guinea	80.9
68	Armenia	80.8
69	Micronesia	80.6
70	South Korea	80.4
71-t	Japan	80.0
71-t	Kazakhstan	80.0
73	Indonesia	79.8
74	Turkey	79.6
75-t	Bhutan	79.4
75-t	Honduras	79.4
77-t	Panama	79.2
77-t	Vietnam	79.2
79-t	Kuwait	79.0
79-t	Lebanon	79.0
81-t	Kyrgyz Republic	78.6
81-t	Uruguay	78.6
83	Philippines	78.2
84-t	Moldova	78.0
84-t	Mozambique	78.0
86	Russia	77.8
87	Morocco	77.4
88	Serbia	77.0
89	Paraguay	76.6
90	Belarus	76.4
91	Sri Lanka	76.2
92-t	Colombia	76.0
92-t	Nicaragua	76.0
92-t	Saudi Arabia	76.0
92-t	South Africa	76.0
92-t	Turkmenistan	76.0
97-t	Dominican Republic	75.8
97-t	Mongolia	75.8
99-t	Malawi	75.4
99-t	Uganda	75.4
101-t	Timor-Leste	75.0
101-t	Ukraine	75.0
103	Azerbaijan	74.6
104-t	Côte d'Ivoire	73.6
104-t	Tajikistan	73.6
104-t	Tonga	73.6
107	Saint Lucia	73.2
108	China	73.0
109	Zambia	72.6
110	India	72.4
111-t	Haiti	72.0
111-t	Senegal	72.0
113	Egypt	71.8
114	Tunisia	71.4
115-t	Burma	70.8
115-t	Kosovo	70.8
117-t	Bolivia	70.4
117-t	Rwanda	70.4
119-t	Argentina	70.0
119-t	Comoros	70.0
119-t	Zimbabwe	70.0
122	Mali	69.8
123-t	Sierra Leone	69.4
123-t	Togo	69.4
125-t	Eritrea	69.2
125-t	Madagascar	69.2
127	Brazil	69.0
128-t	Jamaica	68.4
128-t	Trinidad and Tobago	68.4
130-t	Burundi	68.2
130-t	Cabo Verde	68.2
130-t	Dominica	68.2
133	Tanzania	67.8
134	Algeria	67.4
135	Guyana	66.8
136	St. Vincent & Grenadines	66.6
137	Ecuador	66.4
138	Afghanistan	66.0
139	Niger	65.8
140	Cambodia	65.4
141	Burkina Faso	65.2
142	Pakistan	64.8
143	Suriname	64.6
144	Vanuatu	64.4
145	São Tomé & Príncipe	64.2
146-t	Belize	64.0
146-t	Cuba	64.0
148	Samoa	63.8
149	Bangladesh	63.6
150	Ghana	63.4
151	Guinea	63.2
152	Fiji	62.8
153-t	Dem. Rep. Congo	62.6
153-t	Maldives	62.6
153-t	Mauritania	62.6
153-t	Uzbekistan	62.6
157	Nigeria	62.4
158	Benin	61.8
159	The Gambia	61.6
160	Angola	61.2
161	Ethiopia	60.8
162-t	Kenya	60.4
162-t	Nepal	60.4
164	Liberia	60.1
165	Venezuela	60.0
166-t	Republic of Congo	56.8
166-t	Solomon Islands	56.8
168	Barbados	56.6
169	Guinea-Bissau	55.6
170	Iran	54.6
171	Cameroon	53.4
172	Kiribati	53.2
173	Gabon	51.2
174	Central African Republic	51.0
175	Djibouti	50.4
176	Equatorial Guinea	48.8
177	The Bahamas	47.8
178	Chad	47.2
179	Sudan	45.0
180	North Korea	0.0

SOURCE: Heritage Foundation calculations from the *2019 Index of Economic Freedom* (forthcoming 2019).

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Appendix B: Methodology

Trade freedom is a composite measure of the extent of tariff and non-tariff barriers that affect imports and exports of goods and services. The trade freedom score reported in this *Backgrounder* is based on two inputs:

- The trade-weighted average tariff rate, and
- Non-tariff barriers (NTBs).

Different imports entering a country can (and often do) face different tariffs. The weighted average tariff uses weights for each tariff based on the share of imports for each good. Weighted average tariffs are a purely quantitative measure and account for the calculation of the base trade freedom score using the following equation,

$$\text{Trade Freedom}_i = 100(\text{Tariff}_{max}–\text{Tariff}_i)/(\text{Tariff}_{max}–\text{Tariff}_{min}) – \text{NTB}_i$$

where Trade Freedom_i represents the trade freedom in country i; Tariff_{max} and Tariff_{min} represent the upper and lower bounds for tariff rates (%); and Tariff_i represents the weighted average tariff rate (%) in country i. The minimum tariff is naturally zero percent, and the upper bound was set at 50 percent. An NTB penalty is then subtracted from the base score. The penalty of 5, 10, 15, or 20 points is assigned according to the following scale:

- **20**—NTBs are used extensively across many goods and services and/or act to impede a significant amount of international trade.
- **15**—NTBs are widespread across many goods and services and/or act to impede a majority of potential international trade.
- **10**—NTBs are used to protect certain goods and services and impede some international trade.
- **5**—NTBs are uncommon, protecting few goods and services, and/or have a very limited impact on international trade.
- **0**—NTBs are not used to limit international trade.

We determine the extent of NTBs in a country's trade policy regime using both qualitative and quantitative information. Restrictive rules that hinder trade vary widely, and their overlapping and shifting nature makes their complexity difficult to gauge. The categories of NTBs considered in our penalty include:

- **Quantity restrictions**—import quotas; export limitations; voluntary export restraints; import–export embargoes and bans; and countertrade, etc.
- **Price restrictions**—antidumping duties; countervailing duties; border-tax adjustments; and variable levies/tariff rate quotas.
- **Regulatory restrictions**—licensing; domestic content and mixing requirements; sanitary and phytosanitary standards (SPSs); safety and industrial standards regulations; packaging, labeling, and trademark regulations; and advertising and media regulations.
- **Customs restrictions**—advance deposit requirements; customs valuation procedures; customs classification procedures; and customs clearance procedures.
- **Direct government intervention**—subsidies and other aid; government industrial policies; government-financed research and other technology policies; competition policies; government procurement policies; and state trading, government monopolies, and exclusive franchises.

As an example, Vietnam received a trade freedom score of 79.2. By itself, Vietnam's trade-weighted average tariff of 2.9 percent would have yielded a score of 94.2, but the existence of NTBs in Vietnam reduced its score by 15 points.

Gathering tariff statistics to make a consistent cross-country comparison is a challenging task. Unlike data on inflation, for instance, some countries do not report their weighted average tariff rate or simple average tariff rate every year.

To preserve consistency in grading the trade freedom component, the *Index* uses the most recently reported weighted average tariff rate for a country from our primary source. If another reliable source reports more updated information on the country's tariff rate, this fact is noted, and the grading of this component may be reviewed if there is strong evidence that the most recently reported weighted average tariff rate is outdated.

The most comprehensive and consistent information on weighted-average applied tariff rates is published by the World Bank. When the weighted-average applied tariff rate is not available, the *Index* uses the country's average applied tariff rate; and when the country's average applied tariff rate is not available, the weighted average or the simple average of most favored nation (MFN) tariff rates is used. In the very few cases where data on duties and customs revenues are not available, data on international trade taxes or an estimated effective tariff rate are used instead. In all cases, an effort is made to clarify the type of data used in the corresponding write-up for the trade freedom component.

Sources: The *Index* relies on the following sources in determining scores for trade policy, in order of priority: World Bank, World Development Indicators; World Trade Organization, Trade Policy Review; Office of the U.S. Trade Representative, National Trade Estimate Report on Foreign Trade Barriers; World Bank Doing Business; U.S. Department of Commerce, Country Commercial Guide; Economist Intelligence Unit, Country Commerce; World Economic Forum, The Global Enabling Trade Report; and official government publications of each country.