Unit 3: The Case for Protection

Introduction

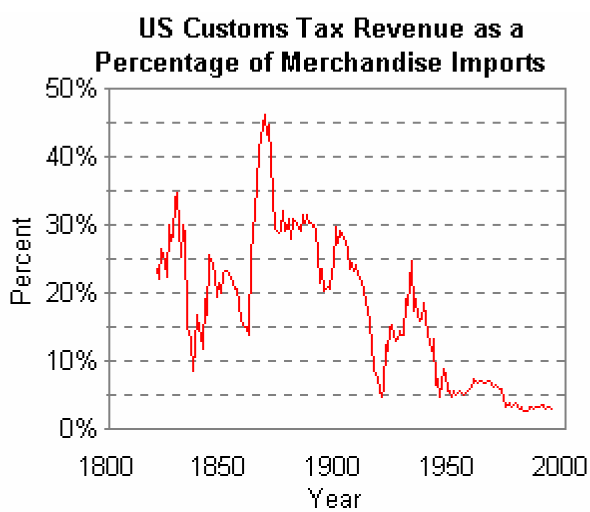
In general, the theory of comparative advantage tells us that protection of domestic industries from open markets makes everyone worse off. However, this isn't exactly true: protectionism affects different people in different ways, and not all kinds of protection are alike.

This unit looks at the history of protectionism in the US, the arguments made in favor of protectionism; some basic economic theory on the effects of tariffs, quotas; and other types of protectionism; and a look at who typically falls on which side of the protectionism-free trade debate.

Part 1: A Brief History of Protectionism in the U.S.

If it's fine to say that in theory protectionism doesn't work, or that it is less efficient than free trade, it's also true that protectionism has been an important part of the American landscape. Most famously, the Boston Tea Party acted out the North American colonists' resistance to a tax put on the tea Americans bought from then-monopoly the British East India company. Moreover, one of the underlying historical sources of tension between the antebellum North and South was American import tariffs on manufactures, which protected northern manufacturers and hurt southern plantation owners. The dispute was so intense that the South insisted the Constitution be drafted in such a way as to make it illegal for the newly empowered federal government to collect revenue through taxing southern cotton and tobacco exports. Even so, revenues from import tariffs quickly became a significant (and incredibly regressive) source of revenue for the US government until the passage of federal income taxes in the early 1900s.

TIP BOX:** A regressive tax taxes the poor at a higher rate than the rich. Because the poor spent nearly all of their income on subsistence consumption—including imports which had higher prices due to the tariffs—their income was essentially being taxed at a higher rate that the income of the rich, who could avoid such taxes through their propensity to save. In fact, such an argument can still be made today over state sales tax—which explains why most states have low or no sales taxes on grocery-store-bought food.



Source: 1821-1970: U.S. Dept. of Commerce: Bureau of Census, Historical Statistics of the United States, Part 2, 1976.

As mentioned in Unit 1, the Industrial Revolution (late 1800s - early 1900s) brought about what is commonly considered the first wave of globalization, and with it came dramatic reductions in US protectionist policy. But this did not last. The onset of World War I and the inter-war Depression Era that ensued saw dramatic increases in protectionism with policies like the Smoot-Hawley Tariff Act. FDR's "New Deal" and passage of the 1934 Reciprocal Trade Agreement Act helped to restore some openness to markets with the introduction of the reciprocal Most Favored Nations concept, but the outbreak of WWII put further steps toward liberalization squarely on hold.

Since WWII, the level of protection—as defined by the Global Agreement on Tariffs and Trade—has been falling. Today's import taxes are, on average, a bit less than a typical American state's sales tax. However, this decline of protectionism in the US has not been consistent across time or industry: it has proceeded in fits and starts and differs systematically across industries.

For example, just after the formation of GATT in the 1950s, tariffs fell dramatically as participants sought to avoid a beggar-thy-neighbor episode such as occurred between the two world wars. And although Europe sought increased protection from US competition as they rebuilt in the '60s, the developed capitalist nations cooperated more fully late in the decade, partly out of fear of the expanding Soviet Empire. In the '70s, oil shocks and the demise of the dollar-backed Breton Woods Fixed Exchange Rate System made protection fashionable again: it wasn't until the 1980s Tokyo Round of trade negotiations that GATT changed to cover non-tariff barriers to trade and paved the way for deeper integration in world trade zones in the '90s—through NAFTA, the EU, and South East Asia. Most recently, the war on terror, the rise of Chinese manufacturing, and concerns over the "outsourcing" of American jobs have lent impetus once again to protectionist feelings, although such feelings are sometimes inconsistently articulated and followed.

The Bush administration's flip-flop on steel tariffs clearly exemplifies this inconsistency. When the administration imposed tariffs on steel, they hoped to win battleground states in the midterm elections in 2002—notably Ohio and Pennsylvania. But in the last few months the administration rescinded the tariffs—years before they were set to expire—in part because they hurt American producers who use steel as an intermediate good, in part because the WTO declared them illegal, and in part because the European Union threatened retaliatory sanctions against goods produced in states even more important in the 2004 presidential election next year—Florida among them. One lesson from this episode in US trade policy: industry protection is frequently proportional to industry political power.

To learn more about the US steel industry tariff case, listen to the following series of audio clips which aired over the days following the WTO's ruling against the US.

AUDIO CLIP: NPR Audio: WTO Panel Rules U.S. Steel Tariffs Illegal (11/11/2003)

http://www.npr.org/features/feature.php?wfId=1501551

AUDIO CLIP: NPR Audio: U.S. Steel Tariffs Poised to End 12/1/2003)

http://www.npr.org/features/feature.php?wfId=1528224

AUDIO CLIP: NPR Audio: Steel Industry Faces Economic Competition (12/01/2003)

http://www.npr.org/features/feature.php?wfId=1528226

AUDIO CLIP: NPR Audio: Steelworkers React to Tariffs' Removal (12/04/2004) http://www.npr.org/features/feature.php?wfId=1532755

Other reasons for protecting industries include their historical significance, labor intensity, and importance for national security. Agriculture, which still receives generous subsidies from the federal government, is an example of an industry that is both labor intensive and historically significant. During the ’80s, the “crisis of the American farmer” was frequently described as the downfall of a way of life—an appeal to its historical significance and Americans’ identification with the rugged, earthy values that it represents. Labor-intensive industries, moreover, tend to draw protection because they *need* protection in international labor markets, and because industry labor intensity can be proportional to political significance—since *not* protecting such industries leads to higher job loss and more dissatisfied voters than failure to protect less labor-intensive industries.

At bottom, history has shown protectionist sympathies tend to grow in times of conflict or recession, and tend to be associated with labor-intensive, politically, and historically important industries. On the other hand, during times when the Bretton Woods and GATT institutions (the IMF, World Bank, and the WTO) are more or less supported, protectionist sentiment falls.

Part 2: Arguments in Favor of Protectionism

There are lots of reasons one could give in favor of protection (some of which were just mentioned above). One could argue that protection:

- saves jobs
- helps national security
- levels the playing field between nations with different environmental or labor regulations
- is patriotic
- generates government revenue
- preserves cultural heritage
- provides protection to newly developed industries until they reach the scale necessary to compete freely
- protects national health and safety
- is part of foreign policy
- is a good retaliatory measure

VIDEO: Arguments for Protectionism

VIDEO: Arguments for Protectionism

These videos will be discussed in Discussion Question #1.

None of these arguments is consistent with the theory laid out in the previous units. Nonetheless, some of these arguments are better than others. For example, the Japanese made the argument that nascent industries need protection for the better part of 20 years, and it resulted in Japan becoming the second largest and most dynamic economy in the world. (There were similar results for other of the Asian "Tiger" economies.).

Another palatable argument favoring protectionism is that of a level playing field.

Why should American workers lose their jobs only because another nation is willing to allow child labor and unsafe and unsanitary working conditions in their factories? Why should American workers lose their jobs when an American corporation finds it profitable to take advantage of another nation's lax environmental standards? Such differences do cause job losses in America, but they also result in lower prices for American consumers. Questions such as these do not have easy or obvious answers.

One argument that everyone can agree on in principle is the need for protectionism if the security or safety of a nation and its citizens are at risk. During the 1970s and '80s there was no question about subsidies for aerospace producers like Lockheed Martin, since defense technology was key to the Cold War and thus national security. Today it is imperative that we tighten security—and consequently the time it takes imports to clear customs—at our borders to minimize the threat of future terrorist attacks. But will there come a time when the delays at customs on the grounds of security are increasingly perceived as a protectionist tool which disadvantages the import competition? As for product safety, clearly the US should be within its rights to ban the importation of children's toys that do meet minimum protocol, but what about when the European Union bans the importation of American agricultural products produced using genetically modified means on similar grounds?

For more information on this contentious trade dispute listen to the following NPR audio clips:

AUDIO CLIP: NPR Audio: U.S. Wants Europe to Lift Ban on Biotech Food (5/14/2003)

http://discover.npr.org/features/feature.jhtml?wfId=1262971

AUDIO CLIP: NPR Audio: The Marketplace Report: Modified Foods Ban (9/10/2003)

http://www.npr.org/features/feature.php?wfId=1427093

These clips will be important to Discussion Question #2.

On the other hand, the argument that protection can stimulate a nation's economic growth by saving jobs only makes sense if the value of a job saved is worth more than the amount consumers must pay in higher prices in order to save it. And empirically, the evidence suggests that American consumers pay around $150,000 more for the goods they buy for every job that is saved. Additionally, one must also consider not only the jobs that are saved in the protected industry, but also the jobs that might be lost in our export industries if higher input prices or retaliatory measures ensue. For example, in the steel industry case mentioned above, it can be argued that although steel workers jobs were saved, many more jobs in were lost in American industries such as automobiles, which subsequently became less competitive due to the higher price they had to pay for the steel needed to produce their products.

VIDEO: The Hidden Cost of Tariffs on Consumers

VIDEO: The Hidden Cost of Tariffs on Consumers

OR

VIDEO: Tariff Escalation, Criticism of Steel Tariffs, Hidden Cost of Protectionism

Perhaps it's best, then, to view the protectionism, and the decision to impose it, as a commodity in the market place which has both its costs and its benefits—there's a certain "supply" of it which can be granted by the government, and a certain "demand" for it from industry adversely affected. On the supply side, before deciding whether to grant protection to an industry, the government should look at the number of jobs saved, the costs to society (in prices and effects on export industries), the political importance of jobs and costs, and the general climate of opinion at decision time. On the "demand" side, industry considers a number of things before petitioning for protection: the degree of their disadvantage, the market penetration of foreign goods, industry concentration, and their dependence on exports (since retaliatory tariffs will surely follow).

VIDEO: The Supply and Demand for Protectionism

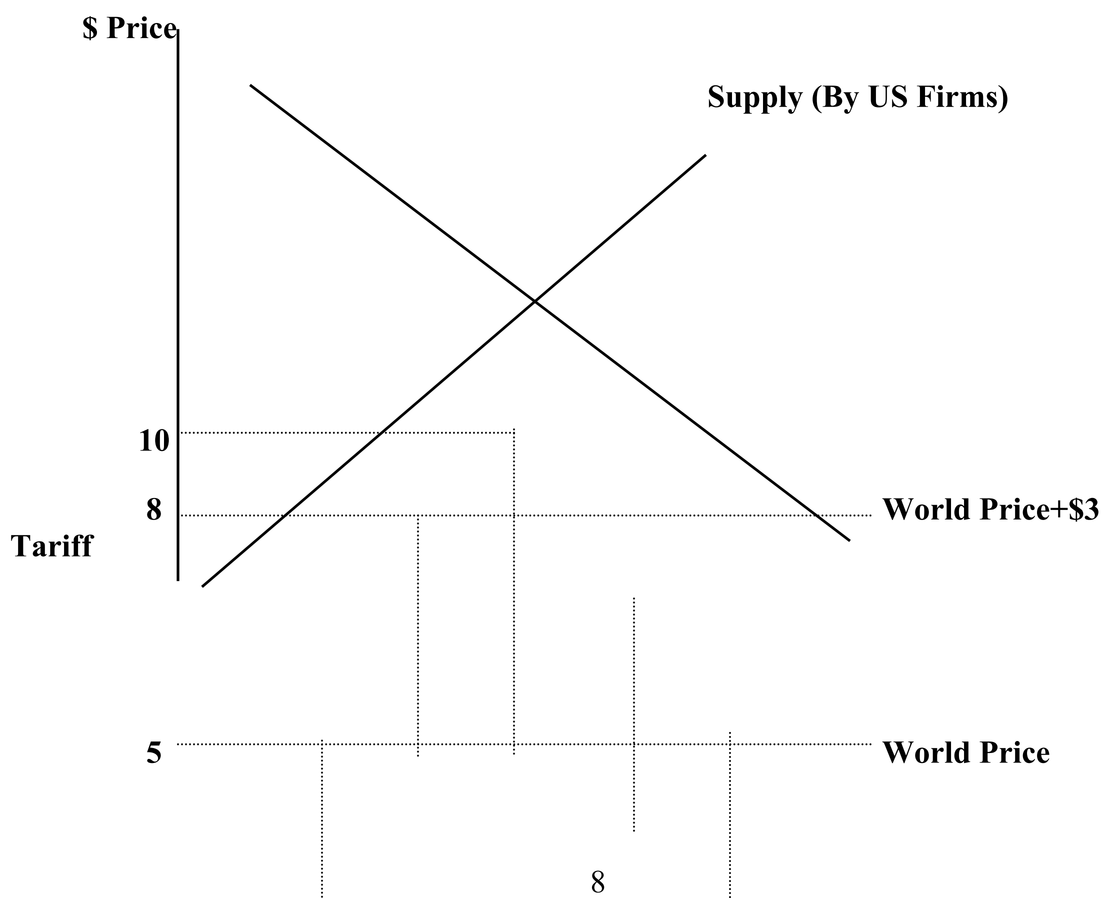
Part 3: The Theory of Protectionism: Tariffs and Quotas

Protection essentially takes one of three forms: tariffs, quotas, and non-tariff barriers. Tariffs are taxes levied on a commodity crossing an international border. Quotas are restrictions on the number of a certain good that can be imported. Non-tariff barriers include all kinds of subsidies and regulatory protection that doesn't count as either a tariff or a quota.

The basic motive for using tariffs is twofold: to protect domestic industry from import competition and to generate revenues for the government. For developing nations—such as China—tariffs afford developing "infant" industries the protection they need to mature. Moreover, tariffs are an important source of revenue for such countries—as they were for the United States until the early part of the 20th century—since, even if developing countries have income taxes in place (and can collect them), incomes are frequently not high enough to sustain government operations necessary for increasing economic growth. While tariffs are more likely to be about revenue and fostering newly developed industries in the developing world, for developed nations the argument for their use rests squarely on jobs.

VIDEO: The Revenue and Protective Effects of Tariffs

The effects within a given industry of a tariff include higher prices, more domestic production, fewer imports, tax revenue, and market inefficiencies because of the increase in higher cost domestic production and loss of consumer purchases caused by the higher market price. For example, consider the following economic market analysis:



Demand (In the US)

10 16 22 28 34 Market Quantity

In the absence of any trade with the rest of the world, this market would be in equilibrium where the supply of the product produced by US firms equals the demand for the product by US consumers – at a price of 10 and a quantity of 22. According to economic theory, this would be an efficient outcome because at $10 there are 22 buyers paying less than they are willing to pay (based on their demand curve) and 22 sellers being paid more than they are willing to accept (based on their supply curve). In other words, each of these 22 market transactions is transferring a product from someone who places a lower value on the product (the seller) to someone who places a higher value on the product (the buyer). And this is the fundamental argument in favor of market systems.

Now, let's consider what would happen in this market if the rest of the world, which could profitably sell this product for $5, were permitted into the US. Facing competition, domestic producers would be forced to lower their price to $5, making them only willing to sell 10 units and causing job losses. On the other hand, at a price of $5, there are 34 buyers who would willingly pay at least that, so they buy the 10 units domestic producers are willing to make and import the remaining 24. Theoretically, this outcome is more efficient than a market without trade for two reasons: First, at a lower price, there are more market transactions—which are beneficial to consumers—and second, the higher cost domestic production, which would have only been produced and sold at prices above $5 (units 10–22) are now replaced by lower cost—more efficiently produced—imports.

Indeed, free trade by almost any empirical account, is more efficient than no trade, and on average benefits consumers more that it harms producers. But the distribution of trade effects are very skewed: millions of consumers pay lower prices—and this adds up to a lot—but some workers lose their jobs. So while it is reasonable to favor trade on the grounds that the gains are bigger than the costs, neither can one ignore the devastating impact it has on an unfortunate few.

Now let's suppose that lobbying efforts by the workers and the domestic industry that is hurt from free trade are successful, and the government imposes a $3 per unit tariff on the import competition. In order to recover the cost of the paying the tariff, the rest of the world is forced to raise their price to $8 ($5 free trade price + $3 tariff = $8). This higher price has two main effects:

- domestic firms benefit because at a price of $8 they will be able to profitably increase production to 16 units (which will require the employment of more workers)

- domestic consumers lose because the price they pay goes up by $3 and the number of market transactions falls from 34 to 28 (which means that 6 consumers who would have benefited from buying the product at the free trade price are now left out)

Additionally, the government collects $36 in revenue from the tariff since each consumer is paying $3 more for each of the 12 units imported (28 demanded – 16 domestically supplied = 12 units imported). In the end analysis, whether protectionism is good or bad for you is really a matter of where you stand, realizing, of course, that on average the total costs to consumers almost always outweighs the total benefits to the workers and industry being protected.

VIDEO: Supply and Demand Analysis of Protectionism

And finally, outside of the industry receiving protectionism, tariffs have other, secondary effects which must also be considered. For example, fewer imports means fewer dollars in the hands of foreigners that can be used to buy home country exports. Tariffs on imports (such as steel or parts assemblies for cars, etc.) increase domestic production costs. In general, they also raise the cost of living, and they have a dampening effect on foreign GDP—which will tamp down their demand for goods of all kinds, including exports from the home country. For example, it is estimated that the steel tariffs mentioned above cost far more Americans their jobs in industries which relied on steel as an import than steel workers jobs were saved.

VIDEO: Non-industry Effects of Protectionism

It's important to keep in mind the general context in which the debate about tariffs takes place. The claim that imports cost jobs looks self-evidently true on the face of it, and so looks like a good case for tariffs. However, empirical evidence clearly suggests that relatively few jobs in the US economy as a whole are lost due to import competition. In a recent speech, Ben Bernanke, a member of the Board of Governors of the Federal Reserve, quoted an estimate that suggested that about 2% of total American job loss per year was due to trade. Moreover, tariffs often temporarily put off a day of reckoning that an inefficient industry ought to have faced long ago. Concern for displaced workers, in other words, need not lead to advocacy of tariffs.

WEBLINK: Ben Bernanke

Quotas

As mentioned above, quotas are limits on the quantity of a good that can be imported into a given country. In a static sense, quotas and tariffs have similar effects, except that tariffs provide tax revenue while quotas put more money per unit in the pocket of the foreign manufacturer. Both raise price, lower imports, help domestic producers at the expense of consumers, and cause market inefficiencies. Dynamically, however, quotas can be even more protectionist than tariffs—explaining why domestic industry favors them and the WTO rejects them. For example, if domestic demand goes up when a quota is in place, then the production gap has to be made up by domestic producers, which means even higher prices for consumers (and more profits for domestic producers). On the other hand, if a tariff is in place, then extra production can be provided through additional imports, which usually means that price goes up less quickly than with a quota in place.

VIDEO: Quotas Versus Tariffs

Part 4: The Theory of Protectionism: Other Types

There are many other non-tariff and non-quota kinds of protection. One obvious one—the subject of much debate—is subsidies. When any nation gives a subsidy to an industry, it lowers that industry's costs, and allows it to be more competitive on the world market. For example, it frequently happens that wealthy nations like the US and those in Europe subsidize farm production. This hurts developing countries—for the majority of whom raw agricultural materials represent their only source of comparative advantage. Both tradition and political power explain these subsidies: farming is thought to embody a valuable "way of life," and farmers also have strong political representation, especially in Europe.

For example, consider a subsidy that pays a flat sum per unit of production. If the going world price of wheat is $.20 per bushel, and the cost to farmers in the US is $.22 per bushel, then the developing countries have a cost advantage and will export wheat. Now, suppose the US government offers a subsidy of, say, $.05 per bushel to its wheat farmers, reducing their cost $.17 per bushel. Such a subsidy encourages farmers in the US to produce *more* wheat—which, when put on the world market, will drive world prices down, possibly to the point that they fall below the developing nations' production costs. It's possible then—and happens frequently—that such a subsidy to US farmers actually prices others out of the market, especially producers in developing countries. That's why subsidies draw attention and criticism from trading partners and the WTO.

AUDIO CLIP: NPR Audio: WTO: Agricultural Subsidies (9/16/2003)

http://www.npr.org/features/feature.php?wfId=1432861

AUDIO CLIP: Criticism of U.S. Agricultural Subsidies at WTO (6/16/2004)

http://www.npr.org/features/feature.php?wfId=1960385

These clips will be important to Discussion Questions #3.

A second example of a trade dispute over subsidies involves what the European Union perceives to be an illegal subsidy—according to WTO rules—based on a tax "loophole" in the US tax code that allows US exporting companies to set up "offshore" accounts which allows them to minimize their tax obligation to the US government. Recently the WTO has upheld the EU's charge against the US and given the EU permission to impose retaliatory measures against the US. To learn more about this debate listen to the following audio clip from NPR:

AUDIO CLIP: NPR Audio: EU Hits U.S. with Sanctions in Trade Dispute (3/1/2004)

http://www.npr.org/features/feature.php?wfId=1724878

Another kind of protection comes from government procurement policies. Such policies outline rules about the amount of non-home-country labor that can be used by government contractors. In effect, the government is giving a subsidy to home-country producers, since it isn't allowing foreign producers to compete for a given contract. We might expect such agreements for defense contractors or civil engineers working on government buildings, dams, or other infrastructure. But this frequently happens in other arenas as well. Have you ever seen a police officer in the US driving a Honda?

One of the most talked about examples of non-tariff protection is dumping, which is the logical and practical outcome of subsidies that encourage overproduction. The US, for example, subsidizes corn production to the tune of $10 billion each year. That subsidy encourages American farmers to overproduce corn, which is then "dumped" in Mexico, for example, driving down the price of corn, and driving many Mexican farmers out of business. Dumping in general is the practice of selling goods in a foreign nation for less than cost (or price) in the home market—which is what subsidies allow. On the other hand, the US has accused foreign furniture manufactures of dumping their product onto the US market in hopes of driving US industry out of business. For a detailed discussion of this topic, read the article in the next segment, written by Andrew Brod, Director of the Office of Business and Economic Research, UNCG.

Finally, "soft" protection also takes the form of regulations about packaging and content, and delays in the processing of goods. For example, if the German government insists that all personal audio systems imported into the country have a particular shape of headphones, and if the shape happens to be the one used by German manufacturers of headphones, they are using content regulations to protect their own producers. Governments use similar kinds of rules with respect to packaging and health and safety restrictions. Food products of all kinds are good examples of this. Food products are also frequently the target of protection through bureaucratic delays: if a foreign producer of cheese knows that 5% of whatever is shipped to the home market will go bad in the process of handling and paperwork, then the trade bureaucracy is offering a subsidy to domestic cheese producers.

VIDEO: Other Types of Protectionism

Global Trade Helps More Than It Hurts

by Andrew Brod

Greensboro News & Record, August 31, 2003

Times are tough in the textile and furniture industries. Foreign imports, most notably from China, are dominating segments in both industries. It seems that every time one opens the newspaper, another factory is being closed and its jobs moved overseas.

Both industries are working hard to cope with the brave new world of global competition. Some companies are going with the flow, by contracting with foreign producers or investing in foreign factories. It doesn't help the employment picture here as much as some would like, but so far it's helping those companies survive.

Other companies are fighting back and taking the foreign competition head-on. They're trying to improve their processes, serve customers better, and focus on high quality instead of low price. The companies that succeed in this will emerge as strong and efficient global competitors themselves.

And there's a third approach: Appealing to the U.S. government to raise trade barriers against foreign-made products. Such appeals make sense to many people who are scared to death by competition from low-wage countries they don't understand. But trade protectionism is bad for the American economy in the long run, and bad for a majority of Americans even in the short run.

The textile and furniture industries are traveling nearly parallel paths in their efforts to restrict trade, but the textile industry is a bit further along. It has successfully petitioned the federal government to consider imposing limits on imports of Chinese products in three specific categories: knit fabric, brassieres, and dressing gowns.

The basis of the appeal is the "China textile and apparel safeguard," a provision of the agreement that allowed China to join the World Trade Organization in late 2001. Any WTO member that believes Chinese textile imports are "threatening to impede the orderly development of trade" may act to limit those imports. The U.S. government has agreed to hear public comment on the petition, after which it will make its decision, possibly late this year.

For a claim to be valid under the China safeguard, the threat of imports must be due to "market disruption," which would seem to indicate fast-changing economic conditions. But the threat of low-wage foreign competition has been a reality in the textile and apparel industry for many years now. Can a process that's been going on for so long be thought of as a disruption, let alone a disorderly development of trade?

The furniture industry has yet to make its appeal for trade protection. But by October the industry intends to file an anti-dumping petition that focuses on wood bedroom furniture made in China.

Dumping is defined to occur when foreign-made products are sold here for less than in the producing country. The conventional wisdom is that foreign producers are willing to sell their products here below cost in hopes of driving out domestic producers. Once they succeed, the foreign producers are believed to be free to raise prices to exorbitant heights.

There are many problems with this folk theory. One big problem is that there's scant evidence that the above horror story has ever happened. If it were a reality, we'd have seen prices rise as our trade exposure increased. However, precisely the opposite has happened. International trade hasn't raised American consumer prices, it's lowered them. Trade has been a significant factor in keeping inflation in check for so long.

A second problem is that supporters of the anti-dumping petition seem to want to have it both ways. They tell us that it's hard to compete with China due to its low labor costs, but then they tell us that Chinese companies are selling furniture in America below cost. Well, which is it? Low prices due to cheap labor, or low prices due to dumping?

Third, what some see as dumping is actually just an example of a very common pricing practice. It's called "price discrimination," and it's not necessarily a bad thing. If two markets can be separated from each other, geographically or otherwise, there will generally be lower prices for the same product in the market in which there is more competition.

Airlines charge lower fares to vacation travelers than to business travelers, because vacation travelers have more options and that means airlines have to compete harder for their business. For similar reasons, electric utilities charge lower rates to residential users than to business users. And when foreign producers export to countries in which product competition is tougher than at home (which is often the case in developing economies like China's), they often charge lower prices abroad.

Do vacation travelers and residential electricity users mind having their purchases partly subsidized by businesses? Of course not. But for some reason, we're told that we should mind if the product is furniture and the subsidy is coming from overseas.

In any case, it's hard to know who "they" and "we" are. China's total exports have tripled since 1994, and according to the investment bank Morgan Stanley, fully 65 percent of that dramatic growth is due to subsidiaries of, and joint ventures with, multinational firms. Many American furniture makers fall into this category, including a number of the anti-dumping petitioners. Don't you just love irony?

Trade protectionists in both industries claim that they support free trade and are merely fighting "unfair trade" and ensuring a "level playing field." These are great sound bites, but it's very hard to determine who is and isn't playing fair in the trade game. And sometimes the cheaters aren't whom you'd expect.

It may be that China subsidizes the production of both textiles and furniture, as the trade protectionists claim. But the U.S. is hardly an innocent flower in this respect. For example, we subsidize our farmers quite aggressively. Along with France, we practically lead the world in this dubious category. We may not be allies in the war in Iraq, but the Franco-American alliance in farm subsidies has held firm, harming developing countries around the world by flooding them with artificially low-priced agricultural goods. If China is a kettle, then we're a pot.

Another of the "unfair trade" claims is that China is a non-market economy. One textile-industry leader even referred to it as a communist country. Such characterizations are years out of date. China has been moving rapidly toward a market economy since Deng Xiaoping started instituting economic reforms in the 1980s. To be sure, the government has retained its authoritarian grip on society, so it's certainly not a democracy. But neither is it a communist country. Some markets in China are more hurly-burly and competitive than in the U.S.

One measure of a market economy is the central government's share of national income. The bigger the share, the less room there is for markets to allocate goods and services freely. In socialist industrial economies like Sweden and Israel, the national government can account for well over a third of the economy (local governments add to that). The average share among developing countries is lower, and in China it's lower still, around 11 percent. In the U.S., it's about 20 percent. The upshot is that it's more accurate to describe China as a developing economy than as a non-market economy.

Yet another claim is that China manipulates its currency, the yuan, to promote exports unfairly. It's true that the yuan's value is fixed by the Chinese government, and most analysts agree that it's significantly undervalued. China manages this by buying huge quantities of dollars and dollar-dominated securities, thereby bidding up the value of the dollar relative to the yuan. However, those purchases also help finance the massive budget deficits the Bush administration is racking up. Without China's cheap-yuan policy, the budget situation in Washington could be much gloomier than it already is. Is that really what we want?

The efforts by the textile and furniture industries to restrict trade are understandable, but wrong-headed. They threaten to undermine the traditional leadership of the United States in promoting free trade around the world, and to harm American consumers in the name of protecting a relatively small segment of the economy.

It's hard to see through the plant closings, but on balance, international trade is a boon to the American economy. According to the Office of the U.S. Trade Representative, the North American Free Trade Agreement (NAFTA) and the creation of the WTO have raised the annual income of the average family of four by about $1,650. Multiplied across the entire population, this represents a net benefit of over $100 billion per year. And this is the opinion of a Bush appointee regarding Clinton-era trade policies.

However, abandoning calls for protectionism doesn't imply abandoning industries and regions that are harmed by international trade. Free trade doesn't mean government is free of responsibility for what happens in a market economy. Trade benefits society as a whole, but it also changes some lives and hurts some people, and in this case they're our friends and neighbors. The government needs to do what it can to retrain and compensate them, and help us all prepare for the future.

Here's the biggest problem with the current push to restrict trade: It won't work. The global economy is a complicated machine, and closing off one valve just causes another to blow. We might as well try to outlaw gravity. As an executive of a Chinese furniture company put it, "The furniture industry will just go to other countries, like Vietnam, Indonesia, or Malaysia. This is the trend of the global marketplace."

Part 5: Protection vs Free Trade—Who's on What Side?

Debates about free trade have many more than two points of view. Nonetheless, it can be useful to understand a perhaps oversimplified view of the positions on trade. In general, the political right has frequently championed free trade, while the left has viewed it with some skepticism. Nonetheless, political realities often dictate the opposite: while George W. Bush erected steel tariffs and signed mammoth farm subsidies into law, Bill Clinton pushed for and won passage of NAFTA. Likewise, Pat Buchanan, conservative Republican presidential candidate, has been an outspoken opponent of free trade. The point is that any taxonomy of positions on protection and free is good so long as things political don't change—which is not very long.

That said, it's relatively easy to find arguments for free trade. Most international economics textbooks used in the US would give such arguments. Some more specific and detailed arguments against protection can be found at the Cato Institute website (see Unit 1) or their symposium by author Douglas Irwin on his book *Free Trade Under Fire*, or at the American Enterprise Institute. Also, for a more moderate voice in support of free-trade, you might see the Institute for International Economics website. Skeptics of free trade include EPI, Dollars and Sense, and the AFL-CIO. As mentioned in Unit 1, for the most part, the difference between these views is not their assumptions, but their approach to market imperfections. While Cato scholars take the market as sacrosanct, EPI and IIE are more likely to view markets as generally helpful, but in need of governance at the margins.

WEBSITES: These websites are listed below:

Cato Institute

"Free Trade Under Fire"

American Enterprise Institute

American Enterprise Institute

Institute for International Economics

EPI

Dollars and Sense

AFL-CIO

Weblinks

During your reading of Unit 3, Parts 1–4, the following weblinks were presented. Read them now if you have not already done so.

NPR Audio: WTO Panel Rules U.S. Steel Tariffs Illegal (11/11/2003)
http://www.npr.org/features/feature.php?wfId=1501551

NPR Audio: U.S. Steel Tariffs Poised to End (12/1/2003)
http://www.npr.org/features/feature.php?wfId=1528224

NPR Audio: Steel Industry Faces Economic Competition (12/01/2003)
http://www.npr.org/features/feature.php?wfId=1528226

NPR Audio: Steelworkers React to Tariffs' Removal (12/04/2004)
http://www.npr.org/features/feature.php?wfId=1532755

NPR Audio: U.S. Wants Europe to Lift Ban on Biotech Food (5/14/2003)
http://discover.npr.org/features/feature.jhtml?wfId=1262971

NPR Audio: The Marketplace Report: Modified Foods Ban (9/10/2003)
http://www.npr.org/features/feature.php?wfId=1427093

Ben Bernanke

NPR Audio: WTO: Agricultural Subsidies (9/16/2003)
http://www.npr.org/features/feature.php?wfId=1432861

NPR Audio: Criticism of U.S. Agricultural Subsidies at WTO (6/16/2004)
http://www.npr.org/features/feature.php?wfId=1960385

NPR Audio: EU Hits U.S. with Sanctions in Trade Dispute (3/1/2004)
http://www.npr.org/features/feature.php?wfId=1724878

Cato Institute

"Free Trade Under Fire"

American Enterprise Institute

Institute for International Economics

EPI

Dollars and Sense

AFL-CIO