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International Trade Developments

Preferential Trade Agreements and the Multilateral Trading System

ASEAN Free-Trade Area Discussions on Including China, Japan, and South Korea

U.S. Trade Developments

International Economic Comparisons

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Robert B. Koopman, *Director*

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INTERNATIONAL TRADE DEVELOPMENTS

Preferential Trade Agreements and the Multilateral Trading System

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Does the current proliferation of preferential trading agreements (PTAs) encourage or impede evolution toward freer global trade? Does it perhaps even increase the likelihood of trade tensions between competing trading blocs? The article presents two models that show how PTAs could affect the multilateral trading system. One model suggests that global free trade may—or may not—be achieved through PTA expansion, depending on a PTA's membership policies. The second model suggests that the greater the degree of preference between the PTA and nonmembers, the less likely PTA members will be willing to undertake multilateral trade liberalization and the more likely nonmembers will be, to support large-scale multilateral liberalization.

As a guiding principle, the multilateral trading system–organized under the auspices of the World Trade Organization (WTO)–is based upon the concept of "most-favored-nation" and "nondiscriminatory" treatment of all WTO members. During the last two decades, however, a growing number of WTO members have begun to explore alternatives to multilateral trade liberalization–in the form of preferential trading agreements (PTAs).[2] By design, these PTAs grant more favorable conditions to trade with other parties to the agreement than to trade with WTO members. Although PTAs clearly depart from the overarching WTO principle of "nondiscrimination," they are permitted under specific conditions spelled out in GATT Article XXIV, the so-called 1979 Enabling Clause, and in GATS Article V.

PTAs have flourished all over the world. Nearly all of the 140 WTO members are now party to at least one agreement.[3] Feeling that progress through WTO talks is too slow, even countries traditionally opposed to the preferential approach are now looking at PTAs as an alternative route to further trade liberalization. For instance, until very recently, Japan has relied completely on the multilateral system, but is now actively pursuing different PTAs with South Korea, Singapore, Mexico, and Canada. South Korea opposed preferential deals in the past, but is negotiating now with New Zealand and Chile as well as Japan.

The "Regionalism versus Multilateralism" Debate

The inherently discriminatory nature of PTAs—in contrast to multilateral trade liberalization—can be harmful to both member and nonmember nations. Although PTAs can create trade, they can also divert

[1] The views and conclusions expressed in this article are those of the author. They are not necessarily the views of the U.S. International Trade Commission as a whole or of any individual Commissioner.

[2] PTAs can take different forms ranging from free-trade areas such as the Latin American Free-Trade Area (LAFTA), or the North American Free-Trade Area (NAFTA); to monetary unions such as the European Union (EU) and customs unions such as the Mercado Común del Sur (Mercosur).

[3] As of May 2000, 127 PTAs have been notified to the GATT/WTO and are in force, of which 100 are under GATT Article XXIV, 17 under the Enabling Clause, and 11 under GATS Article V. See http://www.wto.org/english/tratop_e/region_e/region_e.htm.

trade away from lower cost producers in nonmember countries.[4] Although it is possible to reconcile preferential trading with progress toward freer global trade, policy analysts have identified two big dangers: (1) slower or even blocked multilateral liberalization, and (2) leaving aside of the world's poorest countries. It is therefore important that policymakers understand the relationships between PTAs and the multilateral trading system. Does preferential trading encourage evolution toward globally freer trade, or does it place impediments in its way, and perhaps even increase the likelihood of trade wars between competing trading blocs? This forms the nub of the "Regionalism versus Multilateralism" debate.[5]

In parallel to the proliferation of PTAs, the academic literature on the subject has thrived in recent years, focusing in particular on two dimensions of the issue. One dimension pertains to the dynamics of PTA formation and asks whether PTAs have a tendency to expand their memberships or to merge, and whether this tendency will continue until it culminates in global free trade. The second dimension concerns the effects of the establishment of a PTA on the member and nonmember countries' incentives for multilateral trade liberalization.

The remainder of this article presents two models that could be useful in thinking respectively about these two dimensions. One model about membership dynamics shows that globally free trade may or may not be achieved through PTA expansion depending on the PTA membership policies. A second model focusing on producers' influence shows that the greater the degree of preference in the PTA, the less is the magnitude of multilateral trade liberalization that PTA members are willing to undertake and the greater is the nonmember countries' support for large scale multilateral liberalization.

The "Dynamics" of PTA Formation: Stagnant or Expanding Membership?

Will PTAs continue to expand and merge until one super PTA encompassing the entire world is left? This process has been termed "domino regionalism" by Richard Baldwin, who uses a political economy model to show how the expansion of a PTA increases the incentives of the outsiders to apply for membership.[6] He argues that the most recent wave of regionalism was caused by two idiosyncratic events (namely, the 1994 North American Free-Trade Agreement or NAFTA, and the European Communities' EC 1992 program), multiplied by a "domino effect." Baldwin's results suggest a continuous expansion of the PTA that will stop only when all remaining outsiders conclude they will incur loss of domestic market share and other costs that more than offset preferential market-access and other gains by becoming members of the PTA. One direct implication of his result is that if membership were open (i.e. member countries cannot prevent nonmembers from joining), and if noneconomic factors (e.g. security or sovereignty motives) against seeking entry were absent, regionalism would lead to global free trade.

Baldwin's analysis, though insightful, tells one part of the story but it fails to consider the incentives of the PTA members to keep other countries out of the arrangement. After all, the formation and expansion of a trading bloc require a "coincidence of wants" among all interested parties—members and nonmembers. Both nonmembers must want to join the PTA and, at the other end, the members must be willing to accept them as new members. Therefore, a complete analysis of the issue should also look at the incentives of the members to accept or reject new members. Soamiely Andriamananjara investigates the effects of the formation or expansion of a PTA on members, nonmembers, and the world as a whole.[7] He demonstrates that an expansion of a regional grouping always unambiguously hurts those left out (even if the external tariffs of the PTA remain constant). He also shows that the effects of an expansion on a member country are positive for small PTAs, but become negative as the PTA membership grows more numerous.

Consider an outsider country contemplating entry into a trading bloc. Its choice is determined by the trade-off between the costs of opening up one's own market to more foreign competition and the gains from obtaining better, preferential access to the PTA preferential market. In the context of Andriamananjara's model, it can be shown that the market-access gain is

[4] The seminal work on the trade-creation/trade-diversion tradeoff is by Jacob Viner, *The Customs Union Issue* (Washington DC: Carnegie Endowment for International Peace, 1950).

[5] For a survey of this literature, Jagdish Bhagwati and Arvind Panagariya, "Preferential Trading Areas and Multilateralism—Strangers, Friends, or Foes?" in J. Bhagwati and A. Panagariya, eds., *The Economics of Preferential Trade Agreement* (Washington DC: American Enterprise Institute Press, 1996).

[6] Richard Baldwin, "A Domino Theory of Regionalism," *NBER Working Paper* 4364 (NBER: Cambridge MA, 1995).

[7] For more details on the model, see Soamiely Andriamananjara, "On the Size and Number of Regional Integration Arrangements: A Political Economy Model," *World Bank Policy Research Working Paper* 2117 (World Bank: Washington DC, 1999).

always larger than the costs of allowing entry, as long as the aggregate size of the PTA market exceeds that of the prospective member. Since the larger the PTA, the more an outsider stands to gain from joining, the incentive of a nonmember country to apply for membership increases with the size of the PTA. Outsider countries that initially had little interest in joining the PTA may become interested when the PTA size becomes large enough. According to this model, an outsider would always want to apply for membership to an existing bloc. Thus, *if the PTA had an open membership policy, it would likely continue to expand until global free trade is achieved.*

Consider next the incentives of the PTA members. If member countries could choose to accept or reject new members, the expansion of the bloc is probably not likely to yield global free trade. In fact, when deciding whether to accept or reject a new member, a PTA member compares the gains from getting preferential access to the new member's market against the losses of having to share its original preferential market with the new member—the pie is getting larger but it also has to be shared by more members. For a small bloc size, the gains are large enough to offset the losses so that the insiders are willing to accept new members. As the bloc expands, however, the insider's incentives for further PTA expansion decrease and eventually go to zero before the PTA encompasses the entire world. Hence, *the expansion of a PTA fails to lead to global free trade when PTA membership is selective* (i.e. a PTA grants membership to a new member if and only if all existing members agree to admit the new member) because it implies a reduction of the PTA members' welfare from the levels that they achieve when only a limited number of countries are members.[8] In fact, at some point, the members will refuse to admit new members as "congestion" characteristics of the PTA start to kick in, whereby bureaucratic rigidities may begin to impose additional costs that hamper gains from expanded market access within the PTA.

So far, the process being considered is one in which only one PTA forms and expands at any given time. One can also look at an alternative process whereby PTAs form more or less symmetrically and merge simultaneously to yield progressively larger blocs. Will this continue so as to yield one single bloc, which is global free trade? In this model, it can be shown that in this simultaneous bloc expansion, the regionalism process fails to converge into a single bloc except when the external tariff happens to be low enough. This is an example of open regionalism, based on low external tariffs, leading to multilateral free trade. One direct implication of this is that *global free trade can be achieved through bloc expansion if trading blocs lower their external tariffs, as well as lower and eliminate their own internal tariffs.*

PTAs and Incentives for Multilateralism

The second dimension in the "Regionalism versus Multilateralism" debate is to study the effects of the establishment of the PTA incentives for nondiscriminatory trade liberalization. This is particularly relevant given that preferential trade policies alter the balance of gains and losses that members and nonmembers experience from multilateral trade liberalization. In a recent contribution to the literature, Pravin Krishna uses a three-country model to show that a PTA between two countries reduces the incentives to liberalize tariffs reciprocally with the third country. He also demonstrates that, given sufficient trade is diverted away from nonmembers, multilateral liberalization that was feasible before the PTA formed ceases to be so afterwards.[9]

One can use a simple model to study the effects of regional integration on the incentives of PTA members and nonmembers to undertake multilateral trade liberalization (i.e. reciprocal trade liberalization among members and nonmembers).[10] Consider a world with three countries, two of which are potential PTA members. Assume that the producers' profits play a decisive role in determining a country's trade policies; that is, the gains and losses of domestic producers drive decisions regarding trade liberalization.[11]

Consider a representative firm in one of the potential PTA members. In this model, multilateral trade liberalization has two opposing effects on the profits of that firm: (i) it decreases the profits it makes in the local market as reduced domestic protection produces more competition from abroad, and (ii) it increases the profits it makes abroad (in both other members' and nonmembers' markets) as it gets better access to other

[8] When the PTA members decide to stop further expansion, the rejected countries have an incentive to form their own PTA. The model demonstrates that the possibility of a second bloc leads the members of the original bloc to preempt the losses associated with the creation and enlargement of a second PTA by choosing a group size larger than the one they would have chosen if only one bloc were allowed to form. Hence, the threat of regionalism by outsiders forming additional blocs in competition would encourage previous blocs toward larger PTAs.

[9] When the PTA members decide to stop further expansion, the rejected countries have an incentive to form their own PTA. The model demonstrates that the possibility of a second bloc leads the members of the original bloc to preempt the losses associated with the creation and enlargement of a second PTA by choosing a group size larger than the one they would have chosen if only one bloc were allowed to form. Hence, the threat of additional competition from a second bloc would encourage the first bloc to expand.

[10] Pravin Krishna, "Regionalism and Multilateralism: A Political Economy Approach," *Quarterly Journal of Economics*, vol. 113, No. 1 (1998) pp. 227-251.

[11] Other political economy models may include consumer welfare or tariff revenues as determinants of trade policy.

countries' markets. As the degree of preference rises, it can be shown that the domestic profit loss from multilateral liberalization increases (i.e. the first effect is strengthened) and the profit gain in the other member countries decreases (i.e. the second effect is weakened).[12] This makes the insiders more reluctant to undertake larger scale multilateral liberalization: the more preference an insider gives and gets from other insiders, the less market access it is willing to give up in exchange for that received from outsiders. The simple model therefore offers an example of how *an increase in the degree of preference in the PTA can reduce a PTA member's willingness to undertake larger scale multilateral trade liberalization*.

Consider next the changes in the incentives of a representative firm in the excluded or "outsider"country. Multilateral trade liberalization increases the firm's profits in the PTA market, but decreases those made in its own domestic market. An increase in the level of discrimination that it faces (that is, the level of preference between the PTA members and outsiders) leaves domestic profits unchanged but decreases its profits in the PTA market due to trade diversion from nonmember to member countries. Given these different effects, it can be analytically shown that *the larger the level of preference enjoyed by PTA members, the larger is the excluded country's support for larger scale multilateral liberalization*. Small tariff cuts are not enough to offset the excluded country's profit losses from the trade diversionary effects of the PTA.

Conclusion

The models summarized and discussed in this article are theoretical in nature, based admittedly on stylized assumptions. In practice, incentives vary from country to country, as well as among different types of PTAs. Moreover, some PTAs have been established for political reasons that extend beyond solely economic reasons.

Keeping these limitations in mind, the foregoing discussion could still be useful in thinking about the incentives of members and nonmembers and the implications of the recent proliferation of PTAs on the global trading system. Does preferential trading encourage or impede evolution toward globally freer trade, perhaps even increasing the likelihood of trade tensions or "trade wars" between competing trading blocs? Although it is beyond the scope of this article to offer any specific policy implications, a number of general conclusions emerge from the discussion that could be useful in designing future preferential trade initiatives.

- If a PTA has an open membership policy, it may well continue to expand until global free trade is reached.
- If PTA membership is selective, global free trade is unlikely to be achieved through PTA expansion.
- In a world where more than one PTA forms simultaneously, global free trade can be reached through sequential PTA mergers if (and only if) the trading blocs' external tariffs are not too high.
- The greater the degree of preference in the PTA, the lesser is the magnitude of multilateral trade liberalization that PTA members are willing to undertake.
- The greater the degree of preference in the PTA, the greater is the nonmember countries' support for large scale multilateral liberalization.

[12] The term "degree of preference" refers here to the difference between tariffs charged to PTA members and those charged to nonmembers.

ASEAN Free-Trade Area Discussions on Including China, Japan, and South Korea

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Leaders from the 10 member countries of the Association of Southeast Asian Nations (ASEAN) met in November 2000, and agreed to initiatives aimed at promoting further economic integration in the region. Leaders from China, Japan, and South Korea also joined in these discussions, in what has become known as the "ASEAN-plus-three" meetings. Among the agreed proposals was one to study the impact of creating an ASEAN free-trade area that would include China, Japan, and South Korea.

Leaders from the 10 member countries of the Association of Southeast Asian Nations[2] (ASEAN) met in November 2000 in Singapore, concluding a number of initiatives aimed at promoting further cohesion and economic integration of the ASEAN area. In what has been dubbed "ASEAN-plus-three" meetings, leaders from China, Japan, and South Korea also attended, and reached agreement on a proposal to study the impact of including China, Japan, and South Korea within the ASEAN free-trade area. An overview of the agreements discussed at the ASEAN November meetings follows.[3]

Agreements reached among ASEAN members included an "e-ASEAN" agreement on electronic commerce, several cooperation initiatives on technical assistance and worker training programs, and a plan to relax selected tariff reduction deadlines set under the ASEAN Free-Trade Agreement (AFTA). Agreements reached within the ASEAN-plus-three framework included accelerating construction of the Trans-Asian Railway between Singapore and the Chinese city of-Kunming, a regional Currency Swap Crisis Pact, a proposal to formalize ASEAN-plus-three meetings into a more official "East Asian Summit," and finally a proposal to study the impact of creating an ASEAN free-trade area that would include China, Japan, and South Korea.

Asian Integration[4]

The ASEAN meetings and discussions of possible trade agreements with China, Japan, and South Korea are one of several recent moves toward regional integration in Asia. Singapore has reached a free-trade agreement with New Zealand, and is currently negotiating agreements or considering such with Australia, Canada, Japan, Mexico, and the United States. New Zealand has been negotiating with Chile and Hong Kong. Japan and South Korea have explored the idea of freer trade with each other as well as with other countries. Japan's international trade minister, Takeo Hiranuma, states that Japanese companies particularly want an agreement with Mexico, because their subsidiaries are facing the elimination of a tariff exemption on imported parts used in products they export to the United States. China is still completing negotiations for WTO accession, but has also suggested interest in regional trade agreements. Although the relationship between regional trade agreements and the process of multilateral trade liberalization remains a topic of discussion for economists and policymakers (see related article in this *IER*), leaders of Asian countries appear to

[1] The views and conclusions expressed in this article are those of the author. They are not necessarily the views of the U.S. International Trade Commission as a whole or of any individual Commissioner.

[2] Members of ASEAN include Brunei Darussalam, Cambodia, Indonesia, Laos, Malaysia, Myanmar (Burma), Philippines, Singapore, Thailand, and Vietnam.

[3] Sources consulted for this article include ASEAN Secretariat, "The Fourth ASEAN Informal Summit: Press Statement by the Chairman, Singapore, Nov. 25, 2000," found at internet address http://www.asean.or.id/summit/infs4_cps.htm, retrieved Dec. 20, 2000; U.S. Department of State telegram, message reference No. 03227, "Singapore - ASEAN and ASEAN Plus Three Meet to Discuss Regional Integration," Dec. 1, 2000; BNA, "International Agreements: ASEAN Leaders Pledge to Study Possibility of Northeast Asian Trade Zone," *International Trade Daily*, Nov. 28, 2000; and "China and ASEAN: The Best Things in Life," *The Economist*, Dec. 8, 2000.

[4] Sources consulted for this section include: ASEAN Secretariat, "The ANGKOR Agenda: Report on the High-Level Task Force on the AFTA-CER Free Trade Area," Sept. 2000.

be using both routes to achieve freer trade in the region.

Agreement to Study an ASEAN-plus-three FTA

In this context, ASEAN members met during their November 2000 meetings with officials from China, Japan, and South Korea to discuss proposals to form a free-trade area (FTA) that would include all 10 ASEAN as well as these three additional East Asian countries. A working party headed by South Korea was formed to research the impact of forming an ASEAN-plus-three FTA, and leaders agreed to discuss the results of the report at the next ASEAN-plus-three meeting, scheduled for 2001 in Brunei. Singapore's Prime Minister Goh Chok Tong emphasized that the working group would only study the idea, and that if any type of FTA were to be implemented, it would be over the long term. An official from the Chinese Foreign Ministry stated before the meetings that "China stands ready to explore the possibility of setting up links with the ASEAN free-trade area or of creating a free-trade zone between China and ASEAN." For Japan, an important issue will be the impact any such agreement will have on its relatively high agricultural trade protection. For ASEAN members, the impact on both regional trade and investment flows will be a key point of interest. China has been attracting trade and investment away from ASEAN members in recent years. Before the 1997 Asian financial crisis, ASEAN's share of foreign direct investment attracted to Asia's developing economies was approximately 30 percent; last year, however, this share had fallen to 15 percent.[5]

Significant ASEAN exports to China, South Korea, and Japan include machinery and electrical appliances, mineral products, wood and wood articles, and prepared foodstuffs. The largest ASEAN imports from Japan include chemicals, plastics, machinery and electrical appliances, and motor vehicles. From China, ASEAN imports include machinery and electrical appliances, textiles and apparel, base metals, and metal articles. From South Korea, ASEAN imports include machinery and electrical appliances, mineral products, base metals, and metal articles. ASEAN's largest export partners are the United States, Japan, the European Union, and Hong Kong. Its largest import partners are Japan, the United States, the European Union, South Korea, and China.

[5] "Taiwan Hopes to Strengthen Trade Ties with China, ASEAN Considers China Free Trade Zone," *World Trade*, Feb. 2001, p. 18.

Agreements within the ASEAN-plus-three Framework[6]

China, Japan, South Korea, and ASEAN members agreed to expand work on the $2.5 billion Trans-Asian railway, which will stretch from Singapore in the south to Kunming, China in the north. The project is to be completed by 2006, and has been put under the authority of the Mekong Basin Development Program.[7] The Mekong program is meant to boost economic development in Cambodia, Laos, Myanmar, Thailand, and Vietnam. Areas of particular focus include the development of infrastructure in transport, telecommunications, irrigation, and energy. The Mekong program also seeks to promote development of trade and investment, and development of the agricultural sector.

Another proposal raised at the Singapore meetings was to turn the informal ASEAN-plus-three meetings into a more formal "East Asian Summit." Singapore's Prime Minister Goh Chok Tong said that any such grouping in Asia would not be aimed against any particular country, such as the United States. He said ASEAN "needs the United States in East Asia. This is not an attempt to shut out Washington from East Asia."

The Currency Swap Crisis Pact announced at the ASEAN meetings in Singapore will create a mechanism to help avoid future currency crises within the region. The pact creates a network of bilateral currency swaps, giving participating ASEAN-plus-three countries experiencing short-term liquidity shortfalls an avenue to borrow funds without having to undertake IMF austerity measures.[8] Central banks in the ASEAN-plus-three countries will provide funds to stabilize currencies, and will have the ability to borrow from each other under re-purchase agreements. Lenders will hold various securities from borrowers until the latter repays the swap loan. Swaps conducted outside of an IMF framework will be limited to a duration of 1 year.

[6] Sources consulted for this section include: ASEAN Secretariat, "ASEAN Trade with Major Trading Partners," found at Internet address http://www.aseansec.or.id/stat/extra7.htm, retrieved Jan. 15, 2001; *Financial Times*, "Beijing Signals Trade Pact Interest," Nov. 22, 2000; *Inside US Trade*, "China Premier Zhu Hints at FTA Negotiations with ASEAN," Nov. 27, 2000, found at internet address http://www.insidetrade.com, retrieved Dec. 14, 2000; and "Asian Ambition," *Financial Times*, Nov. 28, 2000.

[7] The Mekong River in Southeast Asia flows approximately 2,600 miles from Southeast China to the South China Sea, creating a vast delta in southern Vietnam known as the Mekong Basin, which is a major rice-producing region.

[8] The IMF has several programs that lend money to countries with liquidity problems. Some of the lending is subject to austerity measures, in which the borrowing country must, for example, improve its fiscal balance or tighten its monetary policy.

Agreements within ASEAN[9]

During the ASEAN meetings, an emphasis was put on bridging a perceived gap between the more developed ASEAN members (Brunei, Indonesia, Malaysia, the Philippines, Singapore, and Thailand) and ASEAN's four newer members (Cambodia, Laos, Myanmar, and Vietnam). The e-ASEAN framework agreement on electronic commerce agreed at the these meetings aims to narrow the divide between higher and lower tech ASEAN countries. Specific goals include increasing Internet connectivity, greater incorporation of local materials (so-called local content), further development of e-commerce, and the liberalization of trade in information and communications technology. In addition, the e-ASEAN framework calls for further development of human resources and worker training, and a proposal to expand "e-governance," which would put government information on-line for public access. Several measures discussed were aimed at increasing trust and confidence in the Internet, including the establishment of a system of mutual recognition of digital signatures, systems to guarantee secure electronic transactions, protection of intellectual property rights, protection of personal data and consumer privacy, and mechanisms to aid the settlement of disputes. Finally, under the e-ASEAN agreement, import duties and non-tariff barriers to intra-ASEAN trade in computer-related goods are to be phased out over time. The phase-outs will begin in January 2003 for the six original ASEAN members, and in 2008 for the four newer members.

A fourth proposal discussed at the meetings was the creation of an Asian information technology (IT) belt, which would electronically link the higher tech cities of the ASEAN-plus-three grouping, such as Bangkok, Kuala Lumpur, Seoul, Shanghai, Singapore, and Tokyo. To achieve this goal, Japan and China both pledged significant funding, aimed at helping ASEAN-plus-three countries improve their IT infrastructure. Japan also announced that it will host a major IT conference for Asia in 2001.

In a separate agreement, ASEAN members announced the "Initiative for ASEAN Integration" (IAI) which includes several measures aimed at worker training, technical assistance, and increasing human capital in Asia. Under a 5-year technical assistance program, Singapore agreed to open special training institutes in Cambodia, Laos, Myanmar, and Vietnam. These institutes will provide vocational training to researchers in the fields of trade development, export promotion, human resource development, agriculture and food business, technical training, and tourism. Courses will include information technology "Train-the-Trainers" seminars to improve IT skills in the four countries. Singapore also agreed to increase its annual grant of scholarships from 30 to 60 per year. The full-time undergraduate scholarships are for citizens of ASEAN countries to study at either the National University of Singapore (NUS) or Nanyang Technical University of Singapore (NTS). Finally, the IAI included a program to sponsor youth exchange programs at primary ("youth") and secondary school levels, aimed as well at promoting regional integration.

Finally, ASEAN members agreed to relax tariff reduction deadlines that had been set under the ASEAN Free-Trade Agreement (AFTA). AFTA was launched at the Fourth ASEAN Summit in Singapore in January 1992, when member countries adopted the Common Effective Preferential Tariff (CEPT) to give ASEAN members uniform preferential tariff treatment in intra-ASEAN trade. The original time table had been to reduce tariff rates to a range of 0 to 5-percent duty on 85 percent of products traded within the ASEAN region by the year 2000, on 90 percent of products by 2001, and on all products by 2002. To be eligible, goods were subject to a 40-percent ASEAN local-content rule. The recent agreement to delay these tariff reductions was prompted by the Malaysian government, which sought to retain its existing tariffs on automobiles.

[9] Sources consulted for this section include: Donghyun Park, "The Prospects for Further Economic Integration in ASEAN," *Journal of Economic Integration*, vol. 14, No. 3, Sept. 1999.

U.S. TRADE DEVELOPMENTS

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The U.S. Department of Commerce (Commerce News FT 900 (00-09)) reported that seasonally adjusted exports of goods and services of $92.4 billion and imports of $126.6 billion in September 2000 resulted in a goods and services trade deficit of $34.4 billion, $4.5 billion (15.4 percent) more than the $29.8 billion deficit of the month of August 2000. September 2000 exports of goods and services were $0.6 billion less than August 2000 exports of $93.0 billion. September 2000 imports of goods and services were $3.8 billion more than August 2000 imports of $122.8 billion.

September 2000 merchandise exports decreased to $67.3 billion from $68.0 billion in August 2000. Merchandise imports increased to $107.5 billion from $104.7 billion, causing the merchandise trade deficit to increase to $40.2 billion from $36.7 billion, an increase of 9.5 percent. For services, exports were virtually unchanged at $25.0 billion but imports of services increased to $19.1 billion from $18.1 billion, resulting in a surplus of $5.9 billion on trade in services, about $1.0 billion lower than the August surplus of $6.9 billion.

Exports of merchandise goods in August-September 2000 reflected decreases in capital goods; automotive vehicles, parts and engines; consumer goods; and foods, feeds, and beverages; as well as other product categories. An increase occurred in exports of industrial supplies and materials. Imports of merchandise goods reflected increases in industrial supplies and materials, capital goods, and consumer goods. A decrease occurred in other product categories. Automotive vehicles, parts and engines, and foods, feeds, and beverages were virtually unchanged. Additional information on U.S. trade developments in agriculture and specified manufacturing sectors, in January-September 2000, are highlighted in tables 1 and 2 and figures 1 and 2. Services trade developments are highlighted in table 3.

[1] The views and conclusions expressed in this article are those of the author. They are not necessarily the views of the U.S. International Trade Commission as a whole or of any individual Commissioner.

Table 1
U.S. trade in goods and services, seasonally adjusted, Aug.-Sep. 2000
(Billion dollars)

Item	Exports		Imports		Trade balance	
	Sep. 2000	Aug. 2000	Sep. 2000	Aug. 2000	Sep. 2000	Aug. 2000
Trade in goods (see note)						
Current dollars–						
Including oil	67.3	68.0	107.5	104.7	-40.2	-36.7
Excluding oil	66.8	67.7	96.2	94.0	-29.4	-26.3
Trade in services						
Current dollars	25.0	25.0	19.1	18.1	6.0	6.9
Trade in goods and services:						
Current dollars	92.4	93.0	126.6	122.8	-34.3	-29.8
Trade in goods (Census basis)						
1996 dollars	74.5	75.6	114.9	112.8	-40.4	-37.3
Advanced-technology products (not seasonally adjusted)	20.1	19.7	21.2	20.1	-.1	-0.4

Note.—Data on goods trade are presented on a balance-of-payments (BOP) basis that reflects adjustments for timing, coverage, and valuation of data compiled by the Census Bureau. The major adjustments on BOP basis exclude military trade, but include non-monetary gold transactions and estimates of inland freight in Canada and Mexico not included in the Census Bureau data. Because of rounding details may not add to totals shown.

Source: U.S. Department of Commerce News (FT 900), Nov. 21, 2000

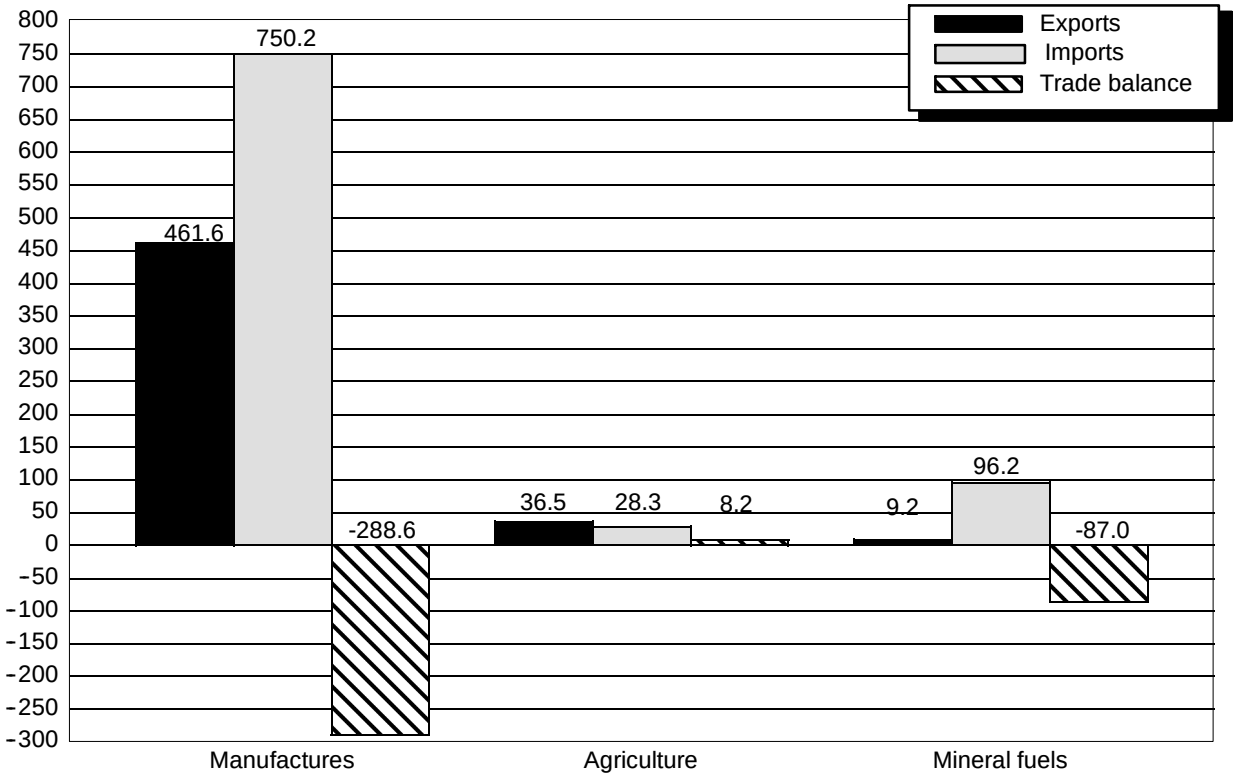
Table 2
Nominal U.S. exports and trade balances, of agriculture and specified manufacturing sectors, Jan.1999 Sep. 2000

	Exports		Change Jan.-Sep. 2000 over Jan.-Sep. 1999	Share of total Jan.-Sep. 2000	Trade balance	
	Sep. 2000	Jan.-Sep. 2000			Jan.-Sep. 2000	Jan.-Sep. 1999
	Billion dollars		*Percentage*		*Billion dollars*	
ADP equipment & office machinery	4.3	33.9	13.8	5.9	-34.0	-31.7
Airplanes	1.7	18.3	-23.8	3.2	9.8	17.3
Airplane parts	1.3	11.1	-3.5	1.9	7.0	7.1
Electrical machinery	8.3	65.9	20.0	11.4	-14.2	-9.1
General industrial machinery	2.7	24.4	9.9	4.2	-2.0	-1.3
Iron & steel mill products	0.5	4.3	16.2	0.7	-8.2	-6.2
Inorganic chemicals	0.5	4.0	17.6	0.7	-0.5	-0.3
Organic chemicals	1.5	13.3	20.9	2.3	-7.6	-5.0
Power-generating machinery	2.8	24.4	7.0	4.2	-1.0	-0.3
Scientific instruments	2.6	22.2	18.1	3.8	6.2	6.0
Specialized industrial machinery	2.6	22.8	24.6	3.9	5.6	1.9
Televisions, VCRs, etc	2.6	20.6	17.0	3.6	-29.3	-17.9
Textile yarns, fabrics and articles	0.9	7.9	14.5	1.4	-3.7	-3.3
Vehicles	4.5	42.6	6.5	7.4	-76.8	-66.1
Manufactured exports not included above	16.3	145.9	12.5	25.3	-139.9	-120.7
Total manufactures	53.1	461.6	11.3	79.9	-288.6	-229.6
Agriculture	4.0	36.5	8.3	6.3	8.2	6.4
Other exports not included above	10.0	79.3	32.6	13.7	-40.6	-14.0
Total exports of goods	67.1	577.4	13.6	100.0	-321.0	-237.2

Note.—Because of rounding, figures may not add to the totals shown. Data are presented on a Census basis.

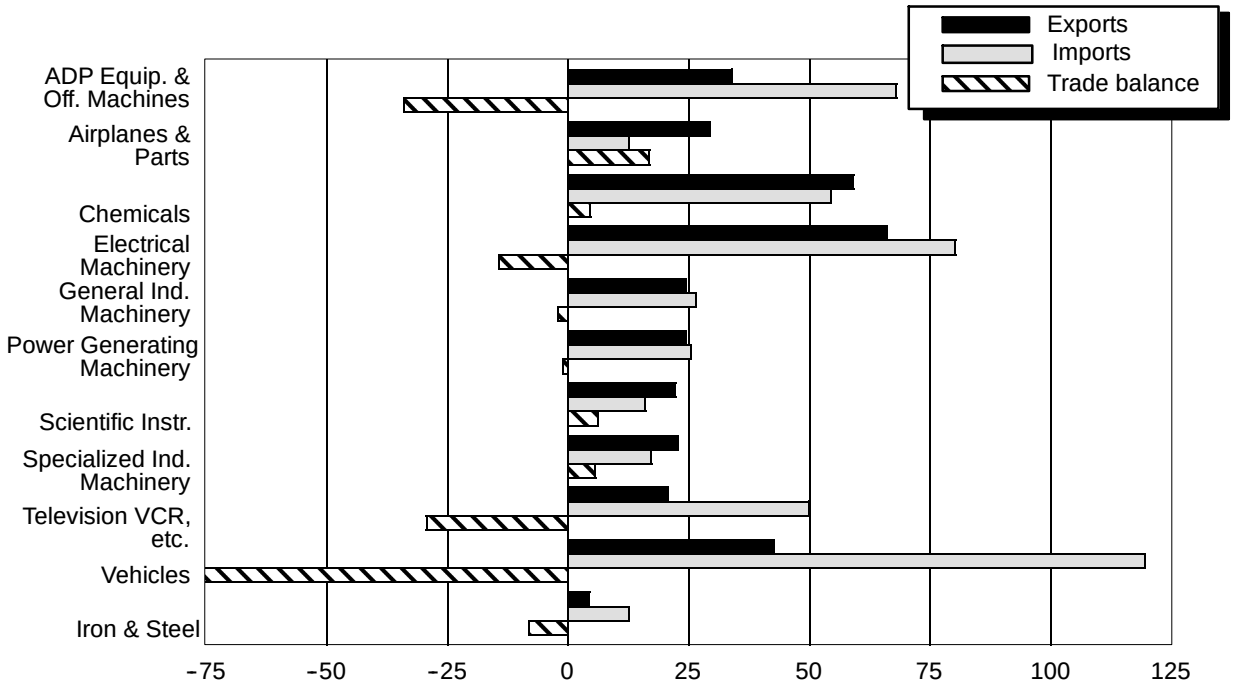
Source: U.S. Department of Commerce News (FT 900), Nov.21, 2000

Figure 1
U.S. trade by major commodity, billion dollars, Jan.-September 2000



Source: U.S. Department of Commerce, FT 900 (00-07).

Figure 2
U.S. trade in principal goods, billion dollars, Jan.-September 2000



Source: U.S. Department of Commerce, FT 900 (00-07).

Table 3
Nominal U.S. exports and trade balances of services, by sectors, Jan.1999-Sep. 2000, seasonally adjusted

	Exports		Change Jan.-Sep. 2000 over Jan.-Sep. 1999	Trade balances	
	Jan.-Sep. 2000	Jan.-Sep. 1999		Jan. Sep. 2000	Jan.-Sep. 1999
	Billion dollars		*Percent*	*Billion dollars*	
Travel	62.6	55.4	13.0	14.0	11.3
Passenger fares	15.4	14.8	4.1	-2.6	-1.0
Other transportation	22.2	19.9	11.6	-7.5	-5.0
Royalties and license fees	28.9	27.4	5.5	17.1	17.8
Other private sales	79.7	71.4	11.6	41.0	36.6
Transfers under U.S. military sales contracts	10.9	12.8	-14.8	0.8	2.5
U.S. Govt. miscellaneous service	0.6	0.7	-14.3	-1.6	-1.4
Total	220.4	202.3	8.8	61.2	60.8

Source: U.S. Department of Commerce News (FT 900), Nov.21, 2000.

Note.—Services trade data are on a balance-of-payments (BOP) basis. Numbers may not add to totals because of seasonal adjustment and rounding.

In September 2000, exports of advanced technology products increased slightly to $20.1 billion from $19.7 billion in August. Imports of the same increased to $21.2 billion in September 2000 from $20.1 billion in August 2000, resulting in a September deficit of $1.1 billion higher than the August deficit of $0.4 billion.

The September 2000 trade data showed U.S. surpluses with Australia, Argentina, Brazil, Egypt, and Hong Kong. Deficits were recorded with Canada, Mexico, Western Europe, China, Japan, Korea, Taiwan, Singapore, and OPEC member countries.

The export of goods and services during January-September 2000 increased to $796.2 billion, up from $706.6 billion during January-September 1999, an increase of 12.7 percent. However, imports of goods and services also increased to $1066.4 billion, up from $895.3 billion during the same periods, an increase of 19.1 percent. As a consequence, the current-account deficit increased to $270.2 billion for the January-September 2000 period, up from $188.7 billion during January-September 1999, an increase of 43.2 percent.

The export of merchandise goods during January-September 2000 increased to $575.9 billion from $504.3 billion during the same 1999 period, an increase of 14.2 percent, but imports of merchandise goods rose to $907.4 billion, up from $753.6 billion in January-September 1999, an increase of 20.4 percent. Consequently, the merchandise trade deficit rose to $331.5 billion from $249.3 billion, a 33.0 percent increase. Regarding trade in services, exports in January-September 2000 increased to $220.3 billion up from $202.3 billion in the same period of 1999, an increase of 8.9 percent. Imports of services rose to $159.0 billion up from $141.7 billion, an increase of 12.2 percent. The surplus on trade in services increased to $61.3 billion from $60.6 billion, an increase of about 1.2 percent.

The January-September 2000 exports of advanced technology products rose to $166.1 billion up from $146.2 billion in January-September1999, an increase of 13.6 percent. Imports rose to $160.9 billion from $130.5 billion, an increase of 23.3 percent. The trade surplus decreased to $5.1 billion from $15.7 billion in January-September 1999, a decline of 67.5 percent.

The January-September 2000 trade data in goods and services showed trade deficits with Canada, Mexico, Western Europe, the so-called Euro area (EU-11), the European Union (EU-15), EFTA, Eastern Europe, China, Japan, Korea, Singapore, Taiwan and OPEC. Trade surpluses were recorded with Belgium, the Netherlands, Spain, Australia, Argentina, Brazil, Hong Kong, and Egypt. U.S. trade developments with major trading partners are highlighted in table 4.

Table 4
U.S. exports and imports of goods with major trading partners, Jan. 1999-Sep. 2000

(Billion dollars)

Country/areas	Exports			Imports			Trade balances	
	Sep. 2000	Jan.-Sep. 2000	Jan. Sep. 1999	Sep. 2000	Jan.-Sep. 2000	Jan.-Sep. 1999	Jan.-Sep. 2000	Jan.-Sep. 1999
Total	67.1	577.4	508.1	106.7	898.4	745.3	-321.0	-237.2
North America	24.4	216.8	184.5	31.7	271.4	226.0	-54.5	-41.5
Canada	14.6	134.4	122.8	19.3	170.3	145.7	-35.9	-23.0
Mexico	9.7	82.5	61.7	12.4	101.1	80.3	-18.6	-18.6
Western Europe	15.4	132.7	121.9	19.8	177.2	154.8	- 44.5	-32.8
Euro Area	10.0	84.6	78.0	13.8	120.2	105.2	-35.6	-27.2
European Union (EU-15)	14.2	120.3	112.1	18.1	161.7	142.1	-41.4	-30.0
France	1.6	14.5	13.9	2.3	21.4	18.9	-6.9	-4.9
Germany	2.4	21.6	19.7	4.8	43.7	40.1	-22.2	-20.4
Italy	1.4	8.2	7.2	2.3	18.8	16.5	-10.6	-9.3
Netherlands	1.8	15.8	14.2	0.8	7.2	5.9	8.6	8.3
United Kingdom	3.5	30.2	28.9	3.3	32.0	28.7	-1.8	0.2
Other EU	0.9	8.6	8.4	2.1	15.4	11.5	-6.8	-3.0
EFTA[1]	0.9	8.8	6.8	1.4	12.3	10.1	-3.5	-3.3
FSR/Eastern Europe	0.5	4.5	4.4	1.8	12.3	8.4	-7.8	-4.0
Russia	0.2	1.7	1.5	0.8	5.9	4.1	-4.2	-2.7
Pacific Rim Countries	17.6	150.3	127.2	37.7	307.3	261.6	-157.0	-134.4
Australia	1.0	9.4	8.4	0.6	4.8	3.9	4.7	4.4
China	1.4	11.7	9.9	10.1	72.8	59.4	- 61.1	- 49.4
Japan	5.5	47.9	42.1	11.6	108.0	95.0	- 60.1	- 52.8
NICs[2]	7.5	63.1	51.9	10.3	82.2	69.0	-19.1	-17.1
Latin America	5.1	43.4	40.6	6.2	54.5	42.3	-11.1	-1.7
Argentina	0.4	3.5	3.6	0.3	2.3	1.9	1.2	1.7
Brazil	1.4	11.1	9.6	1.2	10.6	8.3	0.5	1.3
OPEC	1.9	13.9	14.2	6.1	49.3	29.3	-35.4	-15.2
Other Countries	2.9	22.1	20.7	5.9	48.2	37.9	-26.0	-17.1
Egypt	0.3	2.5	2.2	0.1	0.7	0.5	1.9	1.8
South Africa	0.4	2.3	1.9	0.4	3.1	2.3	-0.9	-0.4
Other	2.2	17.4	16.6	5.4	44.4	35.1	- 27.0	-18.5

[1] EFTA includes Iceland, Liechtenstein, Norway, and Switzerland.
[2] The newly industrializing countries (NICs) include Hong Kong, the Republic of Korea, Singapore, and Taiwan. FSR = Former Soviet Republics.

Note.—Country/area figures may not add to the totals shown because of rounding. Exports of certain grains, oilseeds, and satellites are excluded from country/area exports but included in total export table. Also some countries are included in more than one area. Data are presented on a Census Bureau basis.

Source: U.S. Department of Commerce News (FT 900), Nov.21, 2000

World Trade

According to the most current trade statistics released recently by the World Trade Organization (WTO), world merchandise trade during 2000 is likely to record one of the highest growth rates of the past decade, reaching around 10 percent or twice the rate recorded in 1999.[2] The report also released the first comprehensive, detailed overview of goods and services trade in 1999, with data arrayed by region, country, and product category. Highlights from the report follow.

World economic growth accelerated during 1999, with recovery in Asia after the 1997-98 financial crisis and continued strong economic growth in the United States stimulating world trade growth in particular. Although world merchandise exports in 1999 remained the same as in 1998 on average—about 5 percent in volume terms—the rate of growth in world trade accelerated markedly in the second half of 1999 and more so into 2000. With economic activity outpacing most projections during the first half of 2000, world merchandise exports for 2000 are expected to exceed 10 percent on average, one of highest growth rates for world trade recorded over the past decade. The report suggests a somewhat slower pace for world trade growth in 2001 to around 7 percent.

In value terms, world trade growth in 1999 was composed of world merchandise exports, which rose by 3.5 percent to $5.47 trillion, whereas world commercial services exports rose more modestly, by 1.5 percent to $1.35 trillion. The weakness of the Euro against the U.S. dollar led to decreased exports of commercial services from Western Europe, which typically account for nearly half of total services exports.

Growth in world trade varied widely by geographic region. North America and Asia accounted for strong import and export growth, whereas Africa and Latin America recorded contractions in merchandise and services imports. Nonetheless, merchandise exports from Africa and Latin America registered significant growth. Merchandise exports from developing countries grew by 9 percent during 1999. This increased the developing countries' share of world exports to over 27 percent, with increased manufactures exports as well as higher fuel prices and trade playing a major role. Over the past decade, developing country exports of manufactures have increased their world share from 17 percent of world manufactures trade to 25 percent.

Trade among regional trading agreements also varied during 1999. Intra-NAFTA imports expanded by 11 percent, approximately the average rate worldwide, but NAFTA exports to other regions declined. The recession in Mercosur countries led to a contraction inintraregional trade of 25 percent. Intra-EU trade lagged behind imports from outside the EU. Only the ASEAN grouping recorded an expansion of intraregional trade, somewhat more than exports outside the region.

International capital flows, foreign direct investment in particular, were a major determinant of international trade. Large capital inflows into the United States sustained the large increase of U.S. imports, which reached the unprecedented level of 18.5 percent of world merchandise imports.

In 1999, growth of major product categories for merchandise trade ranged from an increase for fuels of nearly 20 percent, to a decrease for iron and steel products of more than 10 percent. World exports of office and telecom equipment rose by 10 percent to nearly $770 billion, with a sharp rise in semiconductor sales and mobile phones contributing to this dynamic growth. Exports of automotive products rose by 5 percent, with suppliers from Mexico, Korea, the Czech Republic, Hungary, Poland, and other less typical exporters supplanting the large traditional producers. Weak Western European trade, in particular intraregional EU trade, was largely responsible for the decline in world textile exports and the near stagnation in clothing trade. In marked contrast, however, intraregional Asian trade in clothing recovered by 8 percent, and clothing exports from Latin America to North America rose by 15 percent. One of the major features of world clothing trade has been clothing exports from Latin America to North America and from the East European transition economies to Western European markets have begun to surpass clothing exports of developing countries in Asia to these markets.

World exports of commercial services in 1999 expanded by 1.5 percent to $1.35 trillion, although growth in trade in services varied more strongly on a regional basis. Transport services were strong in the United States in particular, related to robust merchandise trade. Travel services were also strong in Asia, recovering from their steep decline following the 1997-98 financial crisis. Commercial services trade in Western Europe and Latin America were weaker than in North America and Asia. Services trade in Africa grew by 8.5 percent, the strongest increase of all regions during 1999, attributed largely to a recovery in Egyptian tourist earnings.

Trade by Region

North America

North America continued as the major engine of world trade expansion during 1999. North America, with roughly a one-fifth share of world imports, in-

[2] WTO, *International Trade Statistics 2000*, Nov. 30, 2000 (WTO: Geneva, 2000).

creased its merchandise imports to $128 billion and its commercial services imports to $16 billion, accounting for more than half of the worldwide expansion in goods and services trade in 1999. North American GDP growth exceeded 4 percent for the third year in a row, contributing to a rise in merchandise imports of over 10 percent annually while merchandise exports remained closer to 6 percent annually. North American imports of services rose faster than exports of services. As the major factor in the North American economy, the U.S. merchandise trade deficit continued to widen in this event, the surplus on trade in services continued to erode, and the U.S. current-account deficit amounted to 3.7 percent of GDP, which exceeded the previous peak set in 1987.

Latin America

Latin America's GDP, which expanded by 3.5 percent annually between 1990 and 1997, slowed in 1998 and stagnated in 1999. Merchandise imports and commercial services declined for the first time in the 1990s, contrasting sharply with the dynamic growth of a decade earlier. Within Latin America, a sharp difference regarding output and trade is salient between Mexico on the one hand, and all other Latin American countries on the other hand, owing principally to Mexico's deep integration into the North American trading system through NAFTA. In 1999, Mexico accounted for about 45 percent of the region's merchandise trade, and recorded double-digit growth in both merchandise exports and imports. All other Latin American countries reported a steep fall in merchandise imports as well as stagnation in the value of merchandise exports. Brazil accounted for another 15 percent of the regional merchandise trade, whereas Mexico, Brazil, and the three other top traders in the region account for more than 75 percent of merchandise exports and imports.

Western Europe

The slowdown in Western Europe's GDP growth in 1999 is reflected in slower regional trade growth. Exports and imports of merchandise and commercial services stagnated in nominal dollar terms, although merchandise exports and imports in real terms expanded by nearly 4 percent.

INTERNATIONAL ECONOMIC COMPARISONS

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U.S. Economic Performance Relative to Other Group of Seven (G-7) Members

U.S. real GDP–the output of goods and services produced in the United States measured in 1996 prices—grew at an annual rate of 2.4 percent in the third quarter of 2000 following a 5.6-percent growth rate in the second quarter, according to revised estimates by the U.S. Department of Commerce (Commerce News BEA 00-34). For the year 1999 real GDP grew by 4.2 percent.

The annualized rate of real GDP growth in the third quarter of 2000 was 2.8 percent in the United Kingdom, 4.8 percent in Canada, 2.7 percent in France, 2.3 percent in Germany, 2.1 percent in Italy, and 1.0 percent in Japan. The annualized rate of real GDP growth in the third quarter was 2.8 percent for EU members linked by the Euro currency, the Euro area (EU-11).

Industrial Production

The Federal Reserve Board (Federal Reserve Statistical Release -G.17 (419)) reported that U.S. industrial production fell by 0.2 percent in November 2000 following a decline of 0.1 percent in October. Manufacturing output dropped by 0.5 percent with declines spread about evenly across durable and nondurable goods industries. Output at utilities surged by 3.6 percent in November due to unseasonably cold weather. The output of consumer goods ticked up by 0.1 percent in November after having fallen by 0.9 percent in October. The production of durable consumer goods decreased for a second month and was pulled down by a drop in the assembly rate of autos and light trucks. The output of other consumer durables, which dipped by 0.3 percent in November, was held down by a decline in carpeting and furniture. Total industrial production in November 2000 was 4.7 percent higher than in November 1999. Overall industrial capacity utilization was 4.6 percent higher in November 2000 than in November 1999.

For the third quarter as a whole, total industrial production index increased at an annual rate of 3.7 percent, the slowest quarterly rate since the first quarter of 2000.

Other G-7 member countries reported the following growth rates of industrial production. For the year ended October 2000, Japan reported an increase of 6.6 percent, the United Kingdom reported an increase of 0.6 percent, Germany reported an increase of 4.1 percent, Italy reported an increase of 4.3 percent. For the year ended September 2000, France reported an increase of 3.4 percent and Canada reported an increase of 4.3 percent. The Euro area reported an increase of 5.6 percent for the year ended September 2000.

Prices

The seasonally adjusted U.S. Consumer Price Index (CPI) increased 0.2 percent in November 2000, the same as in October 2000, according to the U.S. Department of Labor (USDL-00-360). The food index, which rose by 0.1 percent in October 2000, was unchanged in November. The energy index increased by 0.1 percent in November 2000, following a 0.2-percent rise in October. For the 12-month period ended November 2000, the urban CPI ("CPI-U") increased by 3.4 percent.

During the 1-year period ended November 2000, prices increased by 2.4 percent in Germany, 2.7 percent in Italy, 3.2 percent in Canada, 3.2 percent in the United Kingdom, and by 2.2 percent in France. During the 1-year period ended October 2000, prices declined by 0.9 percent in Japan. Prices increased by 2.9 percent in the Euro area in the year ended November 2000.

Employment

The Bureau of Labor Statistics (USDL 01-02) reported that the unemployment rate was unchanged in December 2000 at 4.0 percent. The jobless rate has been in the 3.9 to 4.1 percent range since October 1999. Employment fell in manufacturing, but rose in construction and in the services sector.

[1] The views and conclusions expressed in this article are those of the author. They are not necessarily the views of the U.S. International Trade Commission as a whole or of any individual Commissioner.

In other G-7 countries, their latest unemployment rates were 6.9 percent in Canada, 9.3 percent in Germany, 5.5 percent in the United Kingdom, 9.4 percent in France, 10.5 percent in Italy, and 4.7 percent in Japan. The unemployment rate in the Euro area was 8.9 percent.

Forecasts

The OECD Economic Outlook report No. 68 issued in November 2000 expects global economic growth prospects to remain relatively bright, despite higher oil prices and a weakening in many equity markets.[2] After reaching 4.5 percent this year–the fastest pace in more than a decade–growth among the OECD economies is projected to slow to about 3.25 percent (at an annual rate) in 2001 and 3.0 percent in 2002. Against a background of some modest further tightening in monetary policy in the United States and the Euro area, core inflation is likely to remain low in most OECD countries. Areawide employment should continue to rise while unemployment may remain close to about 6 percent of the labor force. The OECD report also stated that, with a sharper and more widespread rebound in activity outside the OECD area than expected previously, world output may rise by some 4.75 percent this year before slowing to a growth rate of 4.0 percent in 2001 and 2002.

The OECD report also stated that financial market developments so far do not suggest turbulence, but could remain sources of risk in particular if the optimism attached to technology stocks continues to wane and risk premia in high-yield corporate bond markets continue to widen. Such developments could affect confidence and discourage private spending, triggering a sharper slowdown than projected, particularly in the United States. Attractive returns and buoyant economic conditions in the United States have ensured that the record high current-account deficit has been financed without difficulty. Ultimately, however, the current-account deficit requires adjustments that might take place smoothly. However, a change in foreign investor sentiment could slacken the pace of capital inflows and lead to turbulence in foreign-exchange markets, with possibly inflationary consequences that might require a monetary policy response that, in turn, could lead to a more abrupt slowdown in the U.S. economy.

Moreover, the OECD report points out that the unusually long expansion in the United States (although in few other OECD economies), coupled with the strong pick-up in U.S. productivity growth, has prompted much discussion of the sources of growth and the set of policies that might favor better growth performance in OECD economies. Although the debate is dominated by "new economy" arguments emphasizing the production and diffusion of information and communications technology, the evidence suggests that "old economy" mechanisms are still crucial to understanding the growth process. In particular, the accumulation of various kinds of capital–human as well as physical–plus the need for research and development, are considered two key elements for economic growth. Differences across countries in this respect may contribute significantly to explain the observed variations in growth patterns.

Raising levels of per capita income in the long term requires a broad set of policies, including: sound macroeconomic management; a tax system that encourages work effort and entrepreneurship; openness to international trade and competition; and government expenditure programs that emphasize investment and capital accumulation, including investment in infrastructure. Appropriate conditions in financial markets and product market regulations also have an important role in fostering innovation and productivity enhancement. However, the "new economy" does raise some novel policy challenges, notably in respect to consumer protection, taxation, and competition policy, according to the OECD report.

The OECD report projected U.S. real GDP to grow at a rate of 5.2 percent in 2000, 3.5 percent in 2001, and 3.3 percent in 2002. Inflation is projected to reach 2.1 percent in 2000, 2.2 percent in 2001, and 2.3 percent in 2002. U.S. unemployment rate is projected to reach 4.0 percent in 2000, 4.2 percent in 2001, and 4.5 percent in 2002. U.S. current-account deficit would reach 4.3 percent of GDP in 2000, 4.5 percent in 2001, and 4.3 percent in 2002.

In the Euro area (EU-11), the rise in oil prices and less accommodating monetary conditions have already contributed to a moderate deceleration in the pace of economic activity in the area in the course of 2000. Nonetheless, economic growth is set to expand at rates above potential over the coming 2 years. The OECD report projected Euro area GDP to increase at a rate of 2.9 percent in 2000, 2.6 percent in 2001, and 2.7 percent in 2002. Inflation is projected to increase by 1.2 percent in 2000, 1.9 percent in 2001, and 2.0 percent in 2002. Unemployment in the Euro area is projected to reach 9.0 percent in 2000, and then decline to 8.3 percent in 2001, and 7.7 percent in 2002. Current-account balances would show a surplus of 0.1 percent of GDP in 2001 and 0.4 percent of GDP in 2002.

In the broader European Union (EU-15), GDP is projected to increase at a rate of 3.4 percent in 2000, 3.0 percent in 2001, and 2.7 percent in 2002. Inflation is to increase by 1.4 percent in 2000, 2.0 percent in 2001, and 2.2 percent in 2002. Unemployment is projected to reach 8.2 percent in 2000, and decline thereafter to 7.6 percent in 2001, and 7.2 percent in 2002. The current account would show a deficit of 0.2

[2] OECD, *Economic Outlook No. 68*, Dec. 20, 2000, (OECD: Paris, 2000).

percent of GDP in 2000 and 2001, but achieve balance in 2002.

In Japan, the economy has started a moderate recovery. Output is projected to grow at a rate of 2.0 to 2.25 percent during the 2001-2002 projection period, with deflation gradually subsiding as economic growth picks up, according to the report. Japan's current account is estimated to show a 2.8-percent surplus as a percent of GDP in 2000, 2.7 percent in 2001, and 3.0 percent in 2002.

In addition, seven major U.S. forecasters expect real GDP growth in the United States during the fourth quarter of 2000 to reach an average of about 3.2 percent (at an annual rate), and to increase to 3.4 percent in the first quarter of 2001. The growth rate for the year 2000 would average about 5.2 percent. Table 5 shows macroeconomic projections for the U.S. economy from October 2000 to June 2001, and the simple average of these forecasts. Forecasts of all the economic indicators, except unemployment, are presented as percentage changes from the preceding quarter, on an annualized basis. The forecasts of the unemployment rate are averages for the quarter.

The average of the forecasts points to an unemployment rate of 4.1 percent in the fourth quarter, and is expected to remain at that rate over the first and second quarters of 2001. Inflation (as measured by the GDP deflator) is expected to reach about 2.2 percent in the fourth quarter and rise slightly in the first half of 2001.

Table 5
Projected changes in U.S. economic indicators, by quarters, Oct. 2000-June 2001, and annuals 2000-2001

(Percentage)

Period	Conference Board	E.I. Dupont	UCLA Business Forecasting Project	Merrill Lynch Capital Markets	Macro Economic Advisers	Eaton Corp.	Regional Financial Associates	Mean of forecasts
				GDP constant dollars				
2000:								
Oct.-Dec.	5.9	2.5	3.0	3.3	3.0	2.2	2.5	3.2
Annual 2000 .	5.4	5.2	5.2	5.2	5.2	5.1	5.2	5.2
2001:								
Jan.-March . . .	5.4	2.0	2.6	3.5	3.2	3.1	3.7	3.4
April-June	1.8	2.0	2.9	3.8	3.2	4.0	3.2	3.0
Annual 2001 .	3.9	2.6	3.1	3.7	3.3	3.4	3.3	3.3
				GDP Price Deflator				
2000:								
Oct.-Dec.. . . .	3.0	2.6	1.7	1.5	1.9	2.2	2.6	2.2
Annual 2000 .	2.2	2.2	2.1	2.1	2.1	2.1	2.2	2.1
2001:								
Jan.-March . . .	3.4	2.2	1.7	1.9	2.2	2.0	2.6	2.3
April-June	3.0	2.2	1.9	1.5	2.6	1.4	2.2	2.1
Annual 2001 . .	2.9	2.2	1.7	1.7	2.2	1.8	2.4	2.1
				Unemployment average rate				
2000:								
Oct.- Dec.. . . .	3.9	4.1	4.3	4.0	4.0	4.3	4.0	4.1
Annual 2000 .	4.0	4.1	4.1	4.0	4.0	4.2	4.0	4.1
2001								
Jan.-March . . .	3.8	4.2	4.4	4.1	3.9	4.2	4.1	4.1
April-June	3.9	4.3	4.5	4.1	3.9	4.2	4.1	4.1
Annual 2001 .	4.0	4.3	4.5	4.2	4.0	4.4	4.2	4.1

Note.—Except for the unemployment rate, percentage changes in the forecast represent annualized rates of change from preceding period. Quarterly data are seasonally adjusted. Forecast date, Oct. 2000.

Source: Compiled from data of the Conference Board. Used with permission.

STATISTICAL TABLES

Unemployment rates (civilian labor force basis)[1] in G-7 countries, by specified periods, 1998-Oct. 2000

		1999				2000						
Country	**1998**	**IQ**	**IIQ**	**IIIQ**	**IVQ**	**IQ**	**IIQ**	**June**	**July**	**Aug.**	**Sep.**	**Oct.**
United States	4.5	4.3	4.3	4.2	4.1	4.1	4.0	4.0	4.0	4.1	3.9	3.9
Japan	4.1	4.7	4.8	4.8	4.7	4.9	4.8	4.7	4.7	4.6	4.6	4.7
Canada	8.3	7.9	7.8	7.6	7.0	6.8	6.7	6.6	6.8	7.1	6.8	6.9
Germany	9.4	9.0	9.0	9.1	9.0	8.4	8.4	8.3	8.3	8.3	8.2	8.1
United Kingdom	6·3	6.3	6.1	5.9	5.9	5.8	5.5	5.4	5.4	5.4	5.3	5.4
France	11.7	11.3	11.2	11.0	10.6	10.2	9.8	9.6	9.7	9.7	9.7	9.4
Italy	12.3	12.3	12.1	12.1	12.1	11.2	10.8	10.6	10.6	10.6	10.6	10.6

[1] Seasonally adjusted; rates of foreign countries adjusted to be comparable with the U.S. rate.

Source: *Unemployment Rates in Nine Countries*, U.S. Department of Labor, Dec.8 , 2000.

Consumer prices of G-7 countries, by specified periods, 1998-Oct. 2000

(Percentage change from same period of previous year)

	1998				1999				2000						
Country	**IQ**	**IIQ**	**IIIQ**	**IVQ**	**IQ**	**IIQ**	**IIIQ**	**IVQ**	**IQ**	**IIQ**	**June**	**July**	**Aug.**	**Sept.**	**Oct.**
United States	1.5	1.6	1.6	1.5	1.7	2.1	2.3	2.6	3.2	3.2	3.7	3.5	3.4	3.5	3.4
Japan	2.0	0.3	-0.2	0.5	-0.1	-0.3	-0.0	-1.0	-0.7	-0.7	-0.7	-0.5	-0.8	-0.8	-0.9
Canada	1.0	1.0	0.9	1.1	2.6	2.3	2.2	2.6	2.7	2.4	2.9	3.0	2.5	2.7	2.8
Germany	1.2	1.4	0.7	0.4	0.7	0.8	1.0	1.2	1.8	1.6	1.9	1.9	1.8	2.5	2.4
United Kingdom	3.4	4.0	3.3	3.0	1.1	1.2	1.4	1.8	2.3	3.1	3.3	3.3	3.0	3.3	3.1
France	0.7	1.0	0.7	0.4	0.7	0.8	0.9	1.3	1.5	1.5	1.7	1.7	1.8	2.2	1.9
Italy	2.0	2.0	2.0	1.7	1.8	2.1	2.1	2.1	2.4	2.5	2.7	2.6	2.6	2.7	2.6

Source: U.S. Department of Labor, Dec.8, 2000.

U.S. trade balances by major commodity categories and by specified periods, 1998-Oct. 2000

(In billions of dollars)

				2000									
Commodity categories	**1998**	**Nov.**	**Dec.**	**Jan.**	**Feb.**	**Mar.**	**Apr.**	**May.**	**June**	**July**	**Aug.**	**Sept.**	**Oct.**
Agriculture	14.9	1.4	1.0	1.0	1.2	1.0	0.5	0.5	0.8	0.9	1.1	1.1	1.7
Petroleum and selected products (unadjusted) . . .	-43.4	-6.5	-6.0	-7.1	-9.0	-9.6	-8.6	-8.5	-10.0	-10.7	-10.6	-9.6	-9.5
Manufactured goods	-241.1	-31.1	-25.5	-27.9	-27.8	-31.6	-28.7	-32.9	-31.4	-36.4	-35.8	-36.2	-38.9
Unit value of U.S. imports of petroleum and selected products (unadjusted)	$10.81	$20.9	$20.90	$23.18	$23.18	$25.01	$24.42	$24.16	$26.65	$27.76	$26.59	$28.98	$28.62

[1] Exports, f.a.s. value, unadjusted. Imports, customs value, unadjusted.

Source: *Advance Report on U.S. Merchandise Trade*, U.S. Department of Commerce, FT900 (00-07), Dec.19, 2000.