

# Iowa Ag Review



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## Trade, Wealth Creation, and American Agriculture

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**W**hy do we trade? Most Americans would answer this question with some reference to the benefits of expanded markets for U.S. goods and more job opportunities. However, if asked the question, why do we work? most would respond that we work to earn money so that we can buy things. At a personal level, we intuitively know that trading our specialized labor with others (using money as the means of transactions) gives us a higher standard of living than if we tried to produce everything ourselves. We know and act on the knowledge that specialization enhances our individual wealth. But economists have known for more than 200 years that what holds at the individual level also holds nationally. A country will have more wealth and a higher standard of living if the country specializes in producing those products that it is relatively good at producing, exporting the surplus, and using the proceeds to buy imported products.

The notion that the gains from foreign trade should be measured by what we import, not by what we export, is difficult for many to accept. Clearly, the statements of some of our leaders in Washington suggest that they see the benefits of trade in terms of our ability to increase exports, not in terms of our ability to increase our imports. For example, Secretary of Agriculture Veneman frequently argues that she wants to open up overseas export markets for the benefit of U.S. farmers. And it is a common bipartisan belief in Congress that increased



imports are actually bad for the United States. AgWeb.com ("Inside Washington Today," October 1) reported that Senator Lott (R-Miss.) held up the legislation that granted normal trade relations status to Vietnam because of his concerns that the Vietnamese catfish industry threatens U.S. catfish farmers. And Senator Baucus (D-Mont.) has led efforts to limit Canadian softwood lumber because such imports hurt American lumber mills.

As major exporters, Iowa and other Corn Belt states have a keen interest in the direction of U.S. trade policy. Will the United States follow its free trade rhetoric and pursue global free trade agreements that expand trade? Or will concern about the impacts of imports limit expansion of trade? While nobody can say with certainty whether the United States will become more or less protectionist, a closer examination of the issues will help clarify the issues so that a more informed debate can take place.

### IMPORTANCE OF EXPORTS TO CORN BELT AGRICULTURE

The United States has exported an average of 20 percent of its corn production and 45 percent of its soybean production over the last five years. We exported additional amounts of corn and soybeans as

meat. Changes in the demand for U.S. corn, soybeans, pork, beef, and poultry by overseas consumers have a direct impact on the prices Iowa farmers receive for their production. This direct link is why many look to the expansion of feed and meat exports as the only way to achieve sustained strength in market prices.

Most U.S. farm leaders rail against markets closed to U.S. exports. But how easy is it for foreign countries to open up their markets? A look at our own political debates about protectionist policies will show why such openings are difficult to achieve.

### THE POLITICS OF TRADE POLICY

If all our political leaders were well trained in economics, then they would accept the fact that we export goods to earn foreign exchange so that we can purchase imported items. If, in addition to being good economists, they did not care if they were re-elected, then they would adopt the trade policy that would create the most wealth for U.S. residents. That policy would be for us to unilaterally take down all of our trade barriers. This action would lower import prices, raise our standard of living, and increase the level of domestic competition. This increased competition would help to keep consumer

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prices low in the future and would lead to increased productivity as companies invest to stay ahead of domestic and international competition.

If unilateral trade liberalization would be so good for us, why haven't we adopted it? The answer is simple. Enhancing national wealth is not the goal of trade policy. Policy results from the natural desire of our political leaders to respond to the interests of their constituents. And whose interests are most likely to be brought to the attention of our leaders? The interests of those groups for which policy benefits are large enough to justify the hiring of a lobbyist.

In Montana, owners of wheat-producing land and timberland have an interest in limiting wheat and lumber imports from Canada. Steel manufacturers and labor unions that represent steelworkers in Pennsylvania and Ohio have an interest in limiting steel imports from South Korea and the European Union (EU) to maintain steel profits and steel jobs. Sugar producers in North Dakota, Minnesota, and Florida want continued restrictions on sugar imports to maintain their artificially high sugar profits. Clearly, it makes economic sense for all these groups to fund lobbying efforts to convince Congress and the Administration to adopt protectionist policies. And these same forces are at work in every country where competition from U.S. exports threatens their own vested interests.

To see why anti-import forces often win policy debates, consider the U.S. sugar program. A recent report by the Government Accounting Office (GAO) estimated that U.S. consumers would gain between \$770 million and \$1.96 billion per year if we completely opened our market to foreign sugar. This is a substantial amount of money, but it amounts to only \$2.70 to \$7.25 per U.S. resident per year. The GAO report indicated that each U.S. sugar producer would lose an average of about \$125,000 a year, with many growers losing in excess of \$1 million if sugar imports were liberal-

ized. In this case, the small gains to the many would seem to outweigh the losses to the few if we opened our market to imported sugar. Nevertheless, this economic imbalance does not usually translate into adoption of a free trade policy because Congress simply does not hear from outraged sugar consumers. It only hears from outraged sugar farmers.

The political balance of power in trade policy favors those who advocate for protectionism. The benefits of protection fall to the few who can organize and lobby for it, whereas the costs of protectionism are borne by the many (all of us) who do not find it worthwhile to spend time and money in support of free trade.

## WHAT ABOUT UNFAIR TRADE PRACTICES?

Of course, companies and industries that lobby for protectionist policies do not couch their arguments in terms of their desire for higher profits. Rather, they typically argue their case by citing “unfair” competition from foreign exporters. Often the “unfairness” is caused by lower labor costs in the exporting countries. But unfair practices can also include government subsidies to the exporting industries, direct subsidies to exports, and preferential tax treatments. Without some protection, lobbyists argue, companies and industries would be go out of business, and U.S. consumers would be forced to buy from foreign suppliers. What should be the response to these arguments?

One response is to simply say, so what? If a company in a foreign country chooses to supply us with a product at a price lower than we ourselves can make it, then we had better take advantage of the offer. If an exporting country's taxpayers want to subsidize our consumption, then who is taking advantage of whom?

Few countries, with the notable exceptions of Hong Kong, Singapore, and New Zealand, have adopted this “so what” response. This is not sur-

prising given that profits for domestic companies are at risk, and those at-risk profits can be used to lobby for relief. Besides, if domestic companies or industries go out of business because of import competition helped by excessive government subsidies, they may have a legitimate complaint.

Where can harmed industries get relief? From the federal government? There is a problem with allowing the domestic government to adjudicate a trade complaint. Past experience suggests that this results in too much relief and too few imports. (See "Coming Home to Roost: Proliferating Antidumping Laws and the Growing Threat to U.S. Exports," by Brink Lindsey and Dan Ikenon, Center for Trade Policy Studies, July 30, 2001.)

The alternative response is to let a more disinterested third party adjudicate trade complaints, beyond domestic boundaries. That third party is the World Trade Organization (WTO).

#### ROLE OF THE WORLD TRADE ORGANIZATION

The WTO was formed upon completion of the Uruguay Round of trade negotiations in 1994. Its primary purpose is to review trade policies and to settle trade disputes between member countries. The WTO has no ability to enforce its findings, so it can settle disputes only if member countries choose to adhere to WTO rulings. So far, the track record of adherence is mixed. The EU was found to be out of compliance when it banned U.S. beef imports produced with growth hormones. But the ban continues. The WTO has ruled twice against the United States for use of the foreign sales corporation tax, which could lead to \$4 billion worth of sanctions if the dispute continues.

If the WTO finds that a country is out of compliance, then trade partners are allowed to use sanctions in the form of import tariffs against the offending country's exports. As a result, the U.S. has raised

the cost of certain European exports by \$116 million in response to the EU ban on hormone beef, subsequently increasing the cost of these items for U.S. consumers. It might seem odd that a country punishes another country by taxing its own citizens with import tariffs, but that is the only remedy offered.

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### *If an exporting country's taxpayers want to subsidize our consumption, then who is taking advantage of whom?*

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For the WTO dispute settlement mechanism to work, countries must voluntarily give up some of their economic sovereignty and follow WTO rulings. The benefits to the world trading system from reduced national sovereignty are obvious: trade volume and value will expand, accelerating world wealth creation. Giving up some economic sovereignty is good for each individual country as well, because WTO rulings can be an effective counterweight against lobbyists for domestic industries that seek protectionist policies. Thus, for example, if Canada brings a WTO complaint against United States softwood lumber tariffs and wins, then U.S. politicians that have supported the tariffs can say that they have done all they can do, and U.S. citizens can enjoy the benefits of less expensive wood.

#### FUTURE TRADE POLICY AND AGRICULTURE

The best hope for expanded exports of U.S. corn, soybeans, and meat products lies with the WTO. The fourth biannual WTO trade ministers' conference is scheduled to meet in Doha, Qatar, on November 9. (The last conference was held in Seattle in 1999.) At the top of the agenda is an

agreement to start a new round of trade liberalization talks. Trade in agricultural products likely will be a large part of a new round. However, developing-country members are protesting that they did not receive enough of the benefits from the last round of talks. They argue that they still face unfair competition from EU export subsidies, import tariffs, and producer subsidies. They dislike U.S. production subsidies and import restrictions on textiles and certain agricultural products such as peanuts and sugar. Developing countries will need to be convinced that they will have more time to implement the last agreement, and that any new agreement will open up developed-country markets to their goods.

If the United States and the European Union are serious about wanting to increase world trade, then a demonstration of good faith would go a long way toward showing that a new round of trade negotiations will actually benefit the developing countries. Such a demonstration could be a speedup in the timetable by which textile trade is liberalized. Of course, U.S. cotton farmers would line up to fight this liberalization. Or, the European Union could further lower its wheat support price and wheat export subsidies. Of course, French wheat farmers would likely drive their tractors to Paris in protest. Or, the United States could replace all non-recourse loans with recourse loans, which would eliminate the government-provided incentive to keep producing corn, soybeans, cotton, and wheat when the market is signaling farmers to cut production. We all know what the reaction to this proposal would be. Nevertheless, developing countries are looking for such a demonstration. If we want to move forward with further trade liberalization, then the United States and the European Union may have to sacrifice a few sacred cows currently protected from import competition. ♦