Vernon’s Product-Cycle Paradigm
and the Political Economy of Trade:
A Comment on Alan Deardorff’s
“Market Access for Developing Countries”
Introduction

Alan Deardorff’s paper on “Market Access for Developing Countries” addresses one of the classic questions in the political economy of trade policy, and one for which Raymond Vernon’s product-cycle paradigm has important implications. Will established producers act to limit the opportunities of newcomers? Deardorff contends that although “developing countries grow by expanding in industries that developed countries must then leave behind,” the entrenched interests in the developed countries’ “declining industries will inevitably, and to some extent successfully, seek protection” (2000: 1). To the extent that the governments of developed countries grant these demands, the aspirations of the developing countries will be thwarted.

One of the great virtues of Vernon’s scholarship was that it addressed issues of concern to more than one discipline. In Deardorff’s paper we see how the conflict between mature industries and newcomers fits within the received models of neoclassical trade theory. In this comment, I would like to bring some observations from the field of political science into consideration. I do so by reference to the law and diplomacy of the world trading system, especially the rules of the General Agreement on Tariffs and Trade (GATT) and the World Trade Organization (WTO), and through an empirical assessment of recent developments in U.S. trade policy. I draw upon my own interpretation of Vernon’s paradigm to examine how the evolution of industries in a developed economy can shape the options available to their competitors — or partners — in developing countries.

The analysis that follows is generally in agreement with the conclusions that Deardorff reaches with respect to the needs of developing countries and the obligations of their trading partners. I nevertheless employ some assumptions and make some observations that depart from those of his paper. I contend that while traditional demands for protection (tariffs, quotas, and other border measures) have not disappeared altogether, they are no longer the principal instrument of trade policy. The more relevant question is whether and on what terms the existing trade barriers will be reduced or removed. The product-cycle paradigm helps to explain why it is that U.S. barriers to imports in some sectors have been removed, others remain relatively untouched, and still others are reduced or removed only on a selective (i.e., discriminatory) basis. Put another way, an updated version of Vernon’s model helps us to understand why policymakers are increasingly prone to choose the “second best” option of regional trade agreements and preferential trade programs, rather than universal and nondiscriminatory free trade.

The Product Cycle and its Implications

Let us begin by reviewing Vernon’s principal points regarding the technological and geographical transitions of industries. His product-cycle paradigm suggested that an industry’s competitiveness will go through a predictable series of stages:

To begin with, U.S.-controlled enterprises generate new products and processes in response to the high per capita income and the relative availability of productive factors in the United States; they introduce these products or processes abroad through exports; when their export position is threatened they establish overseas subsidiaries to exploit what remains of their advantage; they retain their oligoplistic advantage for a period of time, then lose it as the basis for the original lead is completely eroded. (1971: 66)

While Vernon’s main objective was to explain the causes and consequences of foreign investment, the stages that he identified also implied that an industry’s perspective on trade policy
will evolve. Industries can be expected to favor open markets when they are competitive and to favor protection when they are not. Deardorff’s analysis is largely consonant with this cycle, but brings into closer consideration the role of developing countries’ exports in challenging the developed countries’ industries.

While I am largely in agreement with the basic points raised by both Vernon and Deardorff, I would suggest two adjustments. The first is that a different policy question may be in order. To paraphrase, Deardorff’s question seems to be, “Will developed countries respond to increased competition from developing countries by erecting new barriers to trade?” I would instead ask, “How will the interests of declining industries in developed countries affect the pace and form of new trade liberalization?” While I understand the usefulness of the simplifying assumption that the two countries in the model “are initially engaged in free trade” (ibid.: 3), I think it is equally simple and more realistic to begin with the assumption that restrictions to trade already exist. It would be a great exaggeration to claim that the WTO rules are so watertight as to prevent countries from imposing any new restrictions on trade, but I would quarrel with the suggestion that we “simply assume that [increased import competition will] lead the North to implement a tariff on imports” (ibid.: 9). The track record for both legislated protection1 and safeguards cases2 suggests that protectionist industries have had little success in winning support from government. The clear trend of the past half century has been towards the reduction of tariffs and (more recently) the replacement or elimination of quotas. In an environment of declining tariff barriers, the best that most protectionist industries can hope for is to secure a pledge that their products be exempted from reductions. Even when one acknowledges the continuation of “peak” tariffs in some industries and the mischief that can be done with antidumping duties and other instruments of protection, the fact remains that markets are much more open today than they were in decades past. Moreover, the rules are more comprehensive and enforceable under the WTO than they were under the GATT.

The second important departure is that the range of options is not limited to a dichotomous choice between “free trade” or “protection.” Beyond the almost trivial point that there are many degrees of openness, representing every step from zero barriers to confiscatory levels of protection, discrimination is an equally important consideration. Here the rules of the GATT and WTO have been permissive. Free trade agreements (FTAs) and customs unions are allowable exceptions to the general rule of universal most-favored-nation treatment (provided that they meet the requirements of GATT Article XXIV), and preferential trade programs such as the Generalized System of Preferences (GSP) are granted waivers. While each of these options provide for more liberal trade, and many extend special treatment to developing countries, they are widely seen as a “second-best” alternative to nondiscriminatory liberalization. For reasons that I explore below, however, the increasing use of these discriminatory instruments can also be portrayed as a natural consequence of the product cycle.

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1 Although there have been many efforts since the Hawley-Smoot Tariff Act of 1930 to enact bills imposing tariffs or quotas on imports, no major bills have been enacted over a presidential veto. There have been several instances, however, in which presidents felt obliged to make concessions to protectionist demands in order to win congressional approval of some other market-opening initiative (especially new grants of negotiating authority or the approval of a trade agreement). In other words, some of the rare steps backward have been price for making two steps forward.

2 Petitioners have succeeded in winning import protection in only 23 of the 70 cases considered in the quarter century since enactment of the current safeguards law (section 201 of the Trade Act of 1974).
Implications of the Product Cycle for Trade Policy

The product-cycle model could be used to explain any one of three approaches to trade policy. Depending on how one views the interests of firms and the responses of government, the cycle could be predicted to encourage more open markets, more protection, or more discrimination.

Under the benign view that seems implicit in Vernon’s analysis, the product cycle can be portrayed as a progressive mechanism. A country with an efficient process of “creative destruction” could theoretically sustain a permanent free-trade orientation, with few or no exceptions for specific industries. Vernon’s views were similar to those of Schumpeter (1936), who believed that a combination of entrepreneurial innovation and periodic depressions provided just such an engine of progress. A real free-trading country would regularly produce a new crop of innovators, while firms that lost their competitiveness would either find new lines of work or be swept away when the business cycle swung downward. The survivors favor open markets. This Darwinian optimism is challenged, however, if firms and workers in a declining industry refuse to go quietly into that good night. A more pessimistic interpretation is that old firms and their workers do not always conveniently disappear or get reabsorbed into the economy, but instead seek ways to keep alive even after they pass their prime. Deardorff’s analysis falls into this second category. He concludes that factor owners in the developed country will respond to a competitive challenge by demanding and receiving protection.

I offer yet a third alternative, in which the product cycle encourages the reduction of trade barriers but does so in an increasingly discriminatory fashion. My adaptation of Vernon’s model, which is illustrated in Figure 1, departs from the original in two ways. First, I believe that a wider range of stages should be represented in the model. Second, I more explicitly state what the trade (in addition to the investment) preferences of an industry will be as it passes through these stages. My adaptation recognizes that the policy options available to industries and countries are not limited to opening or closing the market, but also allow for discriminatory initiatives that better lend themselves to manipulation on behalf of specific firms or trading partners.

The stages might respectively be termed pre-competitive, semi-competitive, competitive, and post-competitive. The distinctions between industries in stages 2, 3, and 4A are particularly important. Each one of these stages is “pro-trade,” but they favor different emphases in both the objectives and form of trade agreements. Only the Stage 3A industry is the pure free-trader. Industries in stages 2, 3B, and 4A each take a more qualified approach to open markets, and may be reluctant to support universal liberalization. An industry’s most critical choice comes in the fourth stage, when it must choose between retreat into the domestic market or relocation of its production offshore. The initial decision to invest overseas might have been made in an earlier stage, prompted by such diverse objectives as gaining or maintaining access to a large and protected foreign market, taking advantage of lower wage rates and less restrictive regulatory environments, or reducing transportation costs. When an industry’s competitiveness declines, however, it could decide to shift most or all of its production offshore. Those firms that become multinational producers (Stage 4A) acquire interests and preferences very different from those that do not (Stage 4B). A multinational producer will be much more favorably disposed towards open markets than a “mature” domestic industry, but will not inevitably be a paragon of free-trade purism. These producers may perceive a strong incentive to support discriminatory options, especially if they create sanctuary markets at home or abroad.
**Figure 1**

Varying Paths in the Product Cycle and an Industry’s Policy Preferences

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**Stage 1: Infant Industry**

The industry will theoretically seek protection from import competition, and may favor the free importation of raw materials and capital goods, but in actual practice it is unlikely to have sufficient political influence to obtain such treatment (unless it is deliberately created and fostered by government policy).

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**Stage 2: Emerging Exporter**

The industry will seek the reduction of foreign barriers to its own exports. It may be willing to support reduction of the home country’s import barriers (especially in industries other than its own) in order to achieve this objective.

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**Stage 3A: Dominant Exporter**

The industry is highly competitive, and enjoys a dominant position in markets that are open to exports.

It will favor the reduction or elimination of all foreign barriers to trade, even if this means reducing or eliminating home-country barriers in its own industry.

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**Stage 3B: Competitive Exporter**

The industry competes with foreign producers in the home market and in third-country markets. It favors reduction or elimination of all foreign barriers to trade, but not necessarily the reduction of home-country barriers. It may prefer the use of “reciprocity” laws over the negotiation of mutually liberalizing agreements, and favor discriminatory over multilateral agreements.

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**Stage 4A: Multinational Producer**

In response to declining competitiveness, the industry moves some or all of its production off-shore. It will demand elimination of home-country barriers to imports of its foreign-produced goods, which may mean favoring discriminatory programs or agreements over multilateral liberalization.

The industry is particularly susceptible to internal divisions at this stage, with its workers and less competitive producers staying in Stage 4B.

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**Stage 4B: Post-Competitive Domestic**

The industry is no longer competitive in export markets, and will concentrate on maintaining market share at home. This may entail a return to the protectionist orientation that it professed in infancy.

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**Stage 5: Disappearance**

A post-competitive industry may lose its battle with foreign competitors, and even a competitive multinational producer can be eliminated by shifting consumer preferences or changes in technology.
The process shown in Figure 1 is of course a deliberate simplification. Not all industries will follow along the entire path, not all of the firms in an industry will necessarily be in the same stage at the same time, and it is not inevitable that every industry slouch towards decrepitude and disappearance. It should also be stressed this figure summarizes the preferences of an industry’s management and ownership rather than its workers, a point is that explored below. This scheme nevertheless highlights some analytically useful distinctions.

**Discriminatory Options for Industries in Transition**

When viewed in the aggregate, these changes help to explain the “big picture” of an evolving U.S. trade policy. Largely in response to shifts in the interests of domestic industries, the United States moved from an orientation of nondiscriminatory protection (1816-1933) to discriminatory liberalization (1934-1942), and from nondiscriminatory liberalization (since 1942) to the adoption of a growing number of discriminatory agreements and programs since the mid-1960s. When viewed at the industry level, these changes help to explain the specific policy options that individual industries favor.

One option for the declining industry is to fall back upon the domestic market, and to adopt a protectionist orientation. While several U.S. industries have indeed entered Stage 4B, the batting averages for their efforts to win protection are not good. Presidents usually veto any blatantly protectionist bills that Congress enacts, and (under the stricter rules of the WTO) it would be costly to sustain such restrictions if they were enacted. The most that the typical Stage 4B industry can accomplish is to convince U.S. negotiators that their tariff protection should not be further reduced, and to request that antidumping duties be imposed.

Those protectionist measures that are imposed may only slow the rate of decline. When faced with the alternative of Stage 5 (disappearance), many firms will consider the switch to Stage 4A (multinational production). This may involve the actual relocation of its facilities offshore, or some less drastic form of investment (e.g., outsourcing specific components or production processes). It is at this stage that the interests of firms and their workers diverge. As a general rule, the views of labor and management are congruent on trade (if not other matters) in stages 1 through 3. Workers are just as eager as their employers to obtain protection when the industry is young and to penetrate foreign markets when it is vigorous, but this community of interests will be challenged as an industry faces decline. An industry that enters Stage 4B will continue to hold preferences that still coincide with those of its workers. By contrast, labor-management relations in a Stage 4A industry are bound to be problematic. Capital may move easily across borders, but workers in a declining industry often see no alternative to the adoption of protectionist positions. Vernon’s observations on labor-management disputes in such firms remain valid today. He noted that —

> The real concern [for U.S. labor unions], it sometimes seems, is the very same encountered in the reactions of host governments and their local elites including their labor union leaders. The multinational enterprise is strong and supple. When confronted as an adversary, it seems to have options that U.S. labor does not, such as the option to move its production abroad. From labor’s viewpoint, the hand of management is strengthened by the existence of the options, whether or not they are exercised. (1971: 190)

This passage could easily be written today by any observer of U.S. labor unions. Being trapped by their immobility in a permanent Stage 4B status, unions in declining industries naturally take a hostile view towards proposals for new trade agreements.
Some Stage 4A industries favor a policy of pure free trade in their own sectors (what are sometimes termed “zero-for-zero” initiatives), but others prefer more targeted initiatives. The expansion of discriminatory trade agreements and programs is the most consequential development in U.S. trade policy since the establishment of GATT, and one that is actively encouraged by some multinational producers. Both through the one-way avenue of nonreciprocal trade preferences and the negotiation of reciprocal FTAs, discrimination has created new opportunities for the manipulation of trade rules to benefit specific U.S. industries.

These discriminatory arrangements are now a key part of a multi-tiered trade regime. The six major categories of trading partners are illustrated in Table 1, together with recent trade data. Just under half of all imports in 1999 originated in countries that receive permanent normal trade relation (PNTR, formerly known as most-favored-nation treatment). Even with the extension of PNTR to China, which should mean that this category will once again account for a majority of U.S. imports, the significance of preferential agreements and programs is quite apparent. The table also identifies still more preferential arrangements, both negotiated (reciprocal) and legislated (unilateral), that are under consideration.

Each one of these programs offers opportunities for the manipulation of rules on behalf of specific U.S. industries. The most simple and obvious benefit for Stage 4A industries is that such programs and agreements can limit the extension of preferential treatment to those countries that host their offshore investments, while keeping imports from third countries subject to the existing tariff rates. Some industries take the further step of seeking more specific rules of origin (ROOs). These are the rules by which a product is deemed eligible for preferential treatment. Some programs have fairly simple and standard ROOs, such as the GSP (which generally requires that at least 35 percent of the value of an import originate in the beneficiary country), but the ROOs for the more generous programs are often predicated on the inclusion of U.S. materials. This point is illustrated below, using the examples of preferential trade in automotive products and the textile and apparel sector.

Example 1: The Automotive Industry

The U.S. automotive industry has experienced every stage but disappearance. The policies that it has promoted along the way, and that the government has usually granted, follow the pattern suggested in Figure 1. The industry sought and obtained protection from imports when it was still in its infancy (Stage 1). The tariff acts of 1897 and 1909 imposed high rates of 45 percent ad valorem on automobiles. The industry’s outlook changed as it came to dominate global markets. Even though the Fordney-McCumber Tariff Act of 1922 and the Hawley-Smoot Tariff Act of 1930 were both protectionist instruments, they saw reductions in automobile tariffs to 25 and 10 percent, respectively. The automotive industry then became a core member of the free-trade lobby. The U.S., producers supported the extension of tariff-negotiating authority to the president in 1934, as well as the many renewals of this authority in the decades to come. Through the 1960s, this was a Stage 3A industry that sought reductions in foreign barriers, and was quite willing to see U.S. tariffs reduced in pursuit of that objective.
## Table 1
Discrimination in Access to the U.S. Market

*Presented in descending order of preferential treatment; import data as of 1999*

<table>
<thead>
<tr>
<th>Type</th>
<th>Terms</th>
<th>Countries</th>
<th>Share of Imports</th>
<th>New Programs or Agreements</th>
</tr>
</thead>
<tbody>
<tr>
<td>Free trade agreements</td>
<td>Comprehensive duty- and quota-free access to the U.S. market</td>
<td>Israel (since 1985), Canada (since 1989), and Mexico (since 1994)</td>
<td>31.2%</td>
<td>Free Trade Area of the Americas and APEC agreement are planned</td>
</tr>
<tr>
<td>Special trade preferences</td>
<td>Duty-free access for almost all exports other than oil, textiles and apparel, etc.; a “special access program” for the Caribbean Basin provides quota-free privileges to certain textile and apparel imports</td>
<td>Most Central American and Caribbean countries under the Caribbean Basin Initiative (since 1984); Bolivia, Colombia, Ecuador, and Peru under the Andean Trade Preferences Act (since 1991, expires in 2001)</td>
<td>2.9%</td>
<td>Trade and Development Act of 2000 expands CBI benefits and establishes a new program for sub-Saharan Africa; a Southeastern European Trade Preferences Act is pending in Congress</td>
</tr>
<tr>
<td>Generalized System of Preferences</td>
<td>Duty-free access for many exports, but several significant product areas are excluded, and numerous provisions allow for the removal of specific products or countries</td>
<td>Most developing and transition economies; among the exceptions are China, most OPEC members, some Asian newly-industrialized economies, and Nicaragua (a CBI country)</td>
<td>10.2%</td>
<td>Designation of Nigeria is currently under consideration</td>
</tr>
<tr>
<td>Permanent normal trade relations (NTR or PNTR)</td>
<td>Also known as unconditional most favored nation or non-discriminatory treatment. Countries benefit from negotiated tariff reductions</td>
<td>Major partners that receive PNTR but no preferences include the European Union, Japan, most OPEC countries, and Asian newly-industrialized economies</td>
<td>47.3%</td>
<td>See below on conditional NTR</td>
</tr>
<tr>
<td>Conditional NTR</td>
<td>NTR treatment (as defined above) is subject to the freedom-of-emigration provisions of the Jackson-Vanik law</td>
<td>China, Albania, and most former Soviet republics are in this category (Albania and most former Soviet republics are also designated for GSP)</td>
<td>8.0%</td>
<td>Kyrgyzstan and Albania were graduated in May, 2000, and the graduation of China is pending in Congress</td>
</tr>
<tr>
<td>Sanctions</td>
<td>Countries are either denied NTR treatment (and hence face Hawley-Smoot tariff rates) or are subject to partial or total embargoes</td>
<td>NTR denied to Afghanistan, Laos, and Vietnam; trade embargoed with Cuba, Iran, Iraq, Libya, North Korea, Sudan, and Yugoslavia</td>
<td>0.4%</td>
<td>NTR agreements are pending with Laos and Vietnam; pending initiatives would reform sanctions</td>
</tr>
</tbody>
</table>

Note: Some countries fall under more than one category. For data on shares of U.S. imports, countries are counted in the most favorable category that is applicable. For example, Russia can be classified both as a GSP beneficiary and a recipient of conditional NTR treatment; imports from that country are counted here in the GSP category.

“Share Entering Under Preferences” includes all imports from a group that enter under terms other than MFN.
The industry adopted a more cautious approach in the 1970s, when the rising price of oil led consumers to favor imports of more fuel-efficient cars from Japan and elsewhere. By the late 1970s and early 1980s, U.S. car companies were in serious danger of entering Stage 4B. Their support for mandatory “domestic content” and other protectionist initiatives was clear evidence of this transition. Apart from convincing Japan to impose voluntary export restraints — a “gray area measure” that was permissible under GATT but would now violate the stricter rules of the WTO — those efforts failed. The U.S. producers (but not their associated labor unions) moved instead into Stage 4A, expanding what had already been highly globalized operations. This did not mean returning fully to the advocacy of free trade, but instead led them to support a more discriminatory (and therefore manipulable) approach.

The evolving preferences of this industry have played a major role in the changing U.S. policy towards discriminatory trade agreements. Three sequential North American trade agreements were driven in large measure by the automotive firms’ objective of establishing a regional sanctuary market. The first step in this direction, and indeed the first major U.S. move towards a discriminatory policy, was the AutoPact negotiated with Canada in 1965. This was followed by the U.S.-Canada Free Trade Agreement (CFTA) in 1988 and the North American Free Trade Agreement (NAFTA) in 1993. Each successive agreement further manipulated the rules to restrict trade from non-participating countries. The AutoPact operated on the basis of negotiated production quotas, and some non-North American producers did join between the mid-1960s and the mid-1980s. The CFTA froze company membership in the AutoPact as of 1989, and required that vehicles contain 50 percent North American content. NAFTA rules of origin raised the required level of regional content in stages, reaching 60-62.5 percent (depending on the type of vehicle) in 2002. The net result of these progressively tighter rules is that Japanese, European, and other automotive “transplants” in North America face serious obstacles to participation in NAFTA, while their home-country exports continue to face barriers to each of the North American markets. The Big Three firms were enthusiastic supporters of both the CFTA and NAFTA, but blocked multilateral reduction of U.S. barriers in the Uruguay Round. As the model predicts, the United Auto Workers opposed all three initiatives and remains a strong opponent of trade-liberalizing initiatives.

These successive agreements have prompted a significant reordering of trade flows in the automotive sector. As of 1999, Canada was by far the largest U.S. trading partner in this sector, and Mexico came in third behind Japan. Taken together, the United States exported 53 cents worth of automotive products to its two North American partners for every dollar worth of automotive products that it imported from them. By comparison, every dollar worth of automotive imports from Japan was matched by just 5 cents worth of automotive exports. These comparisons may mean to little to free-traders, for whom market shares should be determined solely by market forces, but they have great persuasive power for neo-mercantilists in government and industry.

**Example 2: The Textile and Apparel Industry**

Preferential trade programs can be just as readily manipulated as FTAs for the benefit of Stage 4A industries, or even to encourage firms to make an orderly transition from 4B to 4A. This is illustrated by the experience with the Caribbean Basin Initiative, the African Growth and Opportunity Act, and the “outward processing” program, each of which is designed to encourage co-production of apparel between U.S. manufacturers and firms outside of Asia. In so doing, they help to retain a significant share of U.S. value in the finished product.
Three successive administrations have employed preferential programs in order to encourage co-production in the textile and apparel sector. These programs are based both on foreign policy goals (i.e., extending assistance to favored countries and regions) and on the economic objective of easing the decline of a U.S. industry. The United States cannot economically preserve a large textile and apparel sector, but segments of this industry could survive and even thrive if they can take full advantage of lower labor costs in offshore facilities. One underpinning of this policy is a direct relationship between the degree of preferential treatment that is extended to a trading partner and the requisite level of U.S. content. In ordinary (non-preferential) imports of apparel, the country of origin for a garment is considered to be wherever the item is assembled. In order to benefit from a preferential program or agreement, a garment must meet much stricter ROOs that require the inclusion of U.S. materials.

The first step towards this policy came with the Reagan administration’s Caribbean Basin Initiative (CBI). The original tariff preferences of the CBI did not cover textile and apparel products — Congress would not have approved such a proposal in the early 1980s — but the Reagan administration instead developed a “special access program” (SAP) based on preferential quota treatment. The program has offered virtually quota-free access to the U.S. apparel market for Central American and Caribbean exports if a garment is made from fabric that is woven and cut in the United States. This approach was taken a step further when the Bush administration negotiated NAFTA. In order to benefit from this agreement’s quota- and duty-free access, products are variously subject to either a “yarn-forward” rule (i.e., the yarn must be spun in a NAFTA country) or a “fiber-forward” rule (i.e., the raw material from which the fabric is made must originate in a NAFTA country). The degree of required North American content is specified for each product.

Recent trade data support the contention that these programs have had the intended effect. Producers in Mexico and the Caribbean Basin reached a watershed in 1997, when they accounted for a larger volume of U.S. apparel imports than did the Far East. And for every dollar worth of textile and apparel products imported from countries in the Western Hemisphere in 1999, the United States exported to them 58 cents worth of products in this sector (including fabric, partial made-ups, and finished goods). By contrast, the United States exported just 4 cents worth of product to Asia for every dollar worth of textiles and apparel imported from that region.

Textile and apparel trade policy is now being reordered in anticipation of the Multifibre Arrangement’s demise. The Uruguay Round agreements set a ten-year schedule for elimination of this instrument and the import quotas that it permits. Tariffs will still be quite high, however, and thus will continue to offer an opportunity for market manipulation through discriminatory programs. Tariff preferences are now being extended to selected U.S. trading partners, for precisely the same reason that quota preferences were extended in the mid-1980s.

The “Trade and Development Act of 2000,” which was enacted into law in May, 2000, expands the preferential treatment extended under the CBI, and creates new preferences for sub-Saharan African countries. What is most interesting about the political economy of these preferences is not that “the U.S. textile unions have mounted an effective campaign against” them (Deardorff, 2000: 17), or that this opposition was eventually overcome, but instead the specific terms on which preferential treatment is being expanded for the Caribbean Basin and extended to

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3 This according to data from the American Textile Manufacturers Institute.
4 Calculated by the author from U.S. International Trade Commission data.
Africa. This is especially notable for the expanded CBI preferences, which were subject to a seven-year legislative battle. Stage 4A apparel producers favored the expansion of preferential access for their offshore production, but Stage 4B textile manufacturers insisted on even stricter ROOs that would require the incorporation of more U.S. materials. After years of confrontation and bargaining, these two industries and their legislative allies struck a compromise. The law provides for duty- and quota-free benefits to apparel made in CBI countries, but generally requires (with certain exceptions)\(^5\) that it be made from U.S. yarn or fabric. Similarly, the new African preferences offer a textbook example of how Stage 4A industries (though not their domestic workers) can convince Congress to manipulate ROOs for their benefit. Duty- and quota-free treatment for apparel imported from Africa is generally limited to garments made with U.S. fabric and yarns. Limited preferences are provided for certain products not meeting this description.\(^6\)

Other recent developments in U.S. policy are similarly designed to help the domestic industry keep a share of the value-added in imported apparel. Consider for example the new “outward-processing program” that applies to imports from Macedonia and Romania (and could be extended to others as well). Under the terms of this program and bilateral agreements, the beneficiary countries are not subject to quota limitations on certain categories of apparel, but only if the products are either assembled of fabrics formed and cut in the United States, or manufactured of fabric formed in the United States.

Once the textile and apparel quotas are phased out, access to the U.S. market is likely to be dominated by two groups of countries: those favored trading partners in the Americas and Africa that will enjoy duty-free access to the U.S. market, and the Asian producers that benefit from greater efficiencies and economies of scale. Third countries, especially “quota babies” that continue to benefit from the MFA restrictions, can expect to see their industries dwindle or even disappear. As for the U.S. industry, much depends on whether the current strategy allows it to maintain profitability in Stage 4A. If it can, further liberalization of the U.S. market is likely to be restricted to regional initiatives. The full and nondiscriminatory liberalization of the U.S. textile and apparel market is unlikely to be achieved unless the domestic industry finally disappears altogether (Stage 5).

**Conclusion**

The brief illustrations above offer examples of how the product cycle affects the trade and investment preferences of U.S. industries. Comparable stories could be told about other industries. The U.S. toy industry, for example, passed through a protectionist phase before it became fully multinational and free-trade oriented, while the experience of the footwear industry

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5 The law also provides for limited benefits for apparel made with fabric produced in the region, under specified conditions. Knit apparel made in CBI countries from regional fabric will receive duty-free, quota-free benefits up to a cap of 250 million SMEs (square meter equivalents). This cap will grow, compounded 16 percent per year for first three years with a Congressional review of the growth rate for the remaining years of bill. Other provisions allow special treatment for specified products such as T-shirts and brassieres.

6 Some provisions allow for preferential imports of products that do not incorporate U.S. fabric. Preferential treatment can be extended to products made with yarns or fibers that are not available either in the United States or Africa, or apparel made from cashmere or silk yarns. The bill limits duty-free access to the U.S. market for African apparel made with African fabric or yarn, subject to a cap of 1.5 percent to 3.5 percent of overall U.S. global apparel imports over eight years. Finally, a special provision will allow countries with an annual *per capita* income below $1,500 to use third-country fabric in African-made apparel for four years.
is very similar to that of the textile and apparel sector. The principal point here is that import competition does not inevitably lead to demands for protection from declining industries. Even when Stage 4B industries do seek restrictions on import competition, they do not receive it automatically. A widening circle of industries in decline have instead found that a combination of foreign investment and discriminatory trade arrangements can give them — though not all of their domestic workers — a means of surviving the competitive challenge. The product-cycle paradigm thus helps us to understand how and why liberalization has proceeded on a geographically and sectorally uneven path. Vernon already identified the investment option a generation ago; it took another decade or two for the discriminatory trade option to emerge.

What does all of this mean for developing countries? By returning to Vernon’s original emphasis on the importance of investment and multinational operations, we can see how the multinational operations of U.S. firms can offer varying challenges and opportunities for developing countries. The implications of this process vary considerably, according to the degree of preferential treatment that a specific country receives. It is fairly obvious that the partners with which the United States negotiates FTAs, or to which it extends special preferences, ought to fare better than those countries that are excluded from these arrangements. The more difficult issue to assess is what the expansion of discrimination means for the world as a whole. It is well beyond the limited aims of this comment to delve into the extensive debate over discriminatory trade agreements as a “second-best” alternative to nondiscriminatory liberalization. Suffice it to say that the received opinion of the economic community ranges from a grudging acceptance of discriminatory agreements to deep concerns over their implications for the multilateral trading system. For good or for ill, they are an increasingly important aspect of the U.S. trade regime. The widening range of discriminatory arrangement can also be seen as a natural consequence of the product cycle.
References