



DAVID HALE GLOBAL ECONOMICS

Obama Must Back Free Trade

By David Hale

As appeared in The Age on April 3rd, 2009

The G20 summit in London is the most important to occur in that city since the global economic conference of June 1933. US president Franklin Roosevelt torpedoed the 1933 conference when he decided to pursue a unilateral devaluation of the dollar rather than collaborate with Europe on managing exchange rates.

It is essential that President Barack Obama use the forum to articulate clear goals and bolster global confidence in his leadership. He has launched the second-largest fiscal stimulus to promote recovery after China. His program will be worth nearly 6 per cent of GDP over three years while China's will be 14.5 per cent over two years. The G20 countries as a group have announced stimulus plans worth about 1.6 per cent of GDP.

The issue of trade is critically important. There has been a dangerous slide towards protectionism since the previous G20 meeting, in Washington. The World Bank reports that 17 countries have introduced 47 measures to restrict trade. The US was one of them by including a "Buy American" provision in the recent stimulus program.

Obama should promise not to enforce the provision in his legislation. He should pledge that his new trade representative will try to revive the Doha global trade round, and he should ask Congress to restore the comprehensive presidential trade negotiating authority that expired two years ago.

Finally, Obama should play down the threats outlined in his recent budget to impose punitive tax increases on US multinational companies. The multinational corporate sector plays a critical role promoting exports and America's role in the global economy. Congressional Democrats will resent him for supporting free trade, but they can take consolation from the fact that global trade will decline more during 2009 than in any year since the 1930s.

After a long period in which its lending contracted, the IMF will now need more capital to play an effective role in the financial crisis. The US should lobby China and other countries with large foreign exchange reserves to bolster the IMF's resources. The US should accept that if China plays a new role supporting the

IMF, the weight of its vote there should also increase. Obama should use the negotiations over this issue to enhance his relationship with the Chinese leadership as well. As a result of the United States' huge budget deficit, Obama should reject Treasury Secretary Timothy Geithner's recent comments on Chinese currency manipulation, and encourage China to continue buying US Treasury securities. The Chinese bought \$US245billion (\$A354billion) of US Government securities last year when the fiscal deficit was \$US450billion. Obama should hope they buy even more as the deficit expands to \$US2trillion.

The US has a greater responsibility than other countries to pursue intelligent responses to the global economic trauma because its financial mismanagement led to the crisis. The situation began 18 months ago when investors became alarmed about rising default rates on \$US1.3 trillion of subprime mortgages written during a housing boom spawned by the Federal Reserve's easy monetary policy, reckless lending by US Government-sponsored mortgage agencies, and irresponsible securitization of the debt by Wall Street investment banks.

The legacy of the US policy errors is awesome compared with the scope of the initial problem. There has been a \$US34.5 trillion contraction of global share market capitalization. The global economy has plunged into the most severe recession since the 1930s. The IMF is now estimating that total losses on US property lending could exceed \$US2.2trillion compared with an initial estimate of \$US965billion a year ago. The G20 was created by the Canadians during the late 1990s to promote North-South dialogue after the East Asian financial crisis. It has not played any role in global economic policy since its creation. George Bush convened the first G20 meeting for heads of government last year because of the scope of the financial crisis that followed the Lehman bankruptcy.

He could not lead the meeting because he was a lame duck. This time around, the meeting has been ideally timed to provide the new US President with an opportunity to play a global leadership role.

The US is still the world's dominant economy, and can set an example that other countries will follow. Obama must rise to this challenge by asserting America's traditional support for free trade, and a determination to resist the creeping global trend towards protectionism.

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