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Introduction

“TRADE is BAD.”

So wrote President Donald Trump on a draft speech he was editing on Air Force One while returning from a G-20 summit meeting in 2017.¹ This statement reflects the president’s deeply held view that imports, enabled by unfair trade agreements, have devastated the U.S. economy, putting manufacturers out of business and destroying jobs in the process. In his January 2017 inaugural address, the president stated:

For many decades, we’ve enriched foreign industry at the expense of American industry. . . . One by one, the factories shuttered and left our shores, with not even a thought about the millions upon millions of American workers left behind. The wealth of our middle class has been ripped from their homes and then redistributed across the entire world. We must protect our borders from the ravages of other countries making our products, stealing our companies, and destroying our jobs. Protection will lead to great prosperity and strength.

In Trump’s view, other countries have long been “taking advantage” of the United States in trade. China and others protect and subsidize their producers at our expense, steal our technology, and refuse to treat our goods fairly. The United States has been a big loser in global trade because the United States buys more from other countries (imports) than it sells to them

1. As reported by *Washington Post* investigative journalist Bob Woodward, *Fear: Trump in the White House*, New York: Simon & Schuster, 2018, 208.

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(exports), and thereby suffers from a \$800 billion merchandise trade deficit. This deficit, the president insists, is not just unfair but drains the lifeblood out of the country. In effect, other countries are raiding our piggy bank and ripping us off.

President Trump promised to confront this situation and “Make America Great Again.” As a first step, he insisted on getting out of bad old trade deals. In particular, he has long singled out the North American Free Trade Agreement (NAFTA), a pact between the United States, Canada, and Mexico that took effect in 1994, as “the worst trade deal ever.” He argued that letting China into the World Trade Organization (WTO) in 2001 was a disaster. And he rejected U.S. participation in the Trans-Pacific Partnership (TPP), a trade agreement between a dozen Pacific Rim countries negotiated by the administration of President Barack Obama.

Therefore, in his first week in office, President Trump withdrew the United States from the TPP. After threatening to withdraw from NAFTA, he was persuaded to renegotiate it. After months of contentious discussions, a new agreement dubbed USMCA (for United States—Mexico—Canada Agreement) was reached. Although he has not tried to kick China out of the WTO, he began to isolate it by ratcheting up tariffs on its goods.

The president has shown himself to be a tariff enthusiast, happy to impose taxes on imported goods in the belief that they would strengthen the American economy. “I am a TARIFF MAN,” he proudly tweeted. “When people or countries come in to raid the great wealth of our Nation, I want them to pay for the privilege of doing so.” Many of his tweets extol the benefits of tariffs: “Tariffs will make our Country MUCH STRONGER, not weaker. Just sit back and watch!” he wrote in May 2019. And so the administration began imposing tariffs: on washing machines and solar panels on grounds that imports were harming domestic producers, on steel and aluminum on grounds that imports threatened national security, and most significantly on imports from China on grounds of unfair trade. And for every tariff that has been imposed many more have been threatened: on imported automobiles from Japan and the European Union (EU), on Mexico over immigration problems, among others. As Trump trade adviser Peter Navarro said, “We love tariffs. Tariffs are a wonderful thing.”²

2. https://www.washingtonpost.com/business/economy/trump-says-he-will-impose-new-tariffs-on-300-billion-in-chinese-imports-starting-next-month-ending-brief-cease-fire-in-trade-war/2019/08/01/d8d42c86-b482-11e9-8949-5f36ff92706e_story.html?utm_term=.458fd9959e26.

These actions have been controversial at home and abroad. At home, even within the Trump administration, there was a sharp division between the so-called globalists, who resisted imposing tariffs and withdrawing from trade agreements in the belief that trade strengthens America and its position in the world, and nationalists who are convinced that trade and international agreements hurt the economy and tariffs would help. The president has sided with the nationalists. As he put it: “I’m different than a lot of people. I happen to think the tariffs for our country are very powerful.”³ As a result, the globalists gradually left the administration.

And abroad, the new tariffs have caused outrage, leading many other countries to retaliate by slapping their own tariffs on American products. After the Trump administration imposed tariffs on imported steel, European Commission President Jean-Claude Juncker said: “So now we [the European Union] will also impose import tariffs. This is basically a stupid process, the fact that we have to do this. But we have to do it. We will now impose tariffs on motorcycles, Harley Davidson, on blue jeans, Levis, on Bourbon. We can also do stupid. We also have to be this stupid.”⁴ China’s retaliation hit American soybean farmers particularly hard and they lost a major market for their goods. (As a result, the Trump administration has promised to spend \$28 billion to help bail out farmers from the effects of the trade war.)

You might expect Democrats, who oppose so much of what President Trump stands for, to object to these aggressive trade actions. You would be wrong. Although they might disagree with his tactics, many Democrats share Trump’s view that trade has been bad for America. (Elizabeth Warren has unveiled a progressive plan to promote what she calls “economic patriotism.”) They also want to bring back blue-collar manufacturing jobs and revitalize the heartland of the industrial Midwest. Meanwhile, Republicans in Congress, who have been the strongest backers of freer trade over the past few decades, want to support the president but fear that he has taken the trade war too far and thereby hurt the economy. Those from agricultural states in the Midwest have seen their constituents stung by foreign retaliation against American farm exports and the failure to increase exports by withdrawing from trade agreements such as the TPP.

As never before in recent history, the Trump administration has put free trade under fire.

3. https://www.wsj.com/articles/u-s-to-move-forward-with-china-tariffs-trump-says-11557424081?mod=hp_lead_pos1.

4. <https://www.euronews.com/2018/03/03/juncker-responds-to-trump-s-trade-tariffs-we-can-also-do-stupid->

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And yet, to some extent, free trade is always under fire. Trade policy invariably generates controversy because dollars and jobs are at stake, and therefore the political wrangling over the direction of policy is ever present.

Of course, the nature of the controversy and the intensity of the arguments about trade change over time. With each passing decade, some of the old fears about trade recede and new ones take their place. In the 1980s, many Americans were convinced that Japan would achieve world economic dominance because Japanese manufacturers seemed to be wiping out industry after industry in the United States, from automobiles to semiconductors to supercomputers. These concerns faded in the early 1990s when Japan entered a prolonged economic slump. In the early 1990s, NAFTA generated fears of a “giant sucking sound” of jobs being lost to Mexico because of its low wages. (We owe this memorable phrase to Texas billionaire and 1992 presidential candidate Ross Perot, who was a leading anti-NAFTA activist.) These concerns faded when the U.S. economy boomed in the late 1990s, leading to a federal budget surplus and low unemployment.

Then, in 1999, the streets of Seattle were filled with large protests against the WTO for its promotion of freer trade and alleged indifference to workers and environment. (The first edition of this book was published in 2002 in part to address such fears.) These concerns faded when the WTO membership failed to move forward with any new trade initiatives and its dispute settlement process successfully defused trade frictions without undermining national sovereignty.

In the first decade of the twenty-first century, attention shifted to China. A goliath in the production of manufactured goods, China—it is often argued—has been responsible for huge job losses in the United States. Around the same time, fears that white-collar jobs (from call centers to software programming) could be “outsourced” to other countries such as India sparked new worries of a “service-sector sucking sound.” Just as both these fears were peaking, the global financial crisis of 2008 struck and the volume of world trade plummeted 12 percent. Economists and policymakers were concerned that the Great Recession of 2009 could lead to widespread protectionism like that seen during the Great Depression of the 1930s, but trade policies in fact remained relatively open. By 2019, with the economy growing and the unemployment rate below 4 percent, fears about “outsourcing” had all but disappeared, but China is still viewed as a serious threat to the American economy—now for national security reasons rather than the job-destroying impact of its exports.

Thus, fears about trade are ever present but ebb and flow, in good times and in bad. The 1990s were a period of robust economic growth and the

lowest U.S. unemployment in thirty years, yet NAFTA and the WTO generated heated debates. And economic downturns invariably continue to bring out cries that foreign countries are stealing our jobs and therefore protectionist trade policies are required to protect American workers and the industries that employ them.

Opponents of free trade are not confined to one segment of the political spectrum, and trade skeptics can be found everywhere. And the litany of complaints placed on the doorstep of free trade goes well beyond the perennial objection—emphasized regularly by most opponents to the current system—that trade forces painful economic adjustments such as plant closings and layoffs of workers. Liberal Ralph Nader charges that “the Fortune 200’s GATT [General Agreement on Tariffs and Trade] and NAFTA agenda would make the air you breathe dirtier, and the water you drink more polluted. It would cost jobs, depress wage levels, and make workplaces less safe. It would destroy family farms and undermine consumer protections.” Conservative Patrick Buchanan chimes in with the claim that “broken homes, uprooted families, vanished dreams, delinquency, vandalism, crime—these are the hidden costs of free trade.”⁵

The many critics of free trade include not just politicians who advocate economic nationalism and workers who have lost their jobs because of imports. A wide range of groups, from environmentalists to religious organizations to human rights activists, have joined in protesting against free trade. These groups rail against trade agreements such as NAFTA and the WTO as benefiting corporations, harming workers, decimating manufacturing industries. Progressives worry that trade will undercut environmental regulations and social policies; conservatives worry that it will undermine America’s sovereignty and compromise national security.

In his 2006 book *Myths of Free Trade*, Senator Sherrod Brown (D-Ohio) wrote:

An unregulated global economy is a threat to us all—to the child in Avon Lake, Ohio, who eats raspberries grown in Guatemala by poorly paid farmers who use pesticides banned in the United States; the unskilled, minimum wage worker in Los Angeles who loses her job to an unskilled, five-dollar-a-day worker in Yucatan; the machinist in New York who takes

5. Ralph Nader, ed., *The Case Against Free Trade: GATT, NAFTA, and the Globalization of Corporate Power*, San Francisco: Earth Island Press, 1993, 1; Patrick Buchanan, *The Great Betrayal: How American Sovereignty and Social Justice Are Being Sacrificed to the Gods of the Global Economy*, Boston: Little, Brown, 1998, 286.

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a wage cut because of his company's threat to move to China; the Chinese prison camp laborer; the tomato grower in Florida who has to sell his farm; and the peasant in Chiapas who must flee the native village where his family had made its home for dozens of generations. But our national leaders—particularly Republican congressional leaders and Presidents Clinton and Bush, economists and newspaper editors, business executives and tenured economics professors—continue to ignore the uncomfortable consequences of free trade, hoping the American public will not take notice.⁶

In an October 2014 op-ed in the *New York Times*, economic journalist Jeff Madrick wrote that “free trade creates winners and losers—and American workers have been among the losers.” Free trade policies, he argues, have been a “major” factor in the erosion of wages and the loss of job security.⁷

The United States is not alone in this regard. In almost every country, international trade brings out anxieties and insecurities. Just about every country lacks the confidence that it can “compete” in world markets, and fears being overrun by imports and being controlled by foreign corporations. Many people in the rest of the world fear economic domination by the United States. They buy Apple iPhones, use Facebook, depend on American wheat and corn, and fly on Boeing jets, and wonder how local producers can ever compete against large, wealthy, and technologically sophisticated American companies.

The rapid increase in international trade in recent decades is sometimes thought to have unleashed a “globalization backlash.” In this view, increased global integration has accelerated the pace of economic change and has brought with it painful economic adjustments. And the reach of world trade rules has gone beyond trade barriers to encompass domestic regulations regarding health, safety, and the environment. As a result, groups disturbed by these changes, whether directly in terms of their jobs or indirectly in terms of the community values they believe are at stake, have questioned the effects of global economic integration and the institutions associated with it. These groups have raised legitimate concerns about commerce and local communities and whether sovereignty has shifted from elected representatives at home to faceless and unaccountable bureaucrats abroad. Not just in the United States but around the world, people feel that they no longer

6. Sherrod Brown, *Myths of Free Trade: Why American Trade Policy Has Failed*, New York: New Press, 2006, 4.

7. Jeff Madrick, “Our Mislplaced Faith in Free Trade,” *New York Times*, October 3, 2014.

control their fate in this globalized world. Many analysts believe that the United Kingdom vote to leave the European Union (Brexit) and the election of Donald Trump, both in 2016, reflect this globalization backlash. Others contend that these events had more to do with cultural concerns about immigration rather than increased foreign trade.

Whatever the case, the debate over trade policy remains intense and shows little prospect of abating. The debate has raised many fundamental questions. Why is free trade considered to be a desirable policy? Do the most frequently made criticisms of free trade, such as its adverse impact on workers and the environment, have merit? Have developing countries benefited from trade, or does it just keep them poor and dependent on others? What is the World Trade Organization, and do world trade rules erode a country's sovereignty and undermine its health and environmental regulations?

This book aims to address these basic questions and demystify some of the complex issues surrounding trade policy. Despite widespread skepticism about free trade among many vocal groups, economists generally take a positive view of international trade and believe that reducing trade barriers is desirable. They see trade between countries as usually being mutually beneficial, just like the exchange of goods within a country. While some groups lose from trade, people around the world are generally much better off with trade than they would be without it. This perspective was originally developed by David Hume and Adam Smith in eighteenth-century Scotland and refined by David Ricardo in early nineteenth-century England and continues to this day.

Trade skeptics often accuse economists of having a religious faith in free trade, of blindly clinging to the doctrine in the face of contrary evidence. Peter Navarro, a trade adviser to President Trump, believes that economists adhere to an "outmoded Ricardian" model of trade that has "little or no relevance to today's world." In a 2019 presentation at Harvard University, entitled "Ricardo is Dead," Navarro argued that the conventional wisdom on trade currently taught in universities "is at best outdated and at worst misleading."⁸

In fact, the economic case for free trade is based not on faith but on logic and evidence. As Paul Krugman has written:

The logic that says that tariffs and import quotas almost always reduce real income is deep and has survived a century and a half of often vitriolic criticism nearly intact. And experience teaches that governments that imagine or pretend that their interventionist strategies are a sophisticated improvement on free trade nearly always turn out, on closer examination,

8. <https://www.thecrimson.com/article/2019/4/26/navarro-iop-talk/>.

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to be engaged in largely irrational policies—or worse, in policies that are rational only in the sense that they benefit key interest groups at the expense of everyone else.⁹

Still, the logic and evidence behind the case for free trade deserve to be put under searching scrutiny, as do the logic and evidence behind alternative policies. Even advocates of free trade need to be reminded of the case, lest they simply rehash stale arguments that fail to persuade. As John Stuart Mill argued, “Even if the received opinion be not only true, but the whole truth; unless it is suffered to be, and actually is, vigorously and earnestly contested, it will, by most of those who receive it, be held in the manner of a prejudice, with little comprehension or feeling of its rational grounds.” Consequently, “however true [a proposition] may be, if it is not fully, frequently, and fearlessly discussed, it will be held as a dead dogma, not a living truth.”¹⁰

While the views of economists deserve critical scrutiny, they also deserve a fair hearing. Economists have studied trade for a very long time and have noticed that the same worries and fears about trade tend to get repeated generation after generation. “With America’s high standard of living, we cannot successfully compete against foreign producers because of lower foreign wages and a lower cost of production.” This claim is heard today, but this particular statement comes from President Herbert Hoover in 1929 as he urged Congress to pass what became known as the Smoot-Hawley Tariff on the eve of the Great Depression. Among the claims heard yesterday and today is that trade will destroy jobs, leading to higher unemployment and lower wages, and that trade deficits will siphon away a country’s wealth. To economists, these are fallacies that history and experience have refuted time and again. One observer has quipped that “free traders are trapped in a public policy version of [the movie] *Groundhog Day*, forced to refute the same fallacious arguments over and over again, decade after decade.”¹¹ Or one could say that defending free trade is like playing the arcade game “Whac-A-Mole”: when one argument is beaten down, another pops up in its place.

This book aims to introduce the reader to some basic economic principles and empirical evidence regarding international trade and trade policy, so that we can better understand the current debate.

9. Paul Krugman, “Dutch Tulips and Emerging Markets,” *Foreign Affairs* 74 (1995): 31.

10. John Stuart Mill, *On Liberty*, New York: Penguin, [1859] 1982, 116, 97.

11. Julian Sanchez, “Lou’s Blues: Lou Dobbs and the New Mercantilism,” *Reason*, October 30, 2003.

Chapter 1, “The United States in the Global Economy,” sets out basic facts about international trade and the U.S. economy. World trade has expanded rapidly in recent decades, and this development provides the context in which to consider trade policy. This chapter discusses the reasons for the increase in trade, how trade has changed with the fragmentation of production and the increase in trade of intermediate goods, and the state of public opinion on the question of globalization.

Chapter 2, “The Case for Free Trade: Old Theories, New Evidence,” examines the economic logic of free trade and recent empirical evidence reinforcing the case for it. Ever since Adam Smith and David Ricardo described the gains from trade in a systematic way more than two centuries ago, economists have stressed the higher income that results from improved resource allocation as the main advantage of trade. But economists have discovered that trade not only helps to improve the allocation of existing resources but also makes those resources more productive. These productivity gains from trade are sometimes neglected but appear to be substantial. The welfare benefits of a greater variety of products as a result of trade have also been ignored until recently, and yet a growing body of evidence suggests that they are also quite important.

Chapter 3, “Protectionism: Economic Costs, Political Benefits?,” considers the flip side of the case for free trade—that trade interventions are often misguided and can be costly. Tariffs and quotas on imports redistribute income from consumers to producers, but they do so inefficiently. That is, trade barriers produce a net economic loss because the costs to consumers exceed the benefits to producers. In addition, trade barriers reduce exports and harm downstream user industries. The chapter also raises the question of why, despite its costs, trade protectionism is often politically attractive. Finally, the chapter examines situations in which protection may be justified in theory, even if governments might be ineffective in trying to take advantage of those situations.

Chapter 4, “Trade, Jobs, and Wages,” focuses on the most frequent argument in favor of limiting trade—that jobs will be saved in industries that compete against imports. As we shall see, reducing trade saves those jobs only by destroying jobs elsewhere in the economy. Opponents of free trade have also argued that imports have replaced good, high-wage jobs with bad, low-wage jobs. The truth turns out to be quite the opposite: Jobs in industries that compete against imports have been largely low-skill, low-wage jobs. This chapter also examines the extent to which trade with developing countries has contributed to the rise in inequality within the United States.

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Chapter 5, “Trade Remedies and Relief from Foreign Competition,” describes the legal framework that allows firms to petition the government for the imposition of tariffs on competing imports. The antidumping law is the most commonly used measure to block so-called unfair imports. The government’s definition of “dumping” is a lower price charged in the United States than in a foreign exporter’s home market, but it is not clear that this is a problem requiring trade restrictions, or that the government calculates the dumping margin in a fair manner. This chapter also examines the case for providing domestic industries with temporary relief from imports so that they can adjust to foreign competition, as well as the recently revived “national security” rationale for limiting imports.

Chapter 6, “Developing Countries and Open Markets,” takes a look at developing countries and asks whether free trade is beneficial in promoting economic development. Did countries such as Japan and Korea—and China more recently—grow rich by rejecting free trade and instead pursuing closed markets and industrial policies? The chapter also addresses the issue of fair trade and how rich-country agricultural subsidies and import tariffs harm developing countries, as well as how developing countries harm themselves with their own anti-trade policies.

Chapter 7, “The World Trading System: The WTO, Trade Disputes, and Regional Agreements,” focuses on the current controversies about the multilateral trading system, particularly the World Trade Organization. At its inception, the WTO was criticized by nongovernmental organizations (NGOs), which have attacked the WTO as an antidemocratic institution that has struck down environmental regulations by ruling them inconsistent with world trade laws. Now President Trump condemns it as a body rigged against the United States. This chapter examines the WTO’s rules and dispute settlement system, the trade conflict with China, as well as the rise of regional trade arrangements such as NAFTA and the TPP.

International trade and trade policies are frequently the object of condemnation rather than approbation. That condemnation is often the result of misconceptions about the benefits of international trade, the impact of trade policies, and the role and function of the WTO. This book seeks to shed light on these debates and is offered in the modest hope that it may improve our understanding of the trade policy issues that confront us.

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