

Removing New Obstacles to Free Trade

John B. Taylor

Basic economics teaches us that government-imposed restrictions on trade between countries hurt the people in the countries where governments impose them. Free trade—zero tariffs and zero restrictions on trade—improves people’s lives through comparative advantage and the expansion of markets. That is why Adam Smith recommended that Britain unilaterally reduce trade restrictions centuries ago, and why Milton Friedman recommended the same for the United States a half century ago saying in *Capitalism and Freedom* “I believe that it would be far better for us to move to free trade unilaterally, as Britain did in the 19th century...”

This *unilateral* approach to free trade, however, has not always worked in practice, and has rarely been used in recent years. Rather we have seen *reciprocal* approaches in which one country says to another country that it will reduce its trade barriers *only if* the other country reduces its trade barriers.

A reciprocal approach works by bringing exporters into the political process. Exporters benefit from lower trade barriers in other countries and thus they counter producers of domestic products who fear foreign competition and argue against tariff reductions. Barriers to trade have been reduced dramatically through such reciprocal trade agreements over the years, including the just-completed United States, Mexico, and Canada (USMCA) trade agreement, which will be fully implemented on July 1, 2020. Sometimes called NAFTA 2.0, USMCA expands the earlier North

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American Free Trade Agreement (NAFTA) which also reduced trade barriers.

But now there are new obstacles to achieving free trade.

One obstacle is that some countries are starting with much higher tariffs than other countries. The asymmetry makes it hard to get a negotiation going. For example, intending to start a trade negotiation with China, the United States recently imposed higher tariffs on steel and aluminum saying that the new tariffs will only be cut if China cuts its barriers to trade. However, this retaliatory approach is dangerous for it can lead to trade wars in which China retaliates with more restrictions, the United States then does the same, leading to an upward spiral. Trade wars have occurred in the past, including during the Great Depression of the 1930s. They certainly do not improve people's lives.

This retaliatory approach is sometimes expanded beyond trade policy to domestic regulations where even greater dangers lurk. In the 1990s, for example, trade negotiations between the United States and Japan—called the Structural Impediments Initiative—included reform of domestic retail store regulations in Japan to encourage more purchases of American goods. Such approaches raise difficulties because the expanded regulatory policies are under the jurisdiction of many different government agencies with less coordination and increased chance of retaliation.

A second obstacle has recently been revealed by the Coronavirus pandemic. This is the realization that many essential products consumed in the United States are produced in global supply chains with inputs of materials and parts made elsewhere, many in China and India. According to the Institute for Supply Management about three-quarters of American firms reported supply chain problems in China this past spring. Paula Dobriansky, who served as Under Secretary of State from 2001 to 2009, notes that China has “threatened to exploit Beijing’s control over medical supply chains as retaliation against U.S. efforts to hold China accountable for its actions during the pandemic.”

Already the United States and other governments are looking for ways to ramp up home production of essential products. And they are developing their own forms of retaliation. For example, the United States is declaring that computer chips made anywhere with American tools cannot be sold to the Chinese firm Huawei without breaking U.S. laws.

Higher costs and less efficiency are created by such breakdowns in global free trade. The pharmaceutical firm Gilead reports in the context of its COVID-19 ther-

apeutic drug remdesivir that “Any disruption to the supply chain impacting these scarce raw materials and other manufacturing inputs could reduce the amount of remdesivir produced and increase the time it takes to do so.”

What can be done to deal with these new obstacles? First, be as clear as possible that the goal of free trade is to improve people’s lives, especially when a trade war appears imminent. Second, look to alternatives to breaking up global supply chains, including the use of stockpiles of essential inputs; this was long ago offered as a solution to concerns that material for military uniforms could be held hostage to fabric and apparel production in Asia or Africa. Third, focus on the specific details when security issues are raised; it is not hard for protectionists to claim vague national security issues to halt competition from free trade.

We must insist on clear evidence, promote good pro-growth international economic policy, and lead in keeping markets open and tariffs low. The Administration and Congress and must work together to bring different constituencies together on this issue.