INTERNATIONAL ECONOMIC POLICY

64. Trade

Congress should

- recognize that the relative openness of American markets is an important source of our economic vitality and that remaining trade barriers are a drag on growth and prosperity;
- move the focus of U.S. trade policy away from ''reciprocity'' and ''level playing fields'' toward commitment here and abroad to free-trade principles;
- take unilateral action to repeal remaining protectionist policies;
- reform U.S. antidumping law to limit abuses and conform with U.S. obligations within the World Trade Organization;
- enact implementing legislation for market-opening trade agreements;
- maintain support for the WTO as a body for negotiating market-opening agreements and settling disputes;
- avoid using trade deficits and concerns about employment levels as excuses for imposing trade restrictions; and
- employ trade expansion, not trade sanctions, as a tool of U.S. foreign policy.

Free Trade Means Free Markets

Its opponents like to portray free trade as an ivory-tower theory, but in fact the case for knocking down trade barriers rests on common sense. It is now widely recognized that free markets are indispensable to our prosperity: when people are free to buy, sell, and invest with each other as they choose, they are able to achieve far more than when governments attempt to control economic decisions. Given that fact, isn't it obvious that free markets work even better when we widen the circle of people with whom we can buy, sell, and invest? Free trade is nothing more than

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the extension of free markets across political boundaries. The benefits of free trade are the benefits of *larger* free markets: by multiplying our potential business partners, we multiply the opportunities for wealth creation.

From this perspective, it becomes clear that Americans gain from open U.S. markets even when other countries' markets are relatively closed. The fact that people in other countries are not as free as they should be is no reason to restrict the freedom of Americans. When goods, services, and capital can flow over U.S. borders without interference, Americans are able to take full advantage of the opportunities of the international marketplace. They can buy the best and cheapest goods and services the world has to offer; they can sell to the most promising markets; they can choose among the best investment opportunities; and they can tap into the worldwide pool of capital. Study after study confirms that nations that are more open to the global economy grow faster and achieve higher incomes than those that are relatively closed.

Unfortunately, supporters of open markets seldom put their case in those straightforward terms. Instead, trade liberalization in this country is identified almost exclusively with international negotiations in which the removal of U.S. trade barriers is seen as a ''concession'' contingent upon the removal of barriers abroad. Such negotiations convey the impression that exports are the primary benefit that accrues from international trade and that open markets at home are the price we pay for greater export opportunities. That impression is misleading—and ultimately harmful to prospects for continued liberalization.

The idea that exports are good and imports are harmful is the essence of the mercantilist fallacy that lies at the root of most protectionist thinking. That fallacy turns truth on its head: imports are in fact the primary benefit of trade. Imports give us goods that are cheaper or better than those we can produce ourselves; exports, which represent production that Americans do not get to consume, are actually the price we pay for the imports we enjoy. To the extent that free traders perpetuate the mercantilist fallacy by endorsing the dogmas of ''reciprocity'' and ''level playing fields,'' they are helping to foster a political culture that is hostile to open markets.

Opinion polls show that many Americans believe that U.S. openness to the rest of the world is destroying jobs and eroding living standards. That such ''globalphobia'' could be so widespread demonstrates that free traders are doing something wrong. To combat the current intellectual confusion, supporters of trade liberalization should return to their free-

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market roots. They need to meet mercantilist misconceptions head-on and to make the case that free trade is its own reward.

Alternatives to Reciprocity

Because free trade is first and foremost in our own national interest, the United States should not deny itself the benefits of open markets just because other countries hold on to self-damaging policies. Free traders should expand beyond their traditionally exclusive reliance on negotiated liberalization and launch a campaign for the unilateral reduction or outright elimination of U.S. trade barriers—including the antidumping law, still-high tariffs on many products, import restrictions linked to agricultural price support programs, the Jones Act ban on foreign shipping between U.S. ports, the similar denial of cabotage rights to foreign airlines, and foreign ownership limits for air transport and broadcasting.

Top 12 Most Costly U.S. Trade Barriers

Quota, tariff, and licensing barriers to imported

- Textiles and apparel
- Domestic maritime transport (Jones Act)
- Sugar
- Footwear and leather products
- Tobacco and tobacco products
- Canned tuna
- Beef
- Watches, clocks, watch cases and parts
- Ball and roller bearings
- Ceramic wall and floor tile
- Dairy products
- Table and kitchenware

SOURCE: U.S. International Trade Commission.

Advocating unilateral reform would enable free traders to frame the trade debate in terms that give them the natural advantage. Instead of always defending free trade, they could attack its alternative: protectionism in actual practice. The beneficiaries of protection would be forced to explain why they deserve their special privileges and why the welfare of

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other American businesses, workers, and consumers should be sacrificed on their account. The U.S. sugar protection program, for example, forces domestic consumers to pay triple the world price for sugar and costs American sugar-using industries and consumers an estimated $1.9 billion a year. Meanwhile, removal of quotas and tariffs on imported textiles and apparel would result in a welfare gain to the U.S. economy of $11.8 billion, according to the U.S. International Trade Commission.

Free traders need to reclaim their populist roots. Free trade benefits American families by injecting greater competition into the marketplace, leading to lower prices, wider choice, and better quality. Protectionism is especially tough on the poor: America's highest remaining trade barriers are aimed at products—such as shoes, clothing, and food—that are disproportionately consumed by poor people at home and produced by poor people abroad. A study by the Progressive Policy Institute found that a single mother of two earning about $20,000 a year pays a much higher effective tariff rate on the goods her family consumes than is paid by a single executive earning six figures.

Unilateral U.S. reforms would do more to encourage liberalization abroad than any trade negotiations ever could. The most sweeping and dramatic moves toward freer trade in recent years—in countries as diverse as Australia, New Zealand, Chile, Mexico, China, and India—have occurred not at the bargaining table but unilaterally. The leaders of those countries finally realized that isolation from the world economy was a recipe for economic stagnation, and therefore they sought to emulate the relatively open-market policies of more prosperous countries. History shows, therefore, that the most effective form of international economic leadership is leadership by example.

Negotiating for Free Trade

Still, pursuing unilateral reform would not mean an end to trade negotiations. International agreements can facilitate the liberalization process by recruiting export interests to support free trade at home; also, such agreements provide a useful institutional constraint against protectionist backsliding. But a new U.S. negotiating posture is needed, one that replaces demands for reciprocity with commitment to free-trade principles.

Instead of seeking to ''win'' at the negotiating table by ''getting'' more than it ''gives,'' the United States could define its key liberalization objectives—for example, global tariff reductions, reforms of antidumping laws, rules on treatment of foreign investment, rules against protectionist

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misuse of health and safety standards, and so on—and offer to elevate its own unilaterally adopted free-trade policies into binding international commitments, provided that some ''critical mass'' of other countries agreed to exceed a defined minimum threshold of liberalization.

The United States does not need protectionist policies as ''bargaining chips'' to exert significant leverage. For example, other countries signed on to the 1997 multilateral agreements on telecommunications and financial services even though the only major U.S. ''concession'' was to lock in current levels of openness. Also, U.S. involvement in international agreements is desirable apart from any consideration of ''concessions,'' since U.S. participation lends legitimacy to an agreement, thereby increasing other countries' confidence in the integrity of each others' commitments.

The same free-trade agenda should animate bilateral or regional trade negotiations. Subsequent free-trade agreements can open markets at home and abroad to more import competition, encourage cross-border integration of industries, and reward economic and political reform in other countries. Although less economically important than a comprehensive WTO agreement, regional and bilateral deals can mark important steps toward the goal of global free trade.

To maximize the benefits of regional and bilateral free-trade agreements, the United States should seek agreements with countries that can provide significant import competition in our domestic market and export opportunities abroad, or countries that are reform leaders in regions of the world where models of successful reform are most needed. U.S. negotiators should avoid the political temptation to exclude or phase in liberalization of the very products or sectors that most desperately need import competition.

Congress should use its constitutional authority over trade policy to facilitate genuine market openings, not to erect roadblocks. Many members of Congress have strongly urged the inclusion of ''enforceable'' labor and environmental standards in any new trade agreements. The whole purpose of trade negotiations, however, is to reduce governmental interference in cross-border flows of goods and services; international regulatory mandates on labor and environmental matters would threaten to increase government interference in those flows and thus subvert the basic mission of negotiations. Meanwhile, labor and environmental standards are implacably opposed by developing countries, and a U.S. negotiating position that insisted upon such standards could end up dooming negotiations to fail.

The U.S. trade remedy laws—the antidumping, countervailing duty, and Section 201 ''safeguard'' laws—and their counterparts in other coun-

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tries are badly in need of reform. In particular, the antidumping law, which purports to focus on ''unfair trade,'' frequently penalizes healthy foreign competition for business practices routinely engaged in by American companies. While the U.S. antidumping law victimizes American import-using industries and consumers, foreign copycat laws now target U.S. exporters with depressing frequency. Indeed, the United States became one of the leading victims of worldwide antidumping actions during the second half of the 1990s.

The prospects for reform here and abroad, however, are dimmed by vehement congressional opposition to any trade negotiations that might ''weaken'' U.S. trade laws. That opposition threatens, not just to block improvements in trade laws, but to prevent market-opening agreements more generally. Many of our trade partners are demanding changes to antidumping rules as a condition of any new agreements. If congressional pressure forces the administration into adopting an obstructionist position on antidumping, the United States could ultimately pay a grievously heavy price in lost opportunities to open markets around the world.

The World Trade Organization

The World Trade Organization is at present the primary institutional support for an open world trading order. In addition to serving as a forum for ongoing trade negotiations, the WTO and its dispute settlement procedures uphold a limited but real rule of law in international commerce. The WTO strongly advances the U.S. national interest in free markets here and abroad and therefore deserves strong U.S. support.

Congress should support the ongoing Doha Development Round of WTO negotiations. If successfully concluded, those talks could open vast new markets for American exports, raise global welfare by hundreds of billions of dollars, and help protect American consumers from trade-distorting barriers here at home.

Complaints that the WTO impinges on U.S. sovereignty are groundless. The WTO cannot overturn U.S. laws; at most, it can declare that U.S. laws are inconsistent with international agreements we have already signed and ratified. The WTO wields no power of enforcement. The WTO itself has no authority or power to levy fines, impose sanctions, change tariff rates, or modify domestic laws in any way to bring about compliance. If a member government refuses to comply with rules it previously agreed to follow, all the WTO can do is approve a request by the complaining member to impose sanctions—a ''power'' that member governments have

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always been able to wield against each other. By establishing procedures for the use of sanctions, the WTO's dispute settlement understanding actually makes their use less likely. So whether we honor our obligations as a member of the WTO is ultimately up to us.

But honor them we should. The principles of market access and nondiscrimination incorporated in WTO agreements are ones that ought to be reflected in U.S. policy. When U.S. laws violate those principles, they ought to be changed. It is a mistake to complain simply because the United States ''loses'' a case in the WTO; when the dispute settlement process leads the U.S. government to reform protectionist policies, that is a victory, not a defeat, for the American people. Furthermore, by heeding ''adverse'' WTO decisions, the United States sets an example for the rest of the world. We stand to gain when other countries follow the WTO's free-trade rules. Consequently, we have a large stake in the legitimacy and credibility of the dispute settlement process, which cannot be sustained if we selectively disregard WTO rulings.

Congress should show its support for the WTO process by passing legislation to implement all outstanding adverse WTO rulings as soon as possible. In particular, Congress should move quickly to comply with a large and growing number of outstanding rulings against various aspects of U.S. trade laws. To the extent that legislation is needed to implement those rulings, Congress should move immediately to make the necessary changes to U.S. law.

Trade and the U.S. Economy

Imports benefit the U.S. economy by injecting more competition into domestic markets, delivering lower prices, better quality, and more choice to American families. Imports benefit American producers as well by lowering the cost of raw materials, intermediate parts, and capital equipment, making U.S. companies more competitive in global markets.

Anxieties about job losses and trade are misplaced. Trade is not about more or fewer jobs but about better jobs. Like technology itself, trade changes the mix of jobs by allowing American workers to shift into sectors where we have greater advantages as a nation. Of course, not everyone benefits from expanding trade. Trade does bring new competitive pressure to bear on certain domestic industries. It can cause those industries to shrink and lay off workers. The adjustment can be painful, but those workers who lose their jobs because of trade are not alone.

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The number of jobs lost each year because of import competition is quite small in an economy that, as of 2004, employed 138 million workers. Within that labor force, ''job churn'' is a fact of life in a healthy, dynamic economy. According to the Bureau of Labor Statistics, jobs lost to imports and offshoring represent only 2 percent of annual job losses in the United States. New technology, domestic competition, and changing consumer demand displace far more workers than trade. To impose new trade barriers to supposedly ''save'' jobs would be as foolish as banning new technologies or restraining domestic competition.

America's trade deficit is not an economic problem. It is the benign consequence of a persistent surplus of foreign capital flowing into the United States. That additional capital has helped to make U.S. workers more productive, raising living standards above what they would be without it and building the foundation for future growth.

The underlying cause of the U.S. trade deficit is the fact that domestic savings in the United States are insufficient to fund all the available domestic investment opportunities. Any savings gap is filled by a net inflow of foreign investment. Those foreign funds allow Americans to buy more than we sell in the international market for goods and services, resulting in a trade deficit. As long as the pool of domestic savings available for investment is smaller than the actual level of investment, the United States will run a trade deficit.

The only real sense in which the trade deficit is a threat to the U.S. economy is its potential effect on public policy. Persistent worries about the trade deficit could prompt policymakers to implement a ''cure'' for the trade deficit, such as higher tariff barriers, that itself could impose serious damage on the economy. Members of Congress should reject the idea of ''balanced trade'' as a policy goal. The best policy response would be to ignore the U.S. trade deficit and concentrate on maintaining a strong and open domestic economy that welcomes trade and foreign investment.

Export Barriers, Trade Sanctions, and U.S. Foreign Policy

Although we complain about other countries' barriers to our exports, the fact is that many barriers are homegrown. In particular, America's export control policies remain detached from the realities of the global marketplace. U.S. companies should be allowed to sell technologies that are being sold freely elsewhere in the world by their foreign competitors and the sale of which fails to present a clear danger to U.S. citizens or

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world peace. That is not the case today for many products, and much bureaucratic wrangling is needed before others can be exported.

Sales and investments abroad by U.S. companies are also hindered by ill-considered foreign policy trade sanctions against Cuba, Burma, and other countries. The Cuban embargo is discussed in Chapter 63. It should be noted here, though, that trade sanctions rarely accomplish their foreign policy objectives. Instead, they end up hurting the very people they are designed to help—the unfortunate subjects of despotic regimes. Absent compelling national security considerations, trade sanctions are almost always a bad idea.

Trade and investment, on the other hand, can improve the lot of despotism's victims while sowing the seeds of political change. As trade and globalization have spread to more and more countries in the last 30 years, so too have democracy and political and civil freedoms. In particular, the most economically open countries today are more than three times as likely to enjoy full political and civil freedoms as those that are relatively closed. Those that are closed are nine times more likely to completely suppress civil and political freedoms than are those that are open. Nations that have followed a path of trade reform in recent decades by progressively opening themselves to the global economy are significantly more likely to have expanded their citizens' political and civil freedoms.

The powerful connection between economic openness and political and civil freedom provides yet another argument for pursuing an expansion of global trade. In the Middle East, China, Cuba, Central America, and other regions, free trade can buttress U.S. foreign policy by tilling foreign soil for the spread of democracy and human rights.

Suggested Readings

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—Prepared by Brink Lindsey and Daniel Griswold

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