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Thinking About International Trade and Trade Policy

Tristan Bodle's Econ Class, Drake High School
November 16, 2018

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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

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What is Globalization?

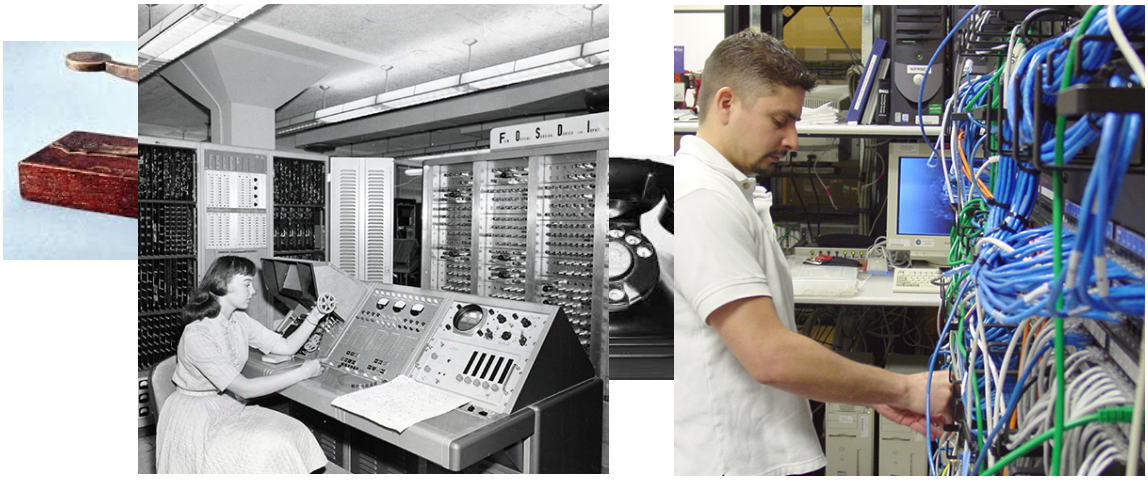
- **The growing interdependence of the world's:**
  - Economies
  - Cultures
  - Populations
- **Brought about by cross-border flows of:**
  - Goods and services
  - Technology
  - Investment
  - People
  - Information

What Drives Globalization?

- Transportation
- Technology
- International Cooperation

Transportation

Technology



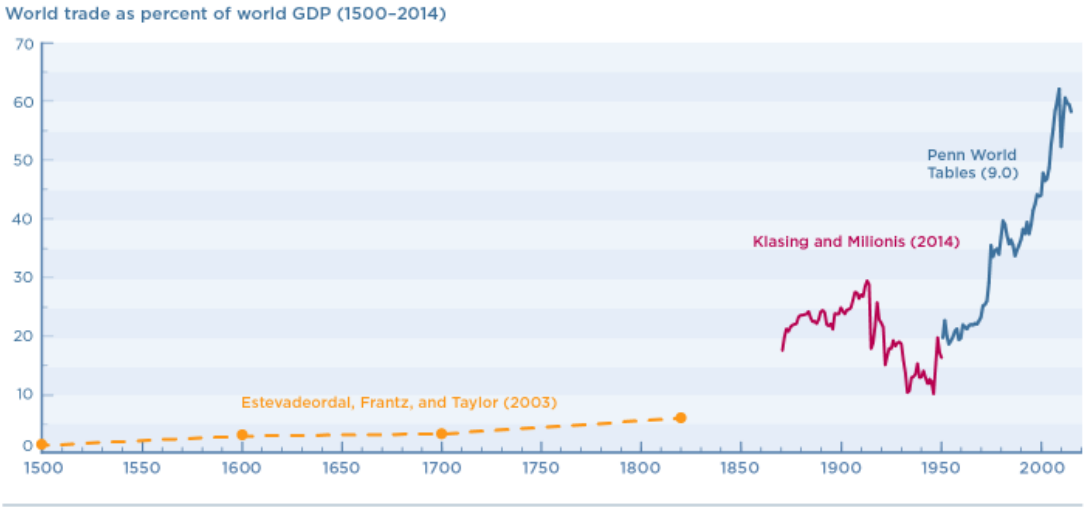
International Cooperation

1995

World Trade Organization (WTO)

The modern trading system governed by rules is established, replacing the GATT.

Trade has skyrocketed in the past century



Note: This chart displays data from three sources. Data from 1500 to 1820 is the average of the upper and lower bound and only includes the years 1500, 1600, 1700, and 1820. Data not available from 1821-1869.

Sources: See chart, "Globalization over 5 centuries," at https://ourworldindata.org/trade-and-globalization for full citations.

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International Cooperation – Ending?

2017 — 2018

President Donald Trump Repudiates Trading System

Trump withdraws from the Trans-Pacific Partnership (TPP), threatens to abandon NAFTA (then later negotiates a preliminary deal that adds new restrictions), and criticizes WTO rules as unfair to the United States. His administration imposes tariffs against China and US allies, which escalates into a tit-for-tat trade war.

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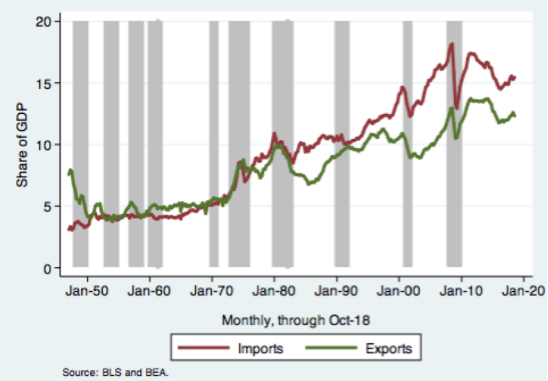
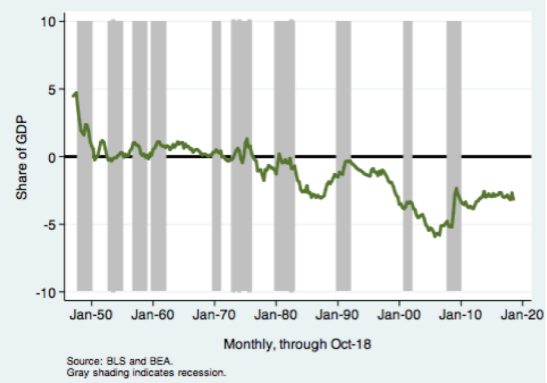
Importance of US trade

- US trade as % of GDP



- US trade balance as % of GDP



What do we Export? ($1.6 Trillion)

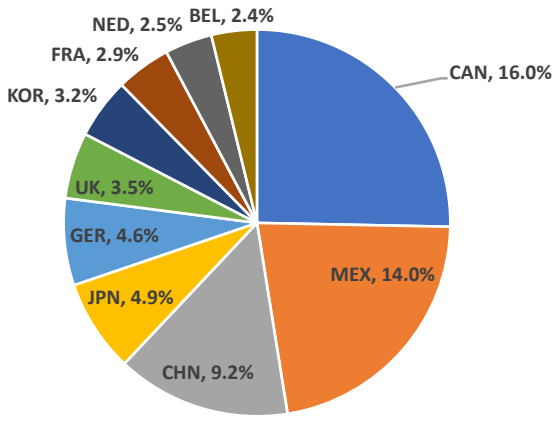
Rank	US Export Product	2017 Value (US$)	Change
1	Processed petroleum oils	$77.8 billion	+25.6%
2	Cars	$53.6 billion	-0.5%
3	Automobile parts/accessories	$44.9 billion	+4.5%
4	Integrated circuits/microassemblies	$38.1 billion	+9.1%
5	Mobile phones, other phone system devices	$34 billion	+0.5%
6	Electro-medical equipment (e.g. xrays)	$26.5 billion	+0.2%
7	Computers, optical readers	$25.3 billion	+4.2%
8	Petroleum gases	$22.3 billion	+67.8%
9	Crude oil	$21.8 billion	+131.6%
10	Soya beans	$21.7 billion	-5.3%

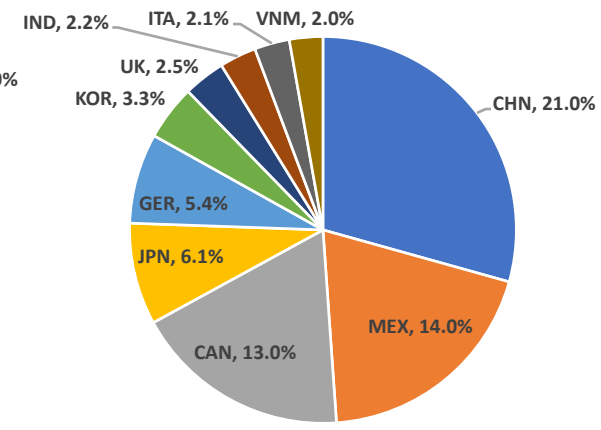
What do we Import? ($2.4 Trillion)

Rank	US Import Product	2017 Value (US$)	Change
1	Cars	$179.6 billion	+3.9%
2	Crude oil	$139.1 billion	+23.4%
3	Phone system devices including smartphones	$113.1 billion	+5.4%
4	Computers, optical readers	$85 billion	+6.4%
5	Automobile parts/accessories	$66.6 billion	-0.3%
6	Medication mixes in dosage	$65 billion	-5.9%
7	Processed petroleum oils	$48 billion	+10.9%
8	Integrated circuits/microassemblies	$33.5 billion	+8%
9	Trucks	$26.5 billion	+8.4%
10	Blood fractions (including antisera)	$26 billion	+27.5%

Top US Trade Partners (Goods, 2016)

- Top 10 US export destinations
- Top 10 US import sources





Why Do Countries Trade?

- **Competition**
- **Varieties**
- **Efficiency**

Why Might Efficiency Differ Across Countries?

- **Labor**
  - Skilled or unskilled
- **Technology**
  - Some countries have firms that produce some goods well
  - Other countries have firms that produce other goods well
- **Environment**
  - Cold/Warm Wet/Dry Sunny/Cloudy
- **Land**
  - Rocky, soil, fertile, barren
  - Tundra, desert, grasslands, forest

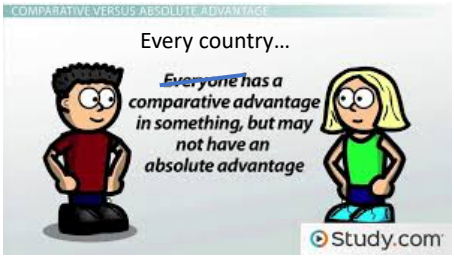
Comparative Advantage – Key Notion

- **Two kinds of advantage: absolute and relative**
- **E.g., Babe Ruth vs Madison Bumgarner**
  - Babe Ruth: ERA – 2 Batting average - .350
  - Madison Bumgarner ERA – 3 Batting average - .185
- **Babe is better at both**
  - *Absolute advantage*
- **If only one can bat and one can pitch, who does what?**
  - *Relative advantage*

Relative Advantage

- **Babe has an absolute advantage in both activities**
  - He is better at both pitching and hitting
- **Is he RELATIVELY better at one than the other?**
  - Pitching: Babe is 33% better (era of 2 vs 3)
  - Hitting: Babe is 100% better (.350 vs .185)
- **Babe has a relative advantage in hitting**
  - So: Babe should hit and Madison should pitch
- **Therefore, Babe has a COMPARARTIVE ADVANTAGE in hitting**
  - Relative advantage determines comparative advantage

Same Holds True for Countries

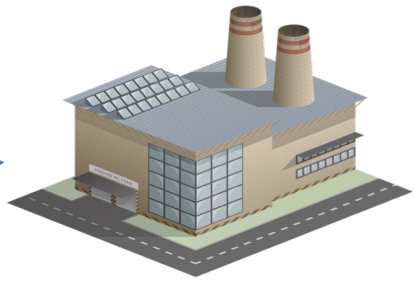


- **Every country has a good or a set of goods that it is RELATIVELY better at producing.**
  - Those are the goods that it will export.
  - It will import the other goods.
- **There are exceptions.**
  - Varieties and competition
  - May find countries trading the same goods back and forth.

How to Think About Imports

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

Ice Cream
(Exports)



Bikes
(Imports)

Trade Contributes to Growth

- EFFICIENCY:
  - Allocates production across countries efficiently so that countries can specialize in what they are best at producing
- Varieties
  - More choice for consumers
  - Better inputs for our production
- Competition
  - Brings in cheaper goods
    - makes consumers better off

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Why is the public turning against trade?

- **Gains from trade are very large for the economy, BUT**
  - Not always noticeable by consumers. Not clear why prices are falling at WalMart?
  - Individual might save $50, but
  - $50 x 300 million = $15 billion!
- **Costs of trade are very high for some workers and groups**
  - these costs have not been sufficiently appreciated or addressed by policymakers

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Problem: Statistics

- **Massive Trade Deficit**
  - 2.7% of US GDP
  - $566 Billion
- **Massive Trade Deficit with China**
  - 2/3 of US Trade Deficit

Trade With China: 63% of US Trade Deficit

Costs of Trade

- **Trade with low-wage countries will lower the earnings of low-wage workers as a group in the U.S.A**
- **Perhaps more importantly, however, is that the adjustment costs are big.**
  - People do not like to move, and getting laid off can be very traumatic, wages likely fall.
- **Costs of trade.**
  - Inequality
  - Adjustment costs

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How to Think About the Trade Deficit

- **A trade deficit is when:**
  - **VALUE of imports > VALUE of exports.**
- **Why does this happen?**
- **International transactions include:**
  - Imports and exports of goods and services - Current Account
  - ALSO: imports and exports of assets (investments) - Capital Account
- **The TRADE DEFICIT only looks at the Current Account**

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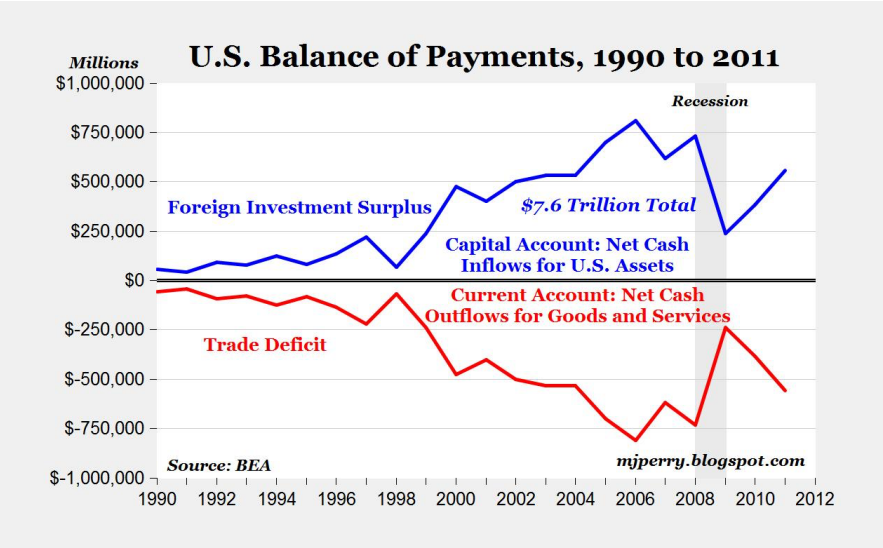
Trade and Investment Flows Balance Out



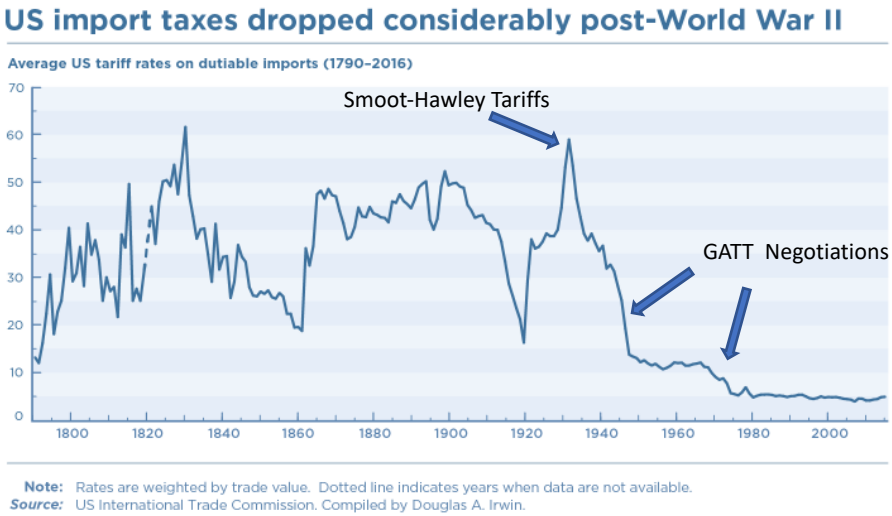
Policy Solutions:

If we must …
How do we "fix" the trade deficit?

Protect Domestic Markets and Workers

- **Tariffs**
  - Tax on imports
- **Quotas**
  - Simply limit the amount of imports

History of US Tariffs



How Does A Tariff Work?

- **It is a tax that is paid by the importer of the product**
- **What effect does it have on the price of the product?**
- **What effect does it have on domestic producers?**
  - Prices?
  - Production?
- **Does it work to protect labor?**
  - Yes and No

Tariffs

- **Tariffs temporarily reduce imports of particular goods.**
- **Tariffs raise prices.**
  - Final goods (*consumers*)
  - Intermediate goods (*producers who use imported inputs*)
- **Tariffs invite retaliation, lowering demand for our exports.**
- **Tariffs lower overall well-being.**
- **Tariffs are generally considered to be an inefficient way to help those people who are hurt by trade.**

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**

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Balanced Budgets & Increased Savings

- Reducing federal borrowing would reduce pressure on trade deficits.
- More savings would mean more domestic investment and less borrowing from abroad.

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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**
  - imposing widespread losses to 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**

What About US Trade Policy: Active!

- **US: Jan 22, 2018: solar panels**
  - 30% tariff on $8.5 billion of solar panels
- **US: Jan 22, 2018: washing machines**
  - 20% tariff $1.7 B of washing machines
- **China: Feb 5, 2018: sorghum**
  - Into effect on 4/17/18
  - $1 billion (178.6% tariff)
- **March 9, 2018: tariffs on steel and aluminum imports**
- **May 18, 2018: Negotiations end tariffs on Sorghum**
- **China: Aug 14, 2018: WTO dispute against US solar panel tariffs**
- **Tariff dispute with China accelerates…**

Trade War

- **United States**
  - March 9: US Tariffs on steel and aluminum
  - April 3: US tariffs on $50 bn in imports from China
  - April 5: considering tariffs on another $100 bn
  - June 15: another $50 bn
  - August 2: another $200 bn
  - August 23: another $30 bn
  - October 30: US hits at tariffs on remaining Chinese imports
- **China**
  - March 23: tariffs on $3bn of US imports
  - April 4: Tariffs on $50 bn in imports from US
  - June 19: tariffs on $50 bn US goods
  - August 3: another $60 bn
  - August 23: another $30 bn
  - China is out of ammunition

Did the US Win?

Trade War…

- **What good might it do?**
  - Chinese are engaged in improper activity wrt intellectual property
  - Might fix it
- **What harm might it do?**
  - Jeopardize future negotiations
  - Great uncertainty in international markets

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?**
  - uncertainty