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The Estey

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Seeking “Better” Trade Deals: Is There Anything Beyond Good Slogans?

William A. Kerr

Associate Member, College of Law, University of Saskatchewan, Canada

In 2016, in separate electoral events in the UK and the United States, the angst arising from a perception of *falling behind* among many voters was successfully tapped into by the proponents of Brexit and Donald Trump’s presidential campaign. Slogans such as *UK Independence Day* and *Make America Great Again* captured the feeling of angst. Both the *Leave* campaign and Donald Trump suggested that existing trade arrangements were to blame and that new trading arrangements could redress the perceived decline. Neither, however, put forth any specific policies outlining how this was to be accomplished. This article examines the options for altering international trade arrangements in ways that could achieve a reversal of the fortunes of those *left behind*. The conclusion, after examining various trade policy options, is that there is no obvious path to achieving the desired result through changes in trading arrangements.

Keywords: Brexit, Donald Trump, new trade arrangements, renegotiation, return of jobs

Introduction

In a word, an industrial development, unparalleled, save in England a century ago, is now her [Germany's] portion. A gigantic commercial State is arising to menace our [Britain's] prosperity, and contend with us for the trade of the world ...

Take observations, Gentle Reader, in your own surroundings: ...

Your investigations will work out somewhat in this fashion. You will find the material of some of your own clothes was probably woven in Germany. Still more probable is it that some of your wife's garments are German importations; while it is beyond a doubt that the magnificent mantles and jackets wherein her maids array themselves on their Sundays out are German-made and German-sold for only so could they be done at the figure. Your governess's fiancé is a clerk in the City; but he also was made in Germany. The toys, and the dolls, and the fairy books your children maltreat in the nursery are made in Germany: nay, the material of your favourite (patriotic) newspaper had the same birthplace as like as not ...

For these articles, it must be remembered, are not like oranges and guano. They are not products which we must import or lack: – they all belong to the category of English manufactures, the most important of them, indeed, being articles in the preparation of which Great Britain is held pre-eminent.

E.E. Williams, *Made in Germany*, 1896, 10-12

As this quote from *Made in Germany*, E.E. Williams' best-selling pamphlet from the end of the nineteenth century (MacMillan, 2013) illustrates, it is often easy to stoke concerns and heighten angst regarding declining relative economic performance and rising numbers of immigrants. In 2016 it would have been easy to replace Germany with China and the UK with the United States in the quote and it would have had resonance with a considerable number of voters in the U.S. election in November. Similarly, replacing German immigrants with those from Central Europe would have resonated with British voters considering their choice pertaining to Brexit. Preying on the level of anxiety regarding the future is relatively easy and leads to opportunities for the effective use of sloganeering. "Make America Great Again" – who could argue with that?; "UK independence day"; "China is stealing our jobs"; "We send the EU £350 million a week, let's fund the NHS¹ instead"; NAFTA "one of the worst deals ever made of any kind signed by anybody". In both the United States and the UK there was a perception that over the past decade or two considerable segments of society had not shared in the benefits brought by trade agreements such as the European Union or the NAFTA or from China's accession to the WTO – those *left behind* by globalization and technological change. While economists argue over

the extent to which this is true, or at least what can be attributed to the trade arrangements entered into by governments, there is little doubt that such a perception was widespread. Of course, the reasons people voted for the vision offered by Donald Trump or Brexit are complex, but there was an expectation among supporters that a Trump presidency and a Britain outside the EU would lead to improvements to their lot. Future trade arrangements were central to those improvements.

Both in the case of the Donald Trump's campaign and those promoting *Leave* in the UK, however, there were no specifics on exactly how changing trade arrangements were to improve the lot of those *left behind* and of society in general. Sloganeering was sufficient to win over voters.² In the wake of their respective victories, however, both President Trump's administration and the British government are faced with actually altering trade arrangements. It may be that this is more urgent for the British government given its self-imposed deadline to initiate Brexit in March 2017. The administration of President Trump may have more latitude but at some point will probably have to try to do something to fulfill such a central part of its election sloganeering. Thus, a hard look at the options for improving the outcome of trade arrangements is warranted.

What is the dissatisfaction with current trade arrangements?

Neither candidate Donald Trump nor those promoting the *Leave* option in the Brexit referendum were against trade as a concept. Both appear to accept the proposition that trade, and expanding trade, would be beneficial to their country. Neither was promoting a move to autarky. Candidate Trump, for example, when promising to scupper the Trans Pacific Partnership (TPP) on his *first day in office*, said he would immediately engage in a series of bilateral negotiations with at least some of the other member countries of the TPP. Those wishing to leave the European Union were either keen to remain part of the EU's single market, presumably because they perceived trade benefits, or, for those wishing to eschew the single market, much was made of the promise of future potential bilateral trade agreements with other countries such as members of the Commonwealth, China and other third countries. Thus, the underlying motive was not some idea of *going it alone* or a policy of economic growth through import substitution (Gerber, 2007). If an *import substitution* strategy were the underlying motive for the desire to alter trade arrangements then it would be relatively straightforward to put in place a set of policies to achieve that goal. Such a policy could go some way to *bringing back the jobs* for those *left behind* to the extent that the underlying source of the loss of jobs was foreign competition and not other factors

such as technological change. Of course, *import substitution* as a strategy to yield sustained economic growth has been widely debunked, in part due to the experience of a number of Latin American countries and India in the twentieth century (Gerber, 2007). It is clear that neither Donald Trump nor the *Leave* proponents have bought into that particular line of thought regarding trade policy.

Given that the existence of *benefits of trade* seems to be accepted by both Donald Trump and those supporting Brexit, the answer seems to lie in the belief that somehow existing trade arrangements were poorly negotiated so as not to be to the advantage of either the United States or the UK. One can always argue that one could have negotiated harder and more skillfully than those who negotiated previous trade agreements. Given the professionalism of those who negotiate trade agreements for modern market economies (Kerr, 2007), it seems likely that *better deals*, while certainly possible, would likely only be improvements at the margin. Certainly, what would have been possible through improved negotiating skill would not be sufficient to reverse the decline of greatness that is implied by the promise to *Make America Great Again* or to improve the lot of those feeling *left behind* in Britain due to the arrangements negotiated as a member of the EU. Of course, *improved outcomes through better negotiating* of this sort is premised on negotiating within the bounds of conventional rules of trade as defined by the multilateral institutions devised in the wake of the Second World War and subsequent *Rounds* of negotiations (Kerr, 2000). Preferential trade agreements such as NAFTA and the EU also follow the same basic principles as those agreed multilaterally – they must be compliant with WTO commitments.³

The concessions for the UK that Prime Minister David Cameron was able to achieve through negotiations with other EU member states prior to the vote on Brexit were not sufficient in the minds of the majority of British voters, and particularly those perceiving themselves as being among those *left behind*, to reverse their fortunes – better to leave the EU and start again. David Cameron was, of course, negotiating under the established rules. The proponents of Brexit must have had something different in mind when they envisioned the nature of future trading arrangements after the UK exited the EU.

Donald Trump during the campaign and subsequent to his election victory has also accused previous administrations of lax enforcement of the existing rules. China and Mexico, in particular, are accused of not playing by the agreed rules, and being allowed to get away with it. The Trump administration is, therefore, expected to be more aggressive in initiating trade actions against what it perceives as *unfair* trade activities on the part of its trade partners. While punishing trade partners for

transgressions, real or imagined, can provide a measure of protection and, potentially, has a deterrent value, the scale of the effect is relatively limited and not sufficient to reverse the relative loss of status – greatness – to China, Mexico or whichever country is seen as engaging in *unfair* trade practices. Being tough on transgressors may sell well with some of those suffering the type of anxiety which the quote that began this article illustrates, but it cannot reverse the underlying changes that underpin the angst.

Hence, if there is a change in trading arrangements that will satisfy those who voted for the change promised by Donald Trump for the United States or those promoting the *Leave* option in the UK, it is unlikely to take place within the existing institutional arrangements governing trade. If such an option exists, it will require a radical change to the approach to international trade relations.

Is there a new approach to trade arrangements?

One of the major concerns of Donald Trump appears to be offshoring by U.S. companies. In the run-up to his inauguration he has attempted to dissuade, for example, car makers from proceeding with plans to move some of their production to Mexico. This has been done in part by suggesting such plans are not patriotic and in part through threats to impose punitive tariffs on U.S. imports of vehicles manufactured in such offshore facilities. This is consistent with the desire to retain manufacturing jobs in the United States and prevent more Americans being *left behind*. Such an approach could be scaled up to encourage repatriation of already offshored manufacturing by U.S. firms. Of course, the moral suasion of appeals to patriotism does not violate trade commitments. The selective use of tariffs, however, would require a retreat from the *Principle of Non-Discrimination* – a central element of the multilateral international trade architecture. In the case of preventing or repatriating offshoring, discriminating among countries and among individual firms would appear to be necessary. In those areas of the WTO where discrimination is allowed and where the underlying economic justification is poor, such as antidumping and countervail (Kerr, 2001; Kerr, 2006), discriminatory tactics can be used to considerable effect. Of course, being able to discriminate on the basis of individual countries is where relative economic power can be used to full effect in negotiations – and, of course, is what the *Non-Discrimination* principle of the multilateral system hopes to temper.

One avenue that is available to pursue discrimination is through preferential trade agreements. There is some evidence that the United States has been able to use its relative economic power effectively through preferential trade agreements. When the United States moved away from virtual multilateral exclusivity in its trade relations to

a willingness to negotiate preferential trade agreements during the Clinton and subsequent Bush administrations, it was able to successfully manipulate smaller countries into granting concessions (Kerr, 2005). As Sydney Weintraub commented on the U.S. move to negotiating preferential trade agreements in 2004,

Just about every country seeks to foster its own trade position by means of preferential arrangements and, in a sense, we are witnessing a revival of beggar-thy-neighbor practices, even if in a context different from the 1930s. The United States is picking and choosing its partners in the hemisphere for special treatment (xiii)

The United States also appears to have had considerable success in negotiating very limited concessions on agriculture in its preferential trade agreements (Kerr and Hobbs, 2006).

As offshoring to Mexico appears to be one of the major irritants regarding trade for Donald Trump, there may be an avenue to incorporate a degree of discrimination into a revision to NAFTA. Donald Trump has said repeatedly that he wants to renegotiate NAFTA with a threat to *tear it up* if Mexico (and presumably Canada) refuses. While the abrogation of NAFTA would represent a considerable loss for all three economies, there is little doubt that Mexico and Canada have more to lose. Faced with the potential disruption that would arise from the demise of NAFTA, they may choose to re-negotiate. Trade mechanisms to punish U.S. offshoring to Mexico could be built into the revamped NAFTA. While this would violate the underlying WTO principles, the changes in NAFTA would stand unless there was a formal challenge at the WTO. As Mexico and Canada would have agreed to the changes, they would be unlikely to complain to the WTO, and other countries might be sufficiently disinterested in such North American matters so as not to mount a challenge.⁴

While a policy of encouraging domestic firms, one way or another, not to further offshore their production or to repatriate production already offshored may produce some results, and photo opportunities, in the short run, it is not likely to be of sufficient magnitude to achieve the objective of *re-shoring* on a large scale the types of jobs hoped for by Donald Trump and those who voted for him. The strategy is only likely to work for a limited set of industries where brand is important and considerable barriers to entry exist – such as automobiles. Where brand is less important and competitors can enter or expand, those firms keeping more costly production in the United States will face competition from non-U.S. firms able to benefit from whatever cost advantages, for example, Mexico offers. If selective tariffs on the goods of U.S. firms operating in Mexico have been applied, those competitors will be able to export to the United States under NAFTA's tariff-free regime. This, in turn, will lead to U.S. firms facing such lower cost imports from Mexico to demand protection. If such

tariffs are not granted then those U.S. firms that have retained production in the United States or have *re-shored* their operations are likely to fail, with the resultant loss of the jobs that were the objective of the policy. If a wider range of U.S. tariffs is proposed to NAFTA partners, at some point they are likely to perceive little benefit from continuing NAFTA and refuse to grant such concessions, provoking the United States to abrogate its NAFTA treaties.⁵ U.S. exporters to Mexico and Canada will lose markets as a result.

Further, a strategy to encourage *on-shoring* may not yield results in terms of the type of jobs hoped for. U.S. firms will be faced with making investments in new domestic plants. They will choose to make those investments in locations where they perceive the highest return. If possible, they will want to locate where they can operate without unionized labour, and where job-saving technologies such as robotics will face less resistance. Hence, they are unlikely to locate in areas such as Michigan, Wisconsin, Pennsylvania or Illinois, where union culture and support is likely to be strong. The result will be that those from those areas *left behind* will remain *left behind*.

One of the reasons for the lack of international competitiveness of some U.S. industries that led to offshoring or their demise was the additional costs associated with wage and benefit packages associated with effective unions. This meant that employment costs for firms were inflated above competitive levels in those industries with effective unions. Of course, these are the types of jobs that many of those *left behind* see as what *Making America Great Again* would include. It can be argued that this type of labour arrangement arose out of different historic circumstances as a way of limiting labour unrest, and possibly revolution, in the first half of the twentieth century (Kerr, 2016). With the failure of the alternative presented by communism and particularly the demise of the Soviet Union, the threat of labour unrest and revolution faded, leading business owners to feel there was less need to share the benefits their success provided. While not the only factor, it is an important one in the decline of unionized workforces outside the public sector in the United States and a number of other industrialized countries. It is also these types labour arrangements, and their inflexibility, where offshoring was often manifest and foreign competition most keenly felt.

Firms, feeling they are faced with an unavoidable return to those types of labour arrangements, may cease export to the United States from their Mexican or other foreign plants but choose not to re-invest in the United States. Given the long-term nature of the investment required to *re-shore* production, this may be particularly the case if they do not believe the new trade policies will be retained beyond one (or

possibly two) U.S. administrations. Taken in total, it seems that a strategy of attempting to renegotiate U.S. preferential trade agreements, and in particular that with Mexico, will have only limited effect on bringing back the types of jobs envisioned by those who voted for the Trump campaign's promise to renegotiate preferential trade arrangements.

For those trading partners where the United States does not have a preferential trading agreement, a change in arrangements means either negotiating new preferential arrangements or somehow altering WTO commitments. The main stated target of such a change in the current arrangements is China. It may be possible that the United States and China could negotiate a bilateral agreement, but it seems unlikely that China would agree to anything that lessens the market access it achieved through membership in the WTO. Accession to the WTO was a major spur to the modernization of the Chinese economy, as it reduced considerably the uncertainty of its international trade relations, and particularly the United States, where access for imports was subject to annual reviews (Hobbs and Kerr, 2000). Lack of secure market access inhibited the investment needed to create an outward focus after years of attempts at self-reliant, autarkic development. China, in its mind, had to make considerable concessions to obtain its accession to the WTO and to subsequently live by its rules (Kerr and Hobbs, 2001).⁶ It is also likely politically unacceptable in China to appear to be bullied into concessions given its experience with what it considers *unequal treaties* imposed on it by European powers and Japan in the nineteenth and early twentieth centuries. *Unequal treaties* of the past remain a sensitive issue in China.⁷

If China won't negotiate the types of concessions required to provide encouragement for U.S. firms to re-shore operations from China and to reduce the competitiveness of Chinese firms in the United States – including no longer *manipulating* its currency – then any unilateral U.S. actions will likely lead to Chinese retaliation. A *beggar-thy-neighbour* trade war with China, or for that matter any other trading partners, will lead to a downward spiral in trade and yield similar results as those experienced in the 1930s (Pomfret, 1991). While taking a *tough line* with China may be politically popular in some quarters, it is not likely to deliver the results hoped for by those seeking altered trading arrangements.

The United States has the dual advantage of being the world's largest economy and having a relatively low proportion of its GDP dependent on trade. This gives it a considerable degree of economic power when dealing with trading partners. While a large economy, the UK does not have sufficient economic power to garner major concessions from trading partners. This is particularly the case with the other member

states of the EU acting as a bloc. With a majority of those who voted having chosen the Brexit option, the UK government is faced with coming up with a strategy that will yield a superior outcome to being a member of the EU. Thus far, there is no indication of what that strategy might be. The UK government had no strategy formulated – Prime Minister David Cameron and his government did not expect the Brexit result. The *Leave* campaigners, while excellent at *sloganeering* did not have a strategy. The post-Cameron administration of Prime Minister Theresa May is apparently struggling to come up with one before the self-imposed deadline on March 2017 when it will trigger Brexit negotiations with the EU.⁸

There is an indication of the *wish list* for post-EU trade relationships. First, there is a desire to remain part of the single market.⁹ Second, to no longer be bound by EU regulations – in particular those pertaining to the labour standards and the environment. Third, to be able to control immigration from EU member states. Fourth, to be able to pursue more favourable trade relations with countries which are not members of the EU.

Can any of this be accomplished? It is not possible to remain part of the single market without accepting EU regulations. British firms have long complained about the costs imposed by EU environmental and labour regulations. Their hope is that their costs will be reduced – their competitiveness increased – by leaving the EU.¹⁰ Of course, this is not acceptable for firms in other member states of the EU, who are still faced with more costly regulations. The EU could not accept such an arrangement when negotiating future relations with Britain.

If Britain wants concessions on immigration from the EU, the question is what can it offer in exchange? As yet it is not clear what that might be, but it would have to be substantial given the contentious nature of immigration among most remaining members of the EU. It is not clear that there is a mutually beneficial point that can be reached in negotiations (Gaisford and Kerr, 2003).

As to negotiating better trade deals with other countries than could be achieved as part of the EU, given that the EU, given its size, has considerable economic power in negotiations, it seems unlikely that other trading partners would give greater concessions than could be obtained by the EU. There has been discussion of new trade arrangements with members of the Commonwealth, as if those historic ties would lead to better trade deals for Britain – there may be trade deals but why would Commonwealth countries be less tenacious in their bargaining with Britain? Further, aggregated together, rich members of the Commonwealth do not approach the size of the EU market. The EU does not have trade deals with China or India (Khorana, Perdakis and Kerr, 2015). There may be more impediments to the EU reaching a trade

deal with China or India than for the UK on its own, but that must be traded off against the much smaller UK market when considering leverage in future negotiations (Khorana et al., 2010). Further, the UK, unlike the EU, has considerable historic baggage with India pertaining to trade relationships in the colonial era and with China regarding the *unequal treaties* it imposed in the nineteenth and early twentieth centuries. In the latter case there were still British gunboats on the Yangtze until the 1940s (Kerr, 2015), and Hong Kong was British until 1997 – not a great deal of time has passed in the Chinese view.

Those who feel *left behind* in Britain may obtain some relief from the pressures of immigration from Brexit, but it is difficult to see how additional trade-related benefits will flow from it. It may be that the realignment of trade relationships forced by Brexit will not make the UK worse off, but that is optimistic.

Conclusions

Despite claims that revamping trade relationships could contribute to *Making America Great Again* and improving the economic lot of those who supported Brexit, there do not appear to be the means to achieve the apparent aims – at least not through altering international trade arrangements. While the United States, given its ability to use its economic power, may be able to achieve some limited success in stemming offshoring and in re-shoring some jobs in the short run, it is unlikely to be able to keep competitive forces at bay without provoking retaliation from trading partners. In the case of the UK, even short-run successes are hard to imagine – except stemming the flow of immigration. Remember, achieving the goals of Donald Trump and his supporters and those who promoted the *Leave* option in the UK saw the way forward (or maybe back) from having trade relations structured in ways that are more favourable – meaning better for those previously *left behind* – to the United States and the UK. This was to be accomplished without setting off a cycle of *beggar-thy-neighbour* trade wars which can only yield a welfare-decreasing result for all parties. There is a danger that frustration with the inability to achieve the positive results expected from attempts to renegotiate trade arrangements will lead to attempts at stronger measures that can precipitate retaliatory spirals whether with the trading partners of the United States or with the EU as the UK attempts to extricate itself from the EU.

Changes in international competitiveness always create losers as well as winners. While the continuing expansion in global trade since the Second World War has brought large benefits for the United States and the UK (Kerr and Perdakis, 2014), there are those who have not benefitted and have, in many cases, been *left behind*. It

seems clear that previous governments in both the United States and the UK did too little to address the distributional effects of a globalizing world. It was, hence, easy to tap into (and foster) the angst that arises from perceptions of *falling behind*. Appealing slogans were easy to come up with given the degree of angst among many voters, but also allowed an escape from having to outline policies by which the source of the angst could be redressed. As the quote that begins this paper illustrates, while the angst may be real, solutions remain as elusive as they were for British readers of *Made in Germany* at the commencement of the twentieth century.

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Endnotes

¹ The National Health Service in the United Kingdom.

² To be fair, neither Hillary Clinton nor the *Remain* campaign provided any solutions for those feeling *left behind* other than to have faith that continuing with existing trade arrangements and negotiating new agreements in the same vein would eventually mean benefits would *trickle down* to them.

³ This requirement for preferential trade agreements has, however, never been formally tested through a dispute.

⁴ An example of this type of willingness to ignore WTO commitment is the export restraints imposed by Canada on shipments of softwood lumber to the United States. While export restraints are not supposed to be used under the WTO, Canada, under the threat of U.S. countervailing duties, chooses to impose them. Neither the United States nor Canada will complain to the WTO, and other trade partners are not interested.

⁵ NAFTA is comprised of three separate treaties, U.S.-Canada, U.S.-Mexico and Mexico-Canada.

⁶ Whether or not China has been living up to its WTO commitments is, however, an emotive issue. This was particularly the case in the U.S. presidential election of 2016.

⁷ See Ceko and Kerr (2000) for a discussion of China's experience with the *unequal treaties* and how they still influence China's perception of trade arrangements with the west and Japan.

⁸ One of the reasons it may be struggling is that it has no trade negotiators. This absence of experience has no quick fix, as the training of trade negotiators is still based on experiential learning – much like articling to be a lawyer or an accountant before much, but not all, of that training was moved into the formal education sector – rather than, say, academic education (Kerr, 2007).

⁹ Although this is not universal, with some prominent *Leave* proponents wishing to cut all existing trade relationships with the EU.

¹⁰ Some naively appear to think that there will be no regulations once the EU regulations no longer apply. Of course, EU regulations will have to be replaced by made-in-Britain regulations. Those who are expecting cost reductions have considerable faith that made-in-Britain regulations will be less onerous than those of the EU. Such faith may not be well founded if the example of British planning regulations is considered.