



Global Trade Analysis Project

Primer on the Costs and Benefits of Trade and Trade Policies

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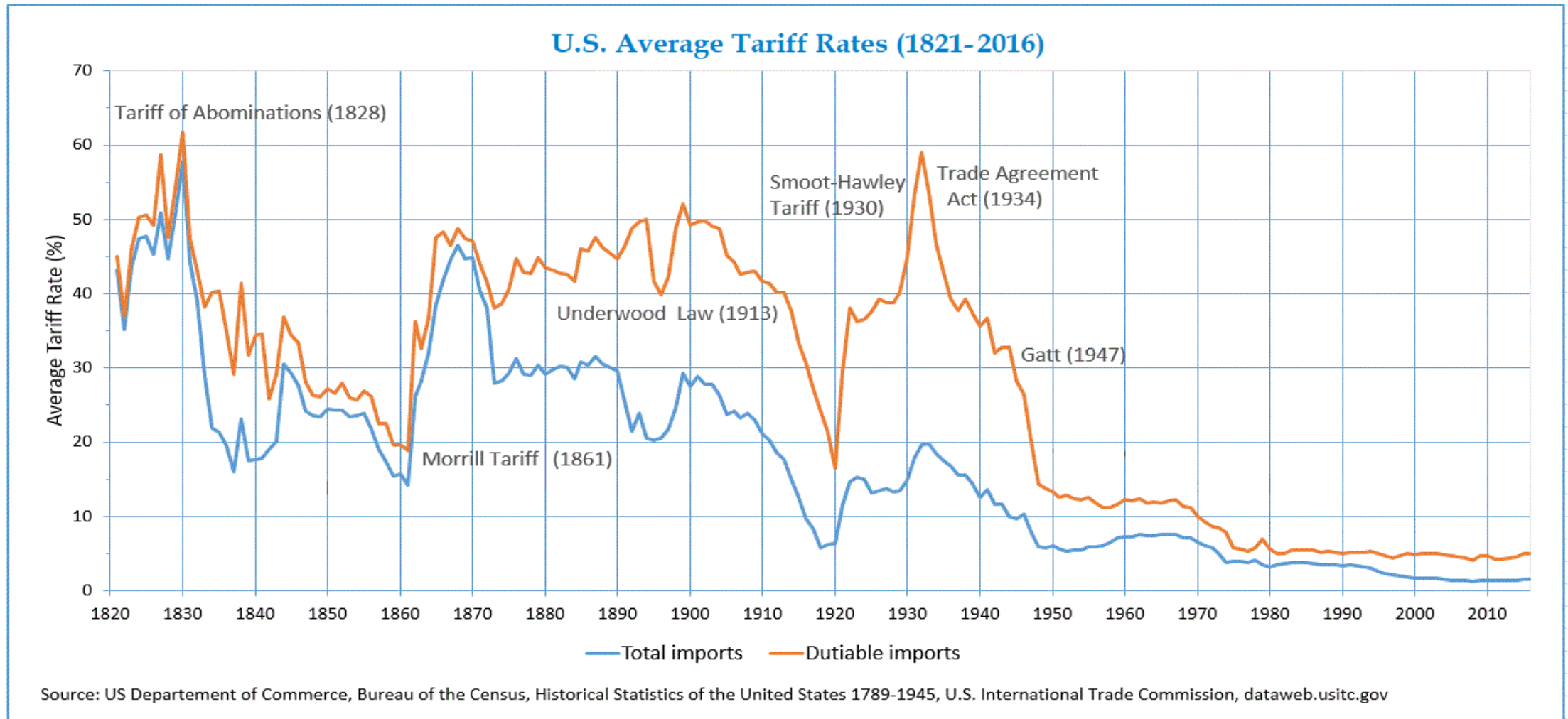
What do economists think?

- **Comparative advantage**
 - 18th & 19th Centuries—Adam Smith, David Ricardo
- **Increasing returns to scale, imperfect competition, love of variety**
 - 1970s & 1980s—Dixit-Stiglitz, Krugman
- **Firm heterogeneity, fixed trade costs, productivity impacts**
 - 2000s—Melitz

Trade-offs

Advantages of free trade	Advantages of protection
Market efficiency	Avoids displacement—especially in the short term
Scale economies	Protects infant industries
Lower prices for inputs and consumer goods	National security (e.g. food or energy self-sufficiency)
More variety	Tariff revenues/luxury taxes
Minimizes rent-seeking behavior	
Promotes innovation	

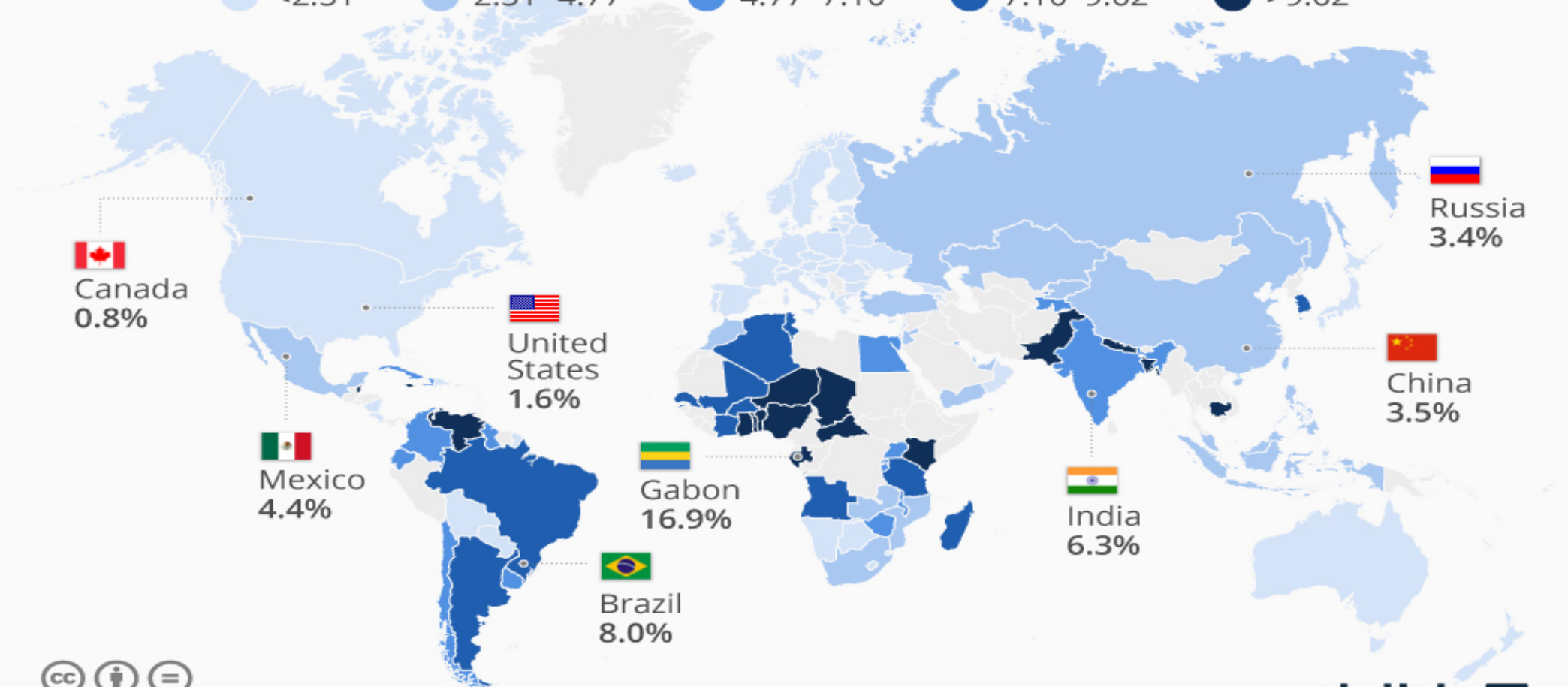
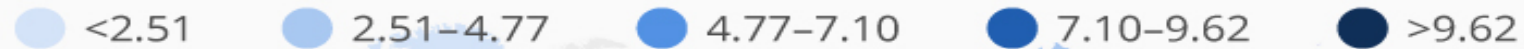
US tariffs have never been lower...



And tariffs are low in most parts of the world

Where Global Tariffs Are Highest And Lowest

Average weighted tariff rate applied across all products in 2016 (%)



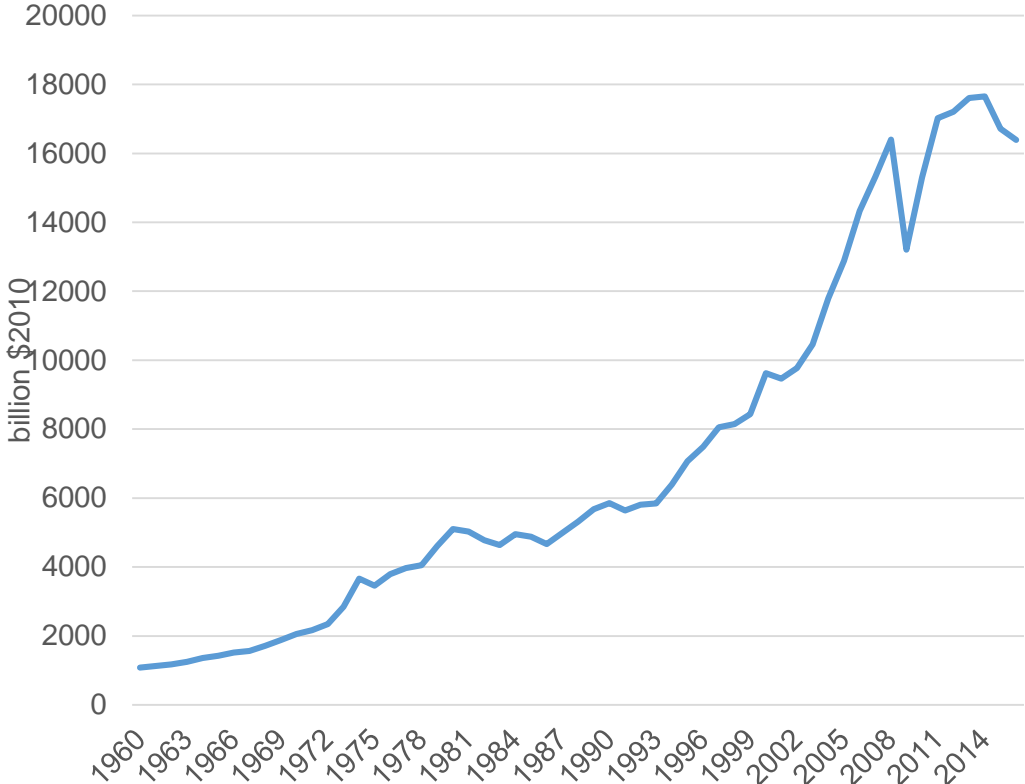
@StatistaCharts

Source: World Bank



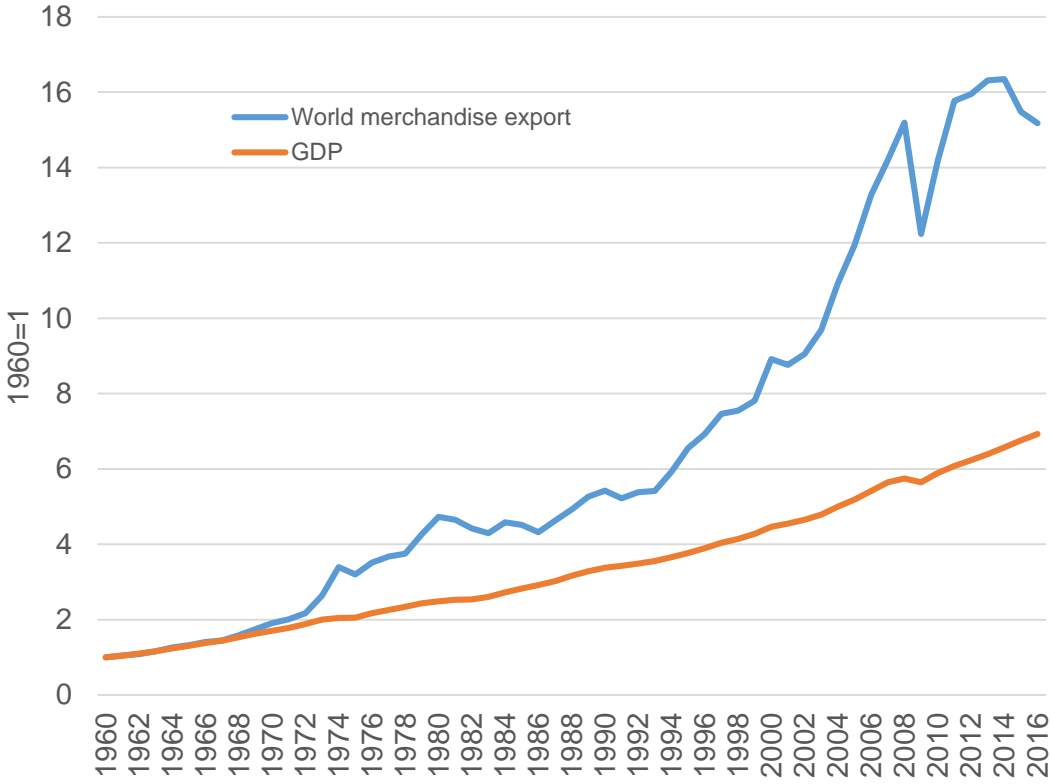
Global trade has outpaced global output

World merchandise export, constant \$2010



Source: World Trade Organization, World Bank

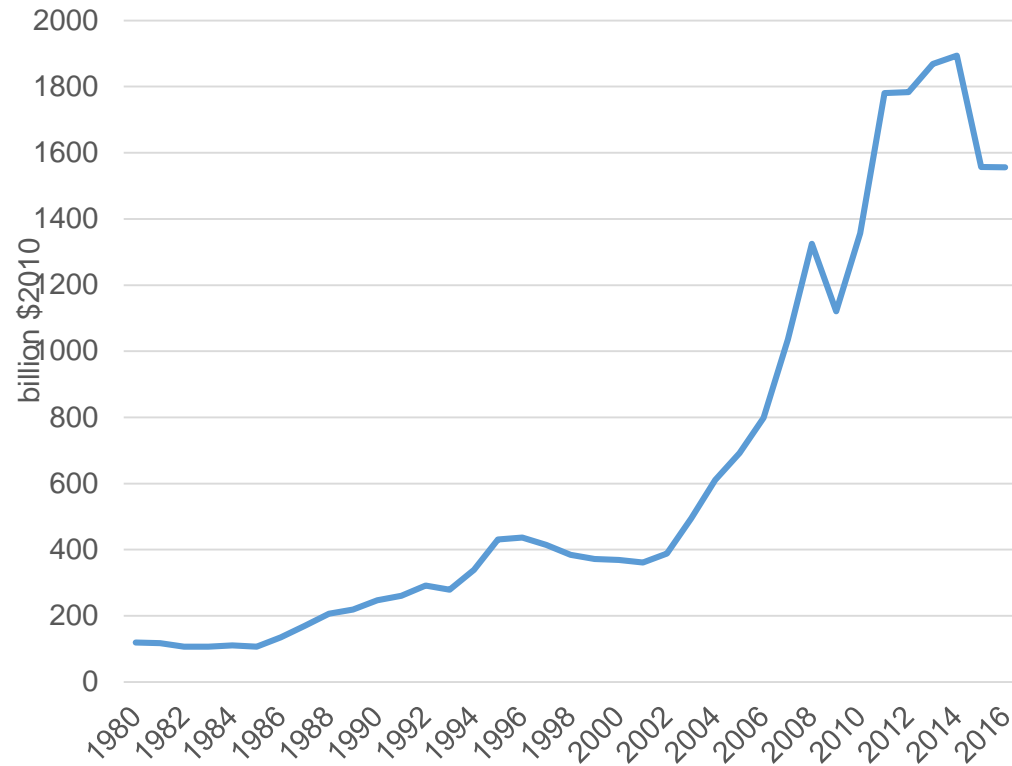
World merchandise export vs GDP (1960=1)



Source: World Trade Organization, World Bank

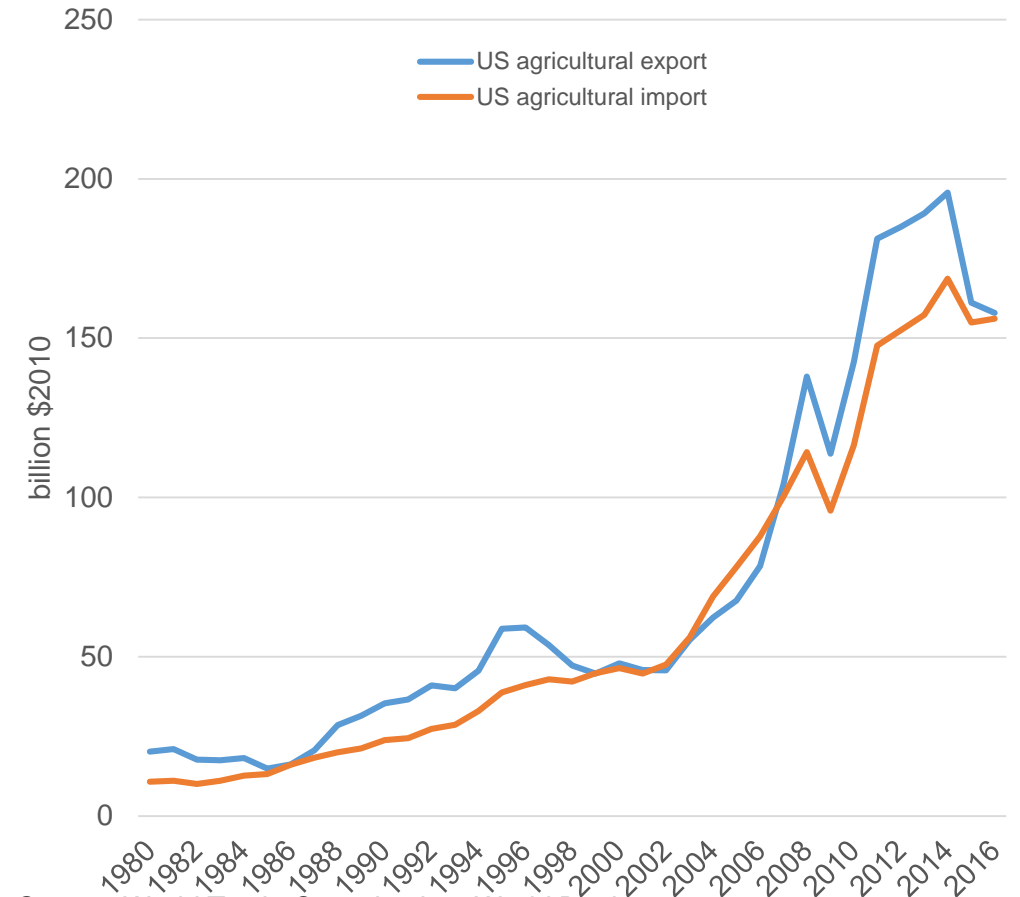
Large rise in agricultural trade, particularly post-2000

World agricultural export, constant \$2010



Source: World Trade Organization, World Bank

US agricultural trade, constant \$2010



Source: World Trade Organization, World Bank

Assessing benefits/costs from free trade

- **+1-2% of GDP from efficiency gains**
 - Ignores dynamic effects (productivity, innovation, pro-competitive, increased varieties)
- **There are nonetheless winners and losers**
 - Those negatively impacted are typically easy to identify, the benefits are more diffuse
- **Gains should be sufficient to help displaced workers**
 - Re-training, re-localization
 - But implementation has typically been deficient

Trade vs. technology

- **Still an open question**
 - Consensus is that productivity improvements account for up to 80% of job losses in manufacturing
- **Global economy made room for China's extraordinary growth**
 - Autor and colleagues estimate that China's emergence displaced around 1 million manufacturing jobs in the U.S.—with a concentration in the Midwest
 - China is currently trying to rotate its economy from investment-led growth to consumer-led growth. This implies oversupply in certain key sectors such as iron and steel.

Macroeconomics and trade imbalances

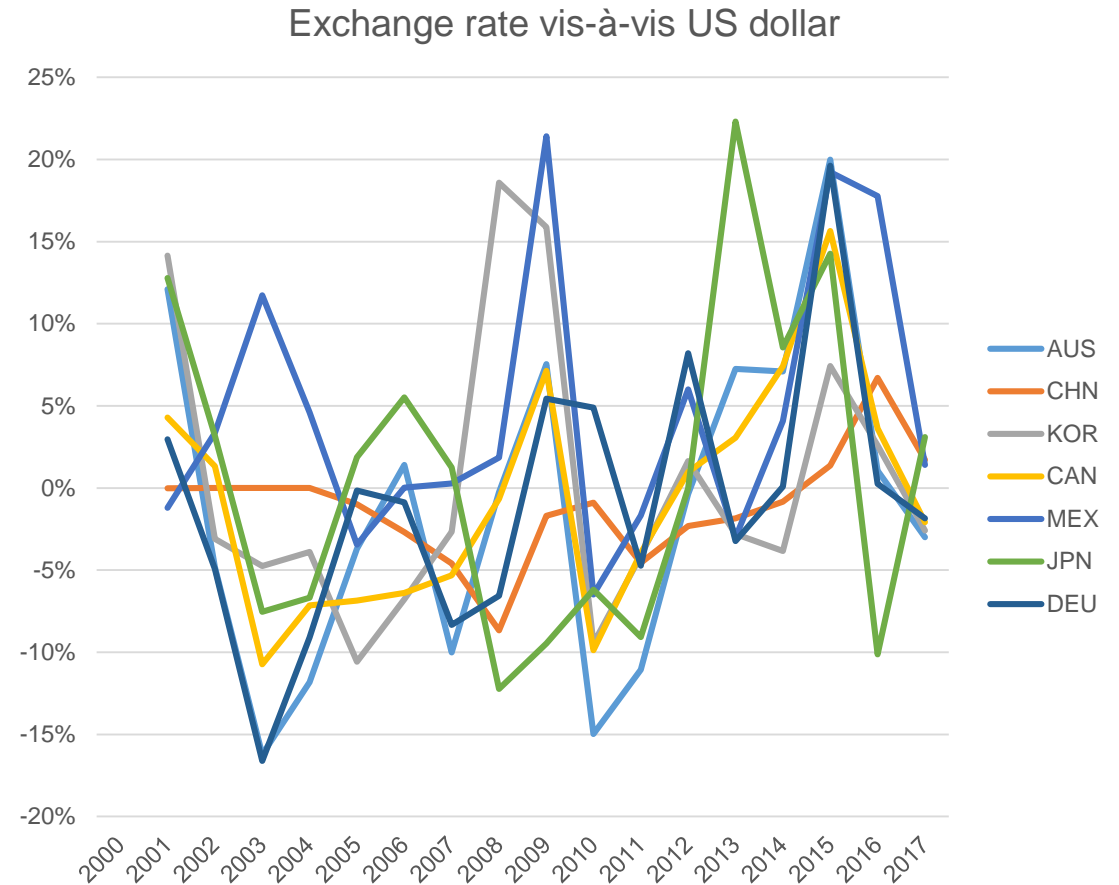
- Econ 101: Difference between savings and investment is equal to the net trade balance

$$S - I = X - M$$

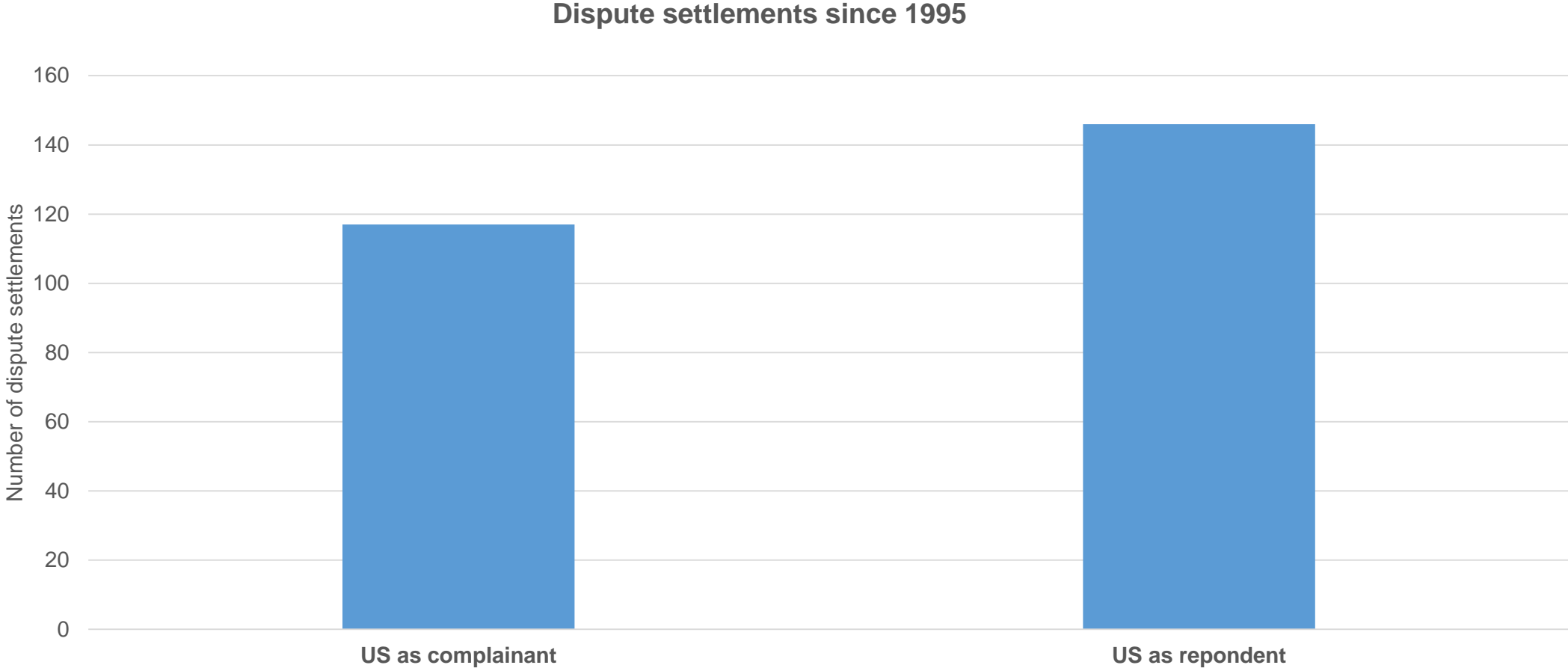
- Dollar is the reserve currency

Is the trading system fair?

- **Negotiated multilaterally**
 - Implies countries see mutual benefit (not necessarily always purely economic)
- **Most tariffs are too low to matter, currency movements and trade impediments (e.g. ports, logistics, procedures, standards) are likely to be a bigger hindrance to trade**
- **Countries do not always play by the rules, but there are remedies**



Significant use of WTO's dispute settlement court



Source: World Trade Organization

Conclusions

- **The global economy is unbelievably complex**
 - Long-integrated supply chains
 - Foreign direct investment & off-shoring
 - Rapidly changing technologies and consumer preferences
- **A trade war will be very costly economically**
 - Ossa (2016) estimates that average tariffs will climb to 60%
 - Nicita et al. (2018) have a lower, but still very significant rise to around 36%
- **Let's hope for the best, but a lengthy period of uncertainty could also prove harmful to the US economy**