



Does the Auto Bailout Undermine Global Trade Rules?

Gary Clyde Hufbauer says the rush to rescue auto industries worldwide may create inefficiencies, hurt consumers, and weaken the global trading system. Hufbauer is coauthor of “Money for the Auto Industry: Consistent with WTO Rules?” (Policy Brief 09-4)

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Steve Weisman: This is Steve Weisman at the Peterson Institute for International Economics. Our guest on Peterson Perspectives today is Gary Hufbauer, senior fellow at the Institute and coauthor with Claire Brunel of the Institute of a new policy brief on whether or not the United State’s efforts to bailout the auto industry are in violation of international trade rules.

Welcome, Gary.

Gary Clyde Hufbauer: Thanks.

Steve Weisman: We’ve just come through a big furor over the Buy American provisions in the stimulus bill, which raised a lot of concerns about violation of international trade laws, NAFTA in particular. Now, we’re in the middle of an automobile bailout that some in Europe have said would be a violation of trade laws similarly. Is there any basis for thinking that the auto bailout would be such a violation?

Gary Clyde Hufbauer: The legal basis is not quite as strong as in the case of the Buy American legislation, or at least the initial version of the Buy American legislation, which had no provision that we would remain consistent with our international obligations. That provision took away at least some of the legal sting. However, in the case of the autos, the impact on trade and on the operations of the international auto industry are likely to far, far exceed what Buy American would have done even without all the saving provision. So, this is quite troublesome. But does it involve a straightforward violation of the WTO rules of our international obligations? That’s really not so clear because the violation depends on the impact of these auto subsidies. We can talk about how they trace through the operation of auto companies. It depends on the impact on trade. It’s not just a violation on the face of a bailout or subsidy or whatever. It depends on the ultimate impact and of course, it’s a little bit hard to say what the impact would be.

Steve Weisman: It could impact the competitive ability of the American auto companies vis-à-vis transplants of foreign-owned automakers in the United States. But that’s not a factor here?

Gary Clyde Hufbauer: You're absolute right. I mean, it will make the companies that received the federal funding—Chrysler and GM—stronger than they otherwise would be compared to let's say Toyota or Honda operating here in the United States. But there are no international rules that say you can't make one company in the industry stronger than another company. The international rules have to deal with trade across borders, so that's where the issue comes into play.

Steve Weisman: Are there some ways they could structure the bailout to guarantee that they would not violate international trade norms?

Gary Clyde Hufbauer: They could certainly take constructive steps. But here's the reality on the ground. The reality on the ground is that, owing to these huge bailouts, major parts of the auto industry will be essentially owned or controlled by the US government. And then the next kind of political pressure would be to indicate as we're doing massive restructuring, closing plants, trimming lines, etc., that should be done in a way that has the least impact on employment in the United States or in a particular state were the congressman or the senators are quite powerful. This can all be by word of mouth. It has the least impact, let's say, in Indiana or Ohio or whatever. Where's the impact going to be? Well, it could be in another state in the United States, it could be out in California. It might also be in another country; Canada and Mexico being quite likely places where you can restructure plants there out of existence, or other countries around the world, and that's the real danger out of this subsidy or bailout situation.

Steve Weisman: Other countries are also undertaking bailouts, or at least they've announced plans to.

Gary Clyde Hufbauer: You're right. It's quite widespread. The auto industry is one of the original multinational industries where there are maybe ten big companies around the world with operations really all over the world and a lot of integration of components and assembly. It's said, for example, that parts between the United States and Canada cross the border five or six times before you get the final auto. That's just this industry. Now, the industry is hurting all over the world because as you know, sales have plummeted like a rock. They are down really about 30 percent to 50 percent wherever you look. So a lot of governments are stepping in to help out their industry, the Canadians and the French definitely, the Germans probably, the Italians I think for sure.

Steve Weisman: What about the Japanese?

Gary Clyde Hufbauer: Not that I've read. There have been cuts.

Steve Weisman: If everyone is doing it, what's wrong with it?

Gary Clyde Hufbauer: What's wrong with it is you wonder how companies will be operated when they have such a big government component in their ownership. And the hard edge of that was illustrated by France, where President Sarkozy said flat-out to Renault

and Peugeot, “We’re going to give you money but you’ve got to cut those jobs out of your Czech factories, not here in France.” That was upfront. We can all see it, it’s all in the papers, but the same thing can happen elsewhere. So, there are two bad consequences. You’re not going to have rational economic decisions; you’re going to have decisions dictated by where the jobs are politically most sensitive and most supported by the government. So, you’re going to introduce a lot of inefficiency.

Steve Weisman: Is that a violation of international law or just economic common sense?

Gary Clyde Hufbauer: That’s economic common sense. Law doesn’t require you to be economically efficient. The rules are trying to encourage that, but there’s not a final efficiency test. But the second question is, when a lot of countries are doing this, who’s going to bring a complaint? Because it’s true as a legal matter, and here I’m talking lawyer talk, the fact that France is doing all these nasty things to its auto industry does not legally prevent France from bringing a complaint against the United States. But in the court of public opinion, it kind of looks silly for France to complain about the United States when France is doing exactly the same thing or even worse.

Steve Weisman: Well, in trade, hypocrisy is not unknown.

Gary Clyde Hufbauer: No, that’s certainly true, but this is such a big and blatant case. People who are experts have opined that it’ll be hard to find any country to actually bring a case against. So that means that the bad consequences may just go into the deep freeze during this period.

Steve Weisman: And I think you’ve said in this paper that what effectively is happening is that the entirely worldwide auto industry is being removed or removing itself from the rules of the international trading system.

Gary Clyde Hufbauer: Well, that seems to be the way we’re going, which is quite unfortunate, because our precedent is agriculture. Once agriculture got deep into the subsidy system in this country and in Europe quite broadly, it removed itself from the trading system, and here we are literally 50 years later since the decisions were made, and we’re working very hard to get agriculture back into the normal trading rules and wouldn’t like to see a three-decade holiday for the auto industry.

Steve Weisman: It would be bad for efficiency, for people buying cars, and for the trading system in the abstract, right?

Gary Clyde Hufbauer: Absolutely. And some countries have tried to have their own national auto industry. I’ll single out two—Brazil and Malaysia did it, and Indonesia even gave a little try at this without having components from other countries and not having the integrated system that I talked about. And the result is that the cars made in those countries are not of particularly good quality. In fact, they’re lousy, and the prices are very high. And the modern exemplar of that is Russia.

Steve Weisman: In Russia the issue has brought people into the streets.

Gary Clyde Hufbauer: Absolutely! The Russian people know that their cars are really poor quality and very inefficient fuel-wise and they break down. So, who wants to go in that direction? Nobody. But you might say, “Oh, well, our cars are pretty good. In the United States and Europe, we don’t have that problem.” But look, we’ve got to revolutionize this whole industry to get it down to a much lower CO2 emissions and other greenhouse gas emissions. That’s the challenge ahead. And that means a whole lot of new technology and so forth. Any country that isolates itself from the world economy is going to be behind the curve on the next generation auto.

Steve Weisman: Do you see a silver lining in these bailouts that could at least send America and other industries in the direction of more fuel-efficient and environmentally-friendly cars?

Gary Clyde Hufbauer: I’m very happy that President Obama has emphasized that in his remarks. I’m also happy that he seems to be choosing as his oversight board for the US auto industry two financial executives—Larry Summers and Secretary Geithner—who really are not going to try to recreate themselves as Henry Ford or Alfred Sloan. I mean, they’re not auto experts and so that means they probably are not in it for the long haul. That’s very good because that means that we’ll probably, hopefully, get in and out quickly.

So, those are two silver linings that I’m hopeful about. The proof will be in the pudding whether we really do push energy efficiency. Right now the most fuel efficient, least carbon dioxide emitting cars are made by Toyota and Honda, not by GM and Chrysler. We have to somehow get GM and Chrysler up to those levels. That will be a huge task, but I think we’re pointed in the right direction.

Steve Weisman: Gary Hufbauer, thank you very much for sharing your thoughts on this. And you’ll find Gary’s policy paper coauthored with Claire Brunel, research assistant here at the Institute, on the PIIE website.

Gary Clyde Hufbauer: Thank you.

