



Thinking About International Trade and Trade Policy



ThinkTank Tuesdays: Wine, Water, and Policy Whimsy
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National Economic Education Delegation

- **Vision**

- One day, the public discussion of policy issues will be grounded in an accurate perception of the underlying economic principles and data.

- **Mission**

- NEED unites the skills and knowledge of a vast network of professional economists to promote understanding of the economics of policy issues in the United States

- **NEED Presentations**

- Are **nonpartisan** and intended to reflect the consensus of the economics profession



Credits and Disclaimer

- **This slide deck was authored by:**
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 - Jon Haveman, NEED
- **Disclaimer**
 - NEED presentations are designed to be nonpartisan
 - It is, however, inevitable that the presenter will be asked for and will provide their own views.
 - Such views are those of the presenter and not necessarily those of the National Economic Education Delegation (NEED).

What Do We Trade?

• Exports

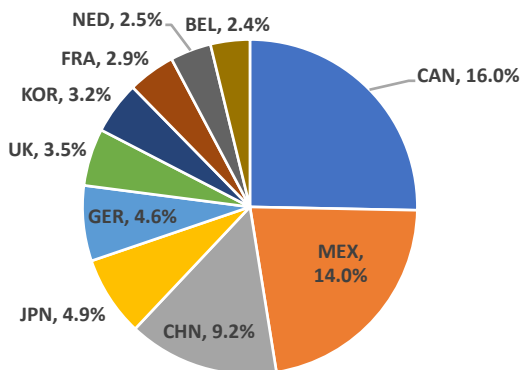
Industry	\$ Billions	Share
Machinery incl computers	201.7	13.0%
Electrical machinery	174.2	11.3%
Mineral fuels including oil	138.0	8.9%
Aircraft, spacecraft	131.2	8.5%
Vehicles	130.1	8.4%
Total	1,552.0	

• Imports

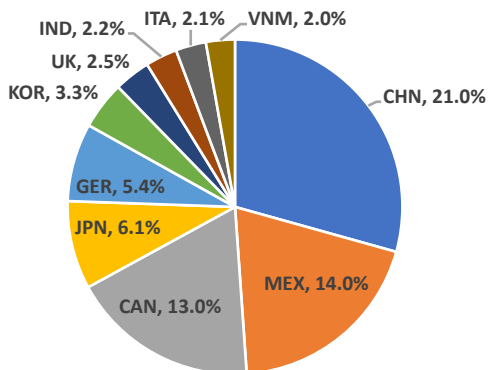
Industry	\$ Billions	Share
Electrical machinery	356.8	14.8%
Machinery incl computers	349.1	14.5%
Vehicles	294.6	12.2%
Mineral fuels including oil	204.2	8.5%
Pharmaceuticals	96.4	4.0%
Total	2,409.0	

Top US trade partners (goods, 2016)

• Top 10 US export destinations

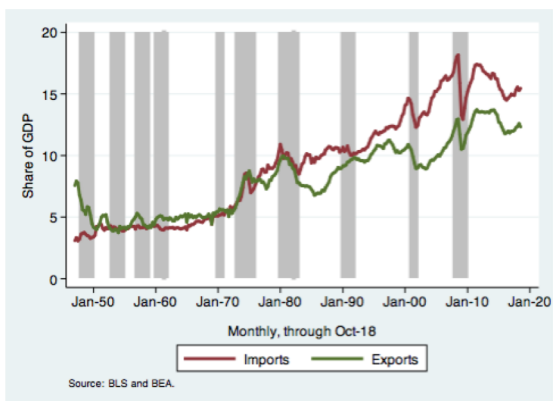


• Top 10 US import sources

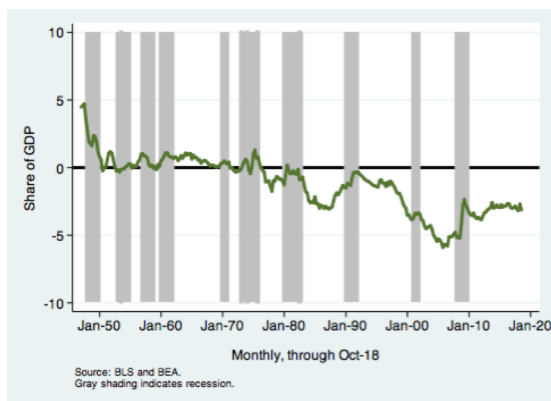


Importance of US trade

• US trade as % of GDP

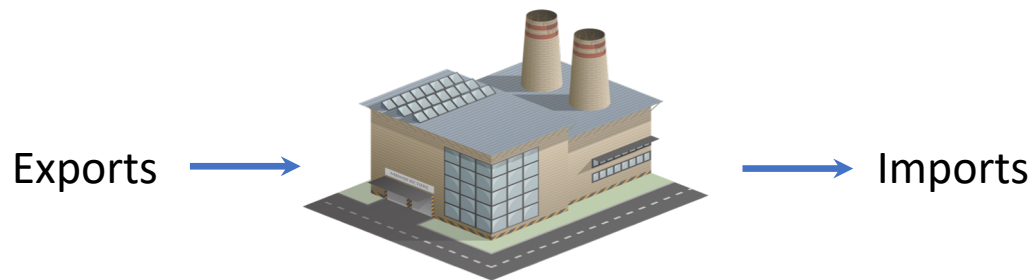


• US trade balance as % of GDP



How to Think About Imports

- Think about international trade as the introduction of a new technology.



- Do we think of new technologies as a problem?

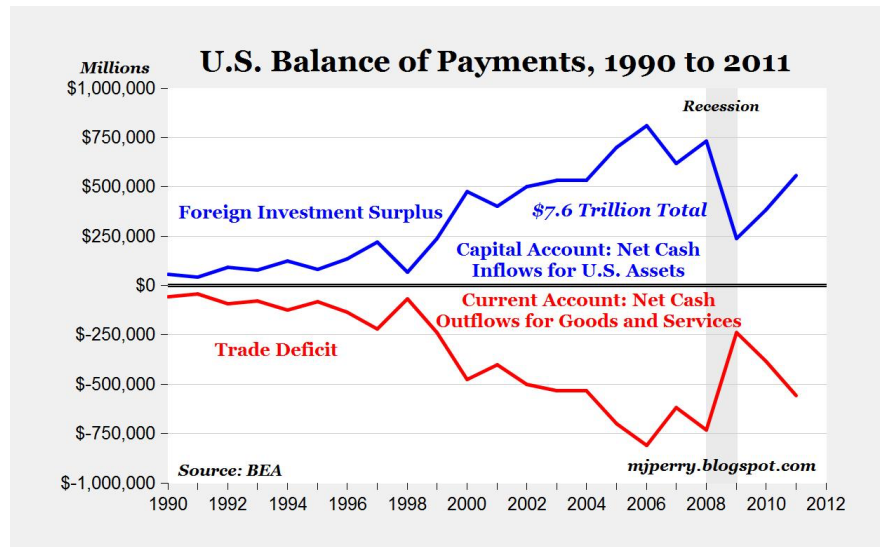


How to Think About the Trade Deficit

- A trade deficit is when the **VALUE** of imports is greater than the **VALUE** of exports.
- Why does this happen?
- **International transactions include:**
 - Imports and exports of goods and services
 - ALSO: imports and exports of assets (investments)
 - Current Account
 - Capital Account



Trade and Investment Flows Balance Out



Trade contributes to growth in many ways

- Increases the varieties of inputs for our production
- Brings in cheaper goods, which may allow for increased savings
- Allocates production across countries efficiently so that countries can specialize in what they are best at producing
- Trade also facilitates transportation, further lowering costs
- AND trade makes consumers better off through lowering prices of goods people like



Why is the public turning against trade?

- **Gains from trade are very large for the economy, BUT**
 - Not always noticeable by consumers. Why are prices lower at WalMart?
 - Not always that large per consumer: consumers might save \$50/year on some imported goods
 - For 300 million consumers, \$50/year would be \$15 billion per year savings to the country!
- **Costs of trade are very high for some workers and groups, and these costs have not been sufficiently appreciated or addressed by policymakers (or economists!)**



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Costs of Trade

- We have known for almost 80 years that trade with low-wage countries will lower the earnings of low-wage workers as a group in the U.S.A. (Stolper-Samuelson 1941)
- Perhaps more importantly, however, is that the adjustment costs, or what some call transition costs, are much larger than previously thought. People do not like to move, and getting laid off can be very traumatic.
- Recent economics studies have estimated the costs of trade across many different groups.
 - Inequality
 - Adjustment costs



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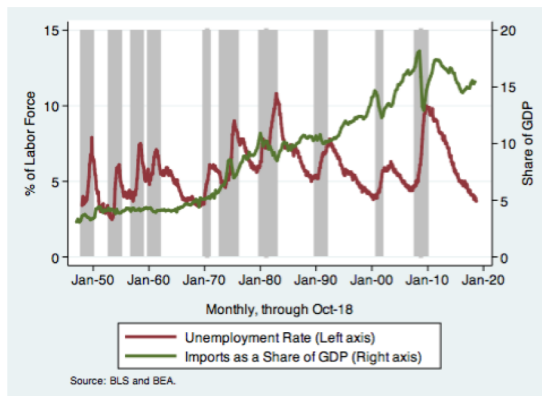
Common Misperceptions about Trade



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Misperception 1: Trade Causes Unemployment

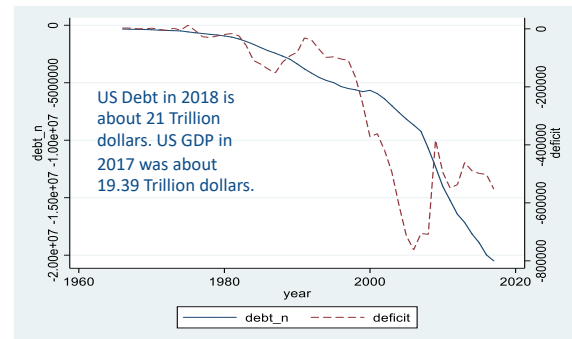
- Import competition may contribute to factories closing and job loss, but there are many other factors that also contribute to job loss.
- The national unemployment rate is driven by business cycles, and not by trade.
- Over the same period shown in the graph, trade has been rising.



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Myth 2: Trade deficits are driven by trade agreements and tariffs can “fix” them

- Trade deficits are driven by imbalances in the capital account, which is the amount we borrow from other countries.
- Since 1960, the U.S. trade deficit has followed the growth of the U.S. federal debt.
- That is, U.S. borrowing from other countries drives our trade deficit.
- Tariffs can NOT solve this problem!



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The Budget Deficit-Trade Balance Link

- **When the U.S. government spends more than it receives in taxes, the shortfall is called the U.S. Federal Budget Deficit**
- **The shortfall must be paid somehow. There are three policy options**
 - Increasing Taxes and/or cutting spending
 - o Both are politically unpopular
 - Printing money, which leads to inflation
 - Borrowing money
 - o U.S. Citizens and/or Foreign Citizens
 - o May “crowd out” domestic investment
 - o Increases the demand for dollars
 - o Rising demand for dollars makes imports cheaper and exports more expensive
 - o Result: Larger trade deficits!



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Policy Solutions



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Tariffs

- **Tariffs temporarily reduce imports on particular goods**
- **Tariffs raise prices**
 - Final goods (consumers)
 - Intermediate goods (producers who use imported inputs)
 - Rising prices distort consumption and production decisions
- **Tariffs invite retaliation, lowering demand for our exports**
- **In the long run, the exchange rate adjusts to offset the tariffs because of the effects of borrowing: Tariffs, therefore, cannot correct a trade deficit**
- **Tariffs lower overall welfare, while generating very large gains for small groups (e.g. A cost of 100 to many for a gain of 80 for a few).**
- **Tariffs are generally considered to be an inefficient way to help those people who are hurt by trade**



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Directed Support: Adjustment Costs

- **The most efficient way to help those hurt by trade is through direct payments**
- **Trade Adjustment Assistance (TAA) is an example of an attempt at this principle**
 - TAA includes some retraining funds and extended unemployment benefits
 - Not generally considered to be very successful
 - Underfunded
 - Hard to determine who is hurt by trade and not other factors
- **Larger direct payments would be most effective and efficient**



**TRADE
ADJUSTMENT
ASSISTANCE
FOR FIRMS**



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Balanced Budgets

- Reducing federal borrowing would reduce pressure on trade deficits.
- Size of debt – nearly 21 trillion in 2018 – means that some combination of cutting spending and rising taxes would be necessary.
- Reducing the debt would also reduce the large share of the federal budget that is directed towards interest payments and free up money for other things.
- Reducing the debt also increases our economic security because it could reduce foreign debt exposure.



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Conclusions

- Trade and growth are positively related
- Gains from trade can be widespread (lower prices for consumers)
- Losses from trade can be highly concentrated
- Tariffs reduce trade overall, thus imposing widespread losses to both producers (who use imported inputs) and consumers (who buy lower-priced imported goods)
- More direct policies can be more efficient and save gains from trade



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Recent U.S. Trade Policy Initiatives/Issues

- Trade staff
- TPP
- NAFTA
- Other FTAs
- Factory location
- Border tax adjustment
- Exchange rates
- WTO
- Executive orders
- China



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Let's Talk About China

- **US: Oct 27, 2018: solar panels**
 - Into effect on 1/22/18
 - \$8.5 billion of solar panels
- **US: Nov 21, 2017: washing machines**
 - Into effect on 1/22/18
 - \$1.7 B of washing machines
- **China: Feb 5, 2018: sorghum**
 - Into effect on 4/17/18
 - \$1 billion (178.6% tariff)
- **May 18, 2018: Negotiations end tariffs on Sorghum**
- **China: Aug 14, 2018: WTO dispute against US solar panel tariffs**
- **Tariff dispute accelerates...**



How to Think About the Trade War

- **Will it stimulate a solution to the underlying problems?**
 - Intellectual property theft.
 - Trade deficit
- **Will it help low skilled workers? Those most affected by imports.**
 - Possibly, but at what cost?
- **Will it foster greater cooperation between the United States and China?**
 - Future trade agreements.
 - Future trade disputes
 - Other international issues
- **What about other economic implications?**

