

SCOMM

136:8

Commercial Diplomacy
Juneau, February 27, 2006

I'm delighted to be here. More copies of this book have been sold in Alaska than in any other state, so I know that interest in the subject is high.

First of all I want to go back to basics and talk about what the subject is.

#2

The two goals of American foreign policy are security and prosperity. They are fundamental purposes of our government, identified in the first sentence of the Constitution. Diplomacy is one of the tools of foreign policy the government uses to achieve those goals.

Most people, when they think about diplomacy, think about what Condoleezza Rice does, flying around the around world visiting mostly bad people and giving them a few good reasons to improve their behavior.

The purpose of that kind of diplomacy is security.

Commercial diplomacy gets less attention. Commercial diplomacy involves negotiations on trade, investment, finance, patent and trademark protection, export promotion, and the like. It's diplomacy that aims at prosperity.

One question I want to deal with right away is whether the government should be doing this stuff at all. Some of you may remember that there was a move in Congress not so long ago, around 1995-1996, to close down the U.S. Department of Commerce and stop funding the Export-Import Bank and the Overseas Private Investment Corporation. Support for U.S. trade was attacked as corporate welfare. Along the same lines, there

were calls for the United States to pull out of the World Trade Organization, which was – and often still is – denounced as a tool of large and evil corporations.

I want to make the case for an active commercial diplomacy.

#3

First of all, trade is good for prosperity, and also for peace.

Commercial diplomacy has produced a lot of prosperity around the world. The trading system put in place after World War II has worked as planned. Since 1950, world trade is up over 20 times, the world's output has risen 8 times, and world population has grown only about 2.5 times. Trade has made people richer.

Of course wealth is not evenly distributed. Neither is peace. The countries that are most involved with the international trading system are the countries that are best off and growing most rapidly. They are also generally the most peaceful places.

#4

The countries that are least engaged with the international trading system include the most dangerous places in the world, and some of the poorest. The World Trade Organization has 149 members. But look at who isn't there: Afghanistan, Belarus, Bosnia, Iran, Iraq, Lebanon, Laos, Liberia, North Korea, Somalia, Syria, and Yemen. It's the roll call from Hell.

In other words, as the saying goes, when goods and services cross borders, armies don't. Tom Friedman, who writes about foreign affairs for the New York Times, expressed the same idea a few years ago when he pointed out that no two countries with a McDonald's restaurant have ever gone to war.

So a more peaceful and prosperous world is one reason why the government should work at commercial diplomacy. Here's another: U.S. success in business is a cause, maybe the most important cause, of U.S. global leadership.

#5

The United States is the world's largest exporter, the world's largest importer, and the world's principal source of and principal destination of capital for investment. We are the engine of the world's economy.

#6

The numbers tell us that the United States is one of the few really good places in the world to do business: it's most lucrative place in which to sell, the most reliable in which to buy, and the safest in which to invest or raise capital. More than military power, it's this strength in business that makes the United States a leader, because it's our business strength that other people want to follow.

People in other countries look at U.S. prosperity and ask: How did that happen? How did the Americans get where they are, and how can we get there too? They know that American business success owes a lot to the business climate and the business infrastructure: our educated, mobile workforce, our willingness to innovate and to accept technological change, our reliance on contracts and laws.

The reliance on contracts and laws is really important. We all tell lawyer jokes, but in the end we're a much stronger country because we settle disputes in court, and when a judge issues an order, we obey. There are a lot of countries where that doesn't happen – Russia, China, most of the developing world. The legal system here is a very

valuable part of the business infrastructure. Other countries want to copy it, not the laws necessarily, but the respect for laws. It part of American leadership by example.

#6

Our business strength also gives us leadership through economic power. The United States was 28% of the world economy in 2005, more than the share of the next four countries combined.

#8

That's an amazing statistic, but it's nothing new. The US has dominated the world economy for over a hundred years.

#9

This economic power translates into military strength. US spending on defense is almost equal to the defense spending of the rest of the world. Yet spending on defense represents a small share, about 4.2%, of the US economy, a lower share than in years past.

So a strong economy is essential to security as well as to prosperity. That's another reason why the government needs to be involved in commercial diplomacy.

#10

Commercial diplomacy comes in many flavors, like Baskin-Robbins. I'm going to talk first about commercial negotiations, which we can divide into macro and micro.

Macro is the big stuff, negotiations on tariffs, patents, standards, subsidies, and so forth – rules that have general application. These negotiations usually involve striking a balance among many competing interests.

Micro is the small stuff, or really the specific stuff, dealing with specific transactions and specific companies – will China buy planes from Boeing, or from Airbus? Will Kazakhstan bring in U.S. or Russian companies to develop its oil and gas? Macro diplomacy requires give and take, a series of compromises. Micro often has just winners and losers.

Macro diplomacy belongs almost entirely to the federal government. Only the federal government can negotiate trade and investment rules on behalf of the United States. Most macro diplomacy is handled by the U.S. Trade Representative, with technical support from other agencies, especially the departments of commerce and agriculture, and oversight by the Congress, especially the Ways and Means Committee in the House and the Finance Committee in the Senate.

#11

I don't want to suggest that states have no role in macro diplomacy. They do. But the state's role is mostly to deal with the federal government, not with the foreigners. So if your constituents come to you and say – I'm making up this example – "we're having trouble exporting seafood products to Korea because of Korean health regulations," you want to make sure the federal government takes this up with the Koreans and makes it an important issue.

How do you do this? You have to show the executive branch that the interests of your constituents line up with a broad public purpose. That's critical. For many good reasons, the federal government wants to be consistent around the world in the way it approaches trade issues, so it wants always to have a basic principle at the heart of its argument in any particular case. In this case, the basic principle, which is part of

international agreements that Korea and the United States have both signed, is that health regulations affecting trade should be based on science. They should protect public health, they can't be designed just to keep out foreign products. Maybe in this example about Korean health regulations your constituents can show that the regulations are not based on sound science.

So you want to advise your constituents to put their complaint together in this way, and maybe you can help them do it. Then you and they can go directly to federal officials, in this case in the office of the U.S. Trade Representative. Federal officials will almost always respond quickly and favorably if they are given what they need to go to work.

Of course you can also look for support from the Alaska congressional delegation, which is one of the strongest and most able in Washington.

#12

Or another example. Let's say that the government of Japan gives big subsidies to its commercial fishing fleet, subsidies that put Alaskan fishermen at a competitive disadvantage. If the Japanese were using subsidies to sell fish below cost in the U.S. market, the U.S. could put extra tariffs on the subsidized fish to offset the subsidies. But let's say that Japanese subsidies hurt Alaskan fishermen not so much in the United States, as in Japan or other Asian markets. The basic principles and the appropriate remedies aren't as clear in this case.

But U.S. law provides a way for private parties, like the Alaska fishing industry, to petition the U.S. government – the U.S. Trade Representative, to be exact – to act against unfair foreign trade practices, even if there is no international agreement that

clearly covers the situation. In fact the Alaska state government could file the petition on behalf of the fishing industry, so long as a substantial percent of the industry – I believe it's 80% – supports the action. Engagement by the state government would increase the political weight behind the petition and increase the pressure on USTR to take strong action.

#13

The state also gets involved with macro diplomacy when state, not federal, laws and regulations are at issue. I'll make up another example. Let's say the state legislature is considering a bill to increase user fees at the Anchorage airport, with revenue earmarked for airport improvements. No doubt you will hear from Federal Express, both on the record in public testimony and off the record in private communications. But you might not hear much, especially on the record, from foreign shippers and carriers who will be affected, unless you ask them to comment. You might want to do that – invite foreign companies to submit statements for the record, or to present oral testimony, regarding proposed legislation that is likely to affect them in serious ways. Whatever happens in the end, people usually feel better about a decision if they've been part of the process and have had a chance to be heard. You may also be able to use the process to build relationships and a reputation for fairness that will be helpful in the future.

#14

That's macro diplomacy. Micro diplomacy happens when the government steps in between U.S. companies and foreign governments or government-controlled entities. This is where U.S. embassies get involved.

When U.S. private companies are dealing with foreign private companies, of course, the U.S. government and its embassies stand clear. But you'd be surprised – or maybe not – by how many private deals get tangled up in some government regulation or requirement. That can bring the embassy into play.

An American embassy, and especially an American ambassador, can be a very powerful ally for American business. For almost every country in the world, the United States is the most important trading partner, the most important market. For many countries, the United States directly or indirectly provides security. Because of the importance of the United States, the American ambassador generally has excellent access to high officials in the host country.

A good ambassador uses this access wisely. He builds trust and confidence. He is someone that officials in the host country listen to and take seriously.

I should say there are some bad ambassadors out there also. Some are lazy or self-indulgent. They don't get out to meet the people they ought to meet, they don't speak the local language or understand the local politics. And some follow their personal views rather than their instructions from Washington, which makes them unreliable as representatives of the president. But most ambassadors and embassy staffs are competent, highly dedicated people.

Just by indicating their interest, embassies elevate a commercial issue and give it some political importance. For example, when a U.S. power company bid on a project in the United Arab Emirates a couple of years ago, the company asked the embassy to get involved. The company had French competition and wanted to make it harder for the French to win the deal with bribery or kickbacks. The U.S. company thought that the

Emirates would be much more careful about sticking to their own rules, which prohibit that sort of stuff, if they knew the United States government was watching. The embassy did get involved – and stayed involved throughout a year of negotiations – and the company won the contract.

#15

Like everyone else, ambassadors and their staffs work better when they are well prepared. The best advice to a company working overseas is to keep the embassy informed, so that they are ready to go if there's a crisis. And I would always tell anyone who is going to brief an ambassador to tell the whole story, not just one side of it. An ambassador going to see a foreign official has to be credible, and he won't be credible if he gets sandbagged because he didn't know the other side of the story.

Where U.S. relations with a country are poor, embassy involvement in a commercial issue may backfire. The host government may see a chance to play up to nationalist sentiment by saying no to Uncle Sam, in a loud voice. That's why some companies don't want to be associated with the U.S. government. When Argentina defaulted on its debts, devalued its currency and imposed price controls at the end of 2001, most U.S. companies invested in the country came to the U.S. embassy for help. But some stayed away. One of the big grain traders told me: "We decided we had better relations with Argentina than the U.S. government did, so we handled our problems ourselves. We think we were better off that way." That's a judgment call, and the grain trader may have been right. The embassy and the U.S. government have leaned on the Argentine government for the past four years, so far with little to show for the effort.

Can a state government get involved in this kind of micro diplomacy, and if it can, should it?

The key to micro diplomacy is leverage. Generally its the federal government that has the leverage to negotiate with foreign governments, and only the federal government has the view across the whole range of bilateral relations to reach a judgment on how to handle any particular case.

Of course state officials can steer businesses with problems to the right people in the federal government – to a U.S. embassy, to the Departments of State, or Commerce, or Agriculture, as the case requires. But frankly, most businesses can figure out for themselves where they need to go. The state government only adds value if it can provide an introduction – if there is a state official who has developed personal relationships with people in U.S. embassies and in the Washington agencies and is known and trusted by them. Alaska is such an export-oriented state that you may already have someone on the payroll who fits that description. If not, maybe you should.

#16

Export promotion

State governments have a larger role in two areas, promotion of exports and attracting inward investment.

Alaska is especially well positioned to make export promotion a state function, because the range of goods and services available for export is not too large, and because some them – tourism obviously, but I would guess also seafood and maybe some wood products – can be Alaska branded. I don't have to tell you about export promotion. The

state knows all about trade missions and trade fairs and the other standard techniques. I would offer only one piece of advice.

I think it's a good idea to charge companies to take part in state-sponsored promotional events, maybe on a one-for-one matching basis. It's a good idea because the companies are the biggest beneficiaries, so fairness indicates they should pay a higher share of the cost. But more important, if the fees are high enough, companies will make sure they get their money's worth. They will set a standard that the government has to meet, and they will know how to measure success. Programs that don't produce a return won't find support, and the ones that do work will be heavily subscribed. The government can't get that kind of feedback in any other way.

#17

Attracting investment

Promoting inward foreign investment is controversial. The federal government doesn't do it at all. One reason is that the government doesn't want to do anything that would favor a foreign investor over a domestic investor. Another is that the federal government doesn't want to favor one state or region over another. So federal policy tries to be strictly neutral.

I don't know what Alaska does about foreign investment, but I'll bet you follow the same policy of neutrality between foreign and domestic investors that the federal government does. Probably when the state goes out promoting investment in Alaska, you're at least as eager to go after investors in the lower 48 as in the rest of the world.

The best thing the state can do to attract foreign investment is to create a business climate that is friendly to investment, domestic or foreign. I mentioned near the

beginning of this talk that the United States attracts more foreign investment – I mean direct investment, ownership of businesses, not just foreigners buying stocks and bonds – than any other country. That's because of the business climate here, the blend of good return and low risk.

Investment promotion is education, making the opportunities here known to investors who otherwise wouldn't think about Alaska, whether those investors are in Taipei or New York.

One way to get the attention of foreign investors is to put Alaska on the itinerary of touring diplomats, including American ambassadors to countries of interest, and ambassadors from those countries to the United States. You can show the diplomats the grandeur and beauty of the state and also teach them something – I'll bet they know very little about the range or scale of opportunities or the legal framework for resource development. Diplomats will repeat your message to people that count, they'll get press attention overseas, they are good multipliers of your message that way. There are a few organizations that have put tours by diplomats together, using a blend of public and private funds, and you might be able to tap into their experience.

Representative Coghill asked me to talk about what the states can do in diplomacy, on their own or by making the country's national resources work for them. I hope I've come up with a few ideas, but I'm sure I haven't exhausted the topic. I'd be happy to take questions.

Commercial Diplomacy

Juneau

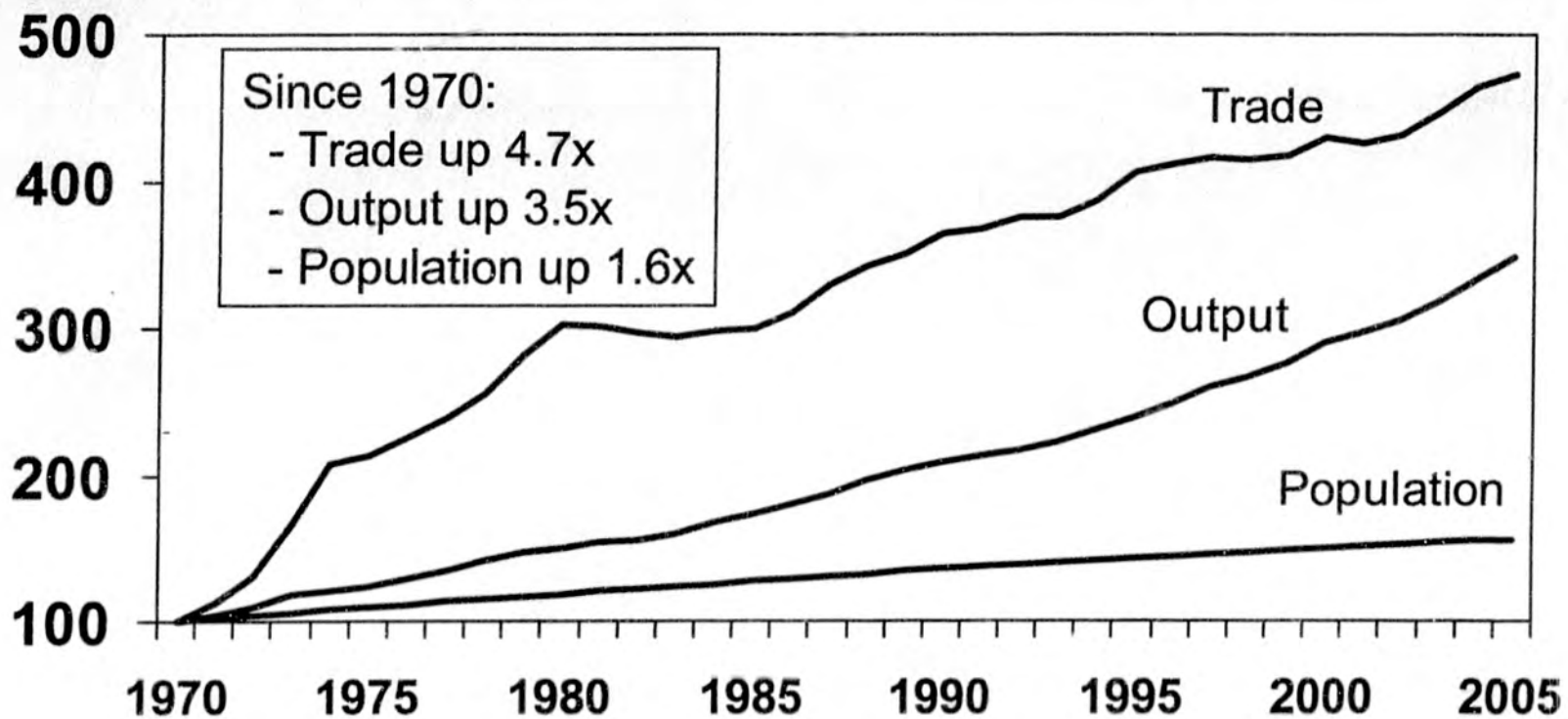
February, 2006

U.S. Constitution - Preamble

We the People of the United States, in Order to form a more perfect Union, establish Justice, insure domestic Tranquility, provide for the common defence, promote the general Welfare, and secure the Blessings of Liberty to ourselves and our Posterity, do ordain and establish this Constitution for the United States of America.

Global trade, global growth (1970 = 100)

Index 1970 = 100



Source: IMF WEO database; US Bureau of the Census

Among the missing

Afghanistan*

Algeria*

Azerbaijan*

Belarus*

Bosnia*

Iran

Iraq*

Lebanon*

Laos*

Liberia

Libya*

North Korea

Russia*

Somalia

Syria

Tajikistan*

Ukraine*

Uzbekistan*

Yemen*

* observer

Top traders, 2004 (\$ billions)

	EXPORTS	IMPORTS
USA	1,137	1,786
Germany	1,046	910
China	655	633
Japan	661	589
France	558	562
<i>World</i>	<i>11,278</i>	<i>11,590</i>

Source: WTO. Goods and commercial services.

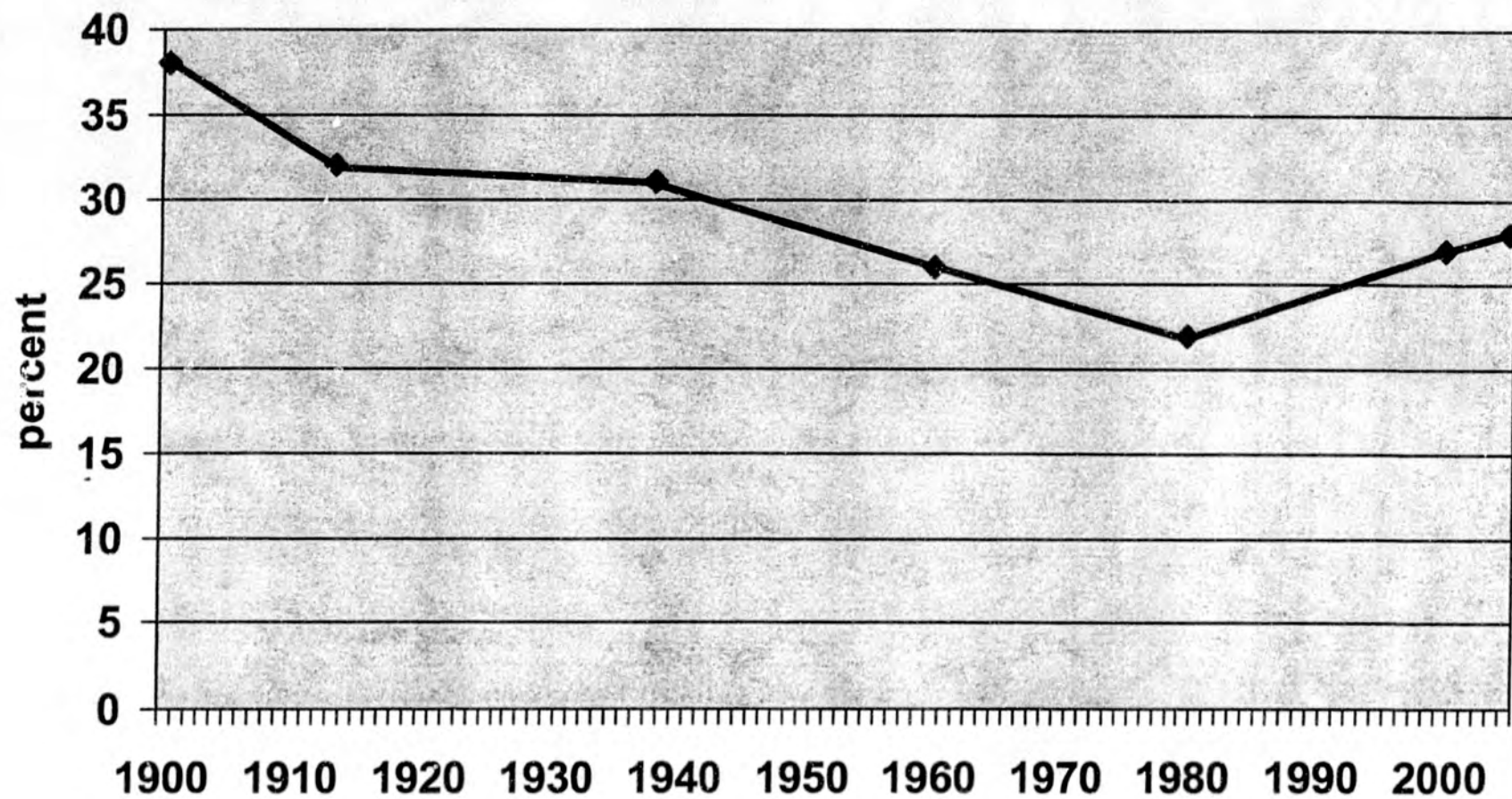
U.S. Business Climate

- Lucrative place to sell, reliable place to buy
- Safe place to invest or raise capital
- Mobile, educated workforce
- Risk-taking entrepreneurs
- Transparent, enforceable rules

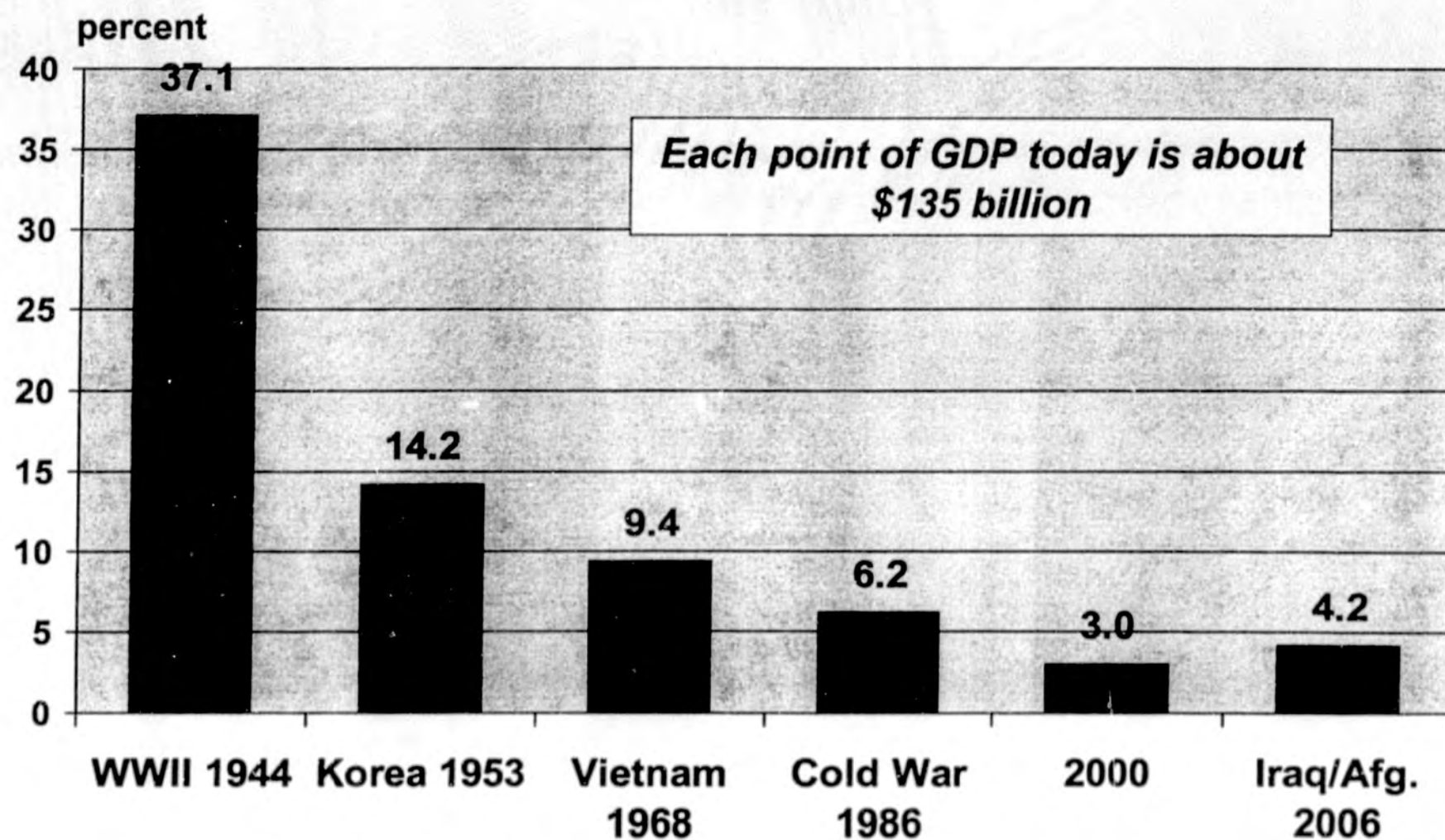
World output, 2005

	\$ trillions	percent
<i>World</i>	43.9	100%
USA	12.5	28%
Japan	4.7	11%
Germany	2.8	6%
UK	2.2	5%
France	2.1	5%
China	1.9	4%

U.S. share of world output



Defense spending as % of GDP



Commercial diplomacy

Macro

- Rules
 - Tariffs and quotas
 - Patents
 - Standards
 - Subsidies
- Requires compromise

Micro

- Transactions
 - Specific companies
 - Specific deals
 - Not a precedent
- Winners and losers

Engaging the federal government

- Private interest → public purpose
- Consistency
- Principle

Engaging the federal government

- Private interest → public purpose
- Consistency
- Principle
- A state can petition USTR on behalf of an industry (Section 301)

State laws

- Some state laws affect foreign trade, investment
- Bring affected foreign parties into the process

Embassies at work

- USG may step in when U.S. companies deal with foreign governments
- US power = ambassador's access
- Political element when embassy acts

Embassies at work

- USG may step in when U.S. companies deal with foreign governments
- US power = ambassador's access
- Political element when embassy acts
- Preparation, candor, full disclosure
- Some risk of backlash
- Role for State government?

Export promotion

- Branding
- Why companies should pay
 - Fairness
 - Efficiency
 - High standards
 - Feedback

Investment promotion

- Federal government: strict neutrality
 - Between foreign and domestic investors
 - Among regions of the USA
- State government
 - Neutral in policy
 - Business climate
 - Use diplomats to get the word out