ECONOMICS U$A
21st Century Edition

PROGRAM #27

# INTERNATIONAL TRADE: FOR WHOSE BENEFIT?

AIRSCRIPT

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Final Transcript

Annenberg Learner (Logo and Music)

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## TEASER

DAVID SCHOUMACHER: Japanese cars brought low prices and high gas mileage to American drivers. What happened when political pressure forced import cutbacks? The American steel industry thought their foreign competitors were violating trade laws to make sales in the United States. How did the U.S. government try to make foreign governments and steel companies play fair? American companies manufacturing abroad and the North American Free Trade Agreement--Would Americans hear a giant sucking sound of millions of jobs going to Mexico?

DAVID SCHOUMACHER: I'm standing in front of the Ronald Reagan Building and International Trade Center in Washington D.C. to ask this question: "International Trade – for whose benefit?" With the help of Economic Analysts Richard Gill and Nariman Behravesh we'll explore that question on this 21st-Century edition of Economics U$A. I'm David Schoumacher.

(MUSIC PLAYS – OPENING TITLES)

## PART I

DAVID SCHOUMACHER: Nobody worried too much about the first Japanese cars to reach the United States. It was the "heyday" of the "gas guzzler." As the nation's largest consumer of steel, glass and rubber, the auto industry drove the economy. Since the days of Henry Ford the American auto industry kept its hand on the wheel and its foot on the accelerator. Detroit sold the big car; and American drivers bought it. High gas mileage didn't mean much to people used to 30-cent gas. 1973 changed that. War in the Middle East and an oil embargo were followed by short supplies, gas lines, and skyrocketing prices. Higher gas prices made Datsuns and Toyotas look a lot better. To some, importing Japanese cars meant exporting American jobs. So why not just cut imports to save jobs? For drivers, cars are transportation, but in Detroit, cars are jobs... good jobs and lots of them. For autoworkers, more imports would mean layoffs, often permanent layoffs, and a search for new work by men and women who had spent their lives on the assembly line. President Douglas Fraser of the powerful Autoworkers Union took the workers' case to Washington. His members and their employers needed protection from their Japanese competitors. Protecting autoworkers and the auto industry made little sense to believers in free trade like economist Robert Crandell of the Brookings Institution, a Washington think tank.

ROBERT CRANDELL: "I rather think that the protection for workers in that industry defeats the purpose. To the extent that we protect those workers and protect that industry…and keep an umbrella over their prices, their profits and their wage rates, there's no incentive for them to reform."

DAVID SCHOUMACHER:  But on Capitol Hill, worried workers swung more weight than eminent economists, especially with Detroit Congressman John Dingell, Chairman of the House committee which sets import rules.

JOHN DINGELL:  “Almost every country has quotas on importation of Japanese automobiles.  The French say that they can bring in any number, but only two or three percent will leave the dock.  The Italians allow in 2,300.   The British allow in approximately 10 percent, the Germans approximately 10 percent.  The Japanese, however, will set up automobile industries around the world in the full expectation that those automobile industries as well as their own are going to be exporting into the United States.  So I felt it was absolutely necessary, in view of the grotesquely unfair trade practices of our trading partners…especially the Japanese...that real quotas, and domestic content requirements equal to those of other nations…should be laid in place by the United States.”

DAVID SCHOUMACHER:  John Dingell was one of the leaders of a building drumbeat of protectionist feeling in Congress and in the press.  Free traders fought back.  In the middle was the nation’s chief trade official… Special Trade Representative, William Brock.

WILLIAM BROCK:  “You know, they came to us…and Congress…and they said, ‘You gotta protect us.’  Congress started talking about passing a bill to hold imports to maybe half the present level at that time.  We didn’t like that because we thought by using the wrong action once, you protect something like that, you can’t get rid of the protection.  So we talked to the Japanese and we said, ‘Look, it takes 5, 6, 7 years to re-tool to a completely new market demand.  You can’t just dream up a new car and put it out for sale.  You have to design and engineer it, build new plants for it, build new machines to produce it, and that’s a long-term process.’  And we suggested that it would be appreciated if they restrained for a limited period of time…3 or 4 years.  They did.”

DAVID SCHOUMACHER: Voluntarily or not, the restrictions took hold. Japanese auto imports dropped by almost eight percent in a year. Thousands of autoworkers were off unemployment and back on the job. Happy ending? Sure, if your livelihood depends on the auto industry, but if you're buying instead of making or selling cars, it might be a different story. In the wake of the voluntary restraints a new sticker appeared on Japanese cars… the ADM--Additional Dealer Markup.

TOYOTA SALESMAN: "Generally you are going to pay a little bit more for a Japanese car versus an American car, but I think the level of quality that you find in a small car is worth it."

CAR BUYER: "Oh it bothers me immensely. I wish they'd get rid of the import quotas. I think it's one of the biggest rip-offs of Americans I ever heard of. It's only to protect incompetent automobile manufacturers."

DAVID SCHOUMACHER: Bad news for buyers was good news for dealers like Toyota dealer, Kay Jennings.

KAY JENNINGS: "For the Japanese car business we sold fewer cars, but we had many many price increases because of the restrictions. Because if you have fewer cars the prices are going to go up but it did the same thing to the American cars. The only thing where the restrictions really hurt was the general public."

DAVID SCHOUMACHER: And it wasn't only the buyers of Japanese cars who were hurting. We paid more for American cars as well, as American car dealers discovered that they could raise prices, too, as long as they stayed under Japanese prices. In Detroit, employment was high, but at what cost to car buyers?

ROBERT CRANDELL: "How much did it cost American consumers in terms of higher prices of automobiles in order to keep one additional job in and around Detroit? And the answer was, by my calculation, somewhere around 160 thousand dollars. That may sound high to you, but almost every calculation of the effective trade restraints on employment levels of the United States comes out with something around 100 or 200,000 dollars per job. It's not unusual."

JOHN DINGELL: "This kind of a fellow looks at the problem that a consumer has in terms of paying a little more for the goods at this particular time. He doesn't look at the future increases that are going to be loaded on once our American automobile industry and other industries are down the tube. Nor does he look at the economic consequences of being dependent on goods abroad. He doesn't look at the other costs that are associated with this and, in consequence, he is breeding himself a splendid future and present disaster because he's not looking at the world as it really exists."

DAVID SCHOUMACHER: The competition that comes with trade means choices for society as well as consumers. The cost of saving thousands of American jobs may be fewer choices and higher prices for millions of American consumers. We asked economic analyst Richard Gill if the American jobs that were saved were worth the higher prices of cars that followed the restrictions.

(MUSIC PLAYS—COMMENT & ANALYSIS I)
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RICHARD GILL: It's a difficult question to answer because it has so many ramifications. Over the long run, exports and imports for a given country tend to balance out, as indeed they must for all nations considered together. Since imports, in a certain sense, "cost" us jobs, and since exports, in a certain sense, "create" jobs, there is, in principle, no long-run unemployment problem associated with free trade. Hence, economists say, let trade <u>be</u> free so that consumers can have lower car prices; that is, they can enjoy the gains from comparative advantage we discussed earlier. However, in the short-run, increases of <u>particular</u> imports, cars, textiles, whatever, can definitely cost jobs in those industries. Thus, against the gain of having cheaper goods for consumers, you can have painful dislocations in specific domestic industries. Also, the long run over which exports and imports are likely to balance may be a very <u>long</u> run. We have been running major deficits with Japan for years. Good news in terms of getting cheaper goods. Bad news in terms of a downward pressure on employment. Still, in total, the gains from comparative advantage tend to be so large that economists, unlike perhaps autoworkers or textile producers, are willing to wait for the long-term adjustments to work out. Of course, if the other country is competing unfairly, then that is another matter!

## PART II

DAVID SCHOUMACHER: America likes competition on the football field, in politics, before the law and in business. An even match on a level field seems to be the best way to decide the best team, the best candidate, or the best buy. But what happens when a foreign company, a company beyond the reach of American law, doesn't play fair? What happens when "free trade" isn't "fair trade?" The American steel industry, Modern America, its buildings, its bridges, its cars, was built on steel. For almost 75 years, the industrial giants which ran American steel played by their own rules. Lack of competition made price increases easy, easier than replacing old and inefficient factories and easier than risking costly strikes over pay raises. But in the 70's, the American steel industry found itself under competitive fire for the first time. And its historic complacency started coming home to roost. As U.S. Steel waned, Euro Steel waxed. Steel producers from countries like Germany and Britain undercut American companies on American buildings and bridges. Some suspected that German and British steel makers were dumping, selling steel in the United States for less than they were selling it at home, perhaps even less that it cost them to make it.

JOHN DINGELL: "There's no way that this country, which has the only private steel industry in the world, can compete with government steel dumped over here. So, through a whole broad spectrum of devices and the clearest violations of GATT and other agreements, and also our laws, subsidy goes on. They bring it over at a subsidized price."

DAVID SCHOUMACHER:  But if foreign governments were willing to take losses selling below cost in the United States, why shouldn't we just sit back and enjoy the low prices?

WILLIAM BROCK:  "Another government could pick an industry, subsidize the dickens out of it, and give it enough money to buy into the U.S. market, and if they gave them enough, they could destroy the U.S. industry because our industry is just one or two or three companies competing with the whole government in some other country, with their whole treasury."

JOHN DINGELL:  "Well, the practical result of that is to simply dispose of your industry.  And ultimately and probably not very far down the line, you will have disposed of your steel, your auto industry.  You will have grotesquely hurt all of the industries of which the auto industry is the largest single consumer.  That includes computers, textiles, steel, non-ferrous metals, glass, rubber, and a lot of other things.  And you will find that you simply will have de-industrialized that part of your economy.  You will find that you have lost a prodigious number of jobs and you will convert from high paying jobs to low paying jobs.  Not on the basis of fair competition, but on the basis of subsidy.  And all of a sudden, all of those consumers that you had been trying to benefit by seeing to it that they got low prices on subsidized exports that come into the United States—they're not consumers anymore because they can't afford to buy anything."

ROBERT CRANDELL:  "Congressman Dingell doesn't have enough faith.  One of our greatest resources is our human capital stock.  We have an enormously talented educated work force.  The notion that somehow the only thing that we'll be able to find for them to do is to flip hamburgers at McDonald's I think is outrageous.  I don't think that a society is likely to succeed for most of its citizens by trying to lean against the forces of technological and economic change.  And it seems to me that that's what this debate's about."

DAVID SCHOUMACHER:  With industry and jobs on the line, pressure mounted on

President Jimmy Carter. Americans deserve protection from predatory pricing practices from abroad, but Congressman Dingell might lead Congress to pass outright quotas, which could wreck the complex and delicate framework of world trade. As the crisis reached its peak, Carter turned to one of the country's experts on international trade and finance, Deputy Treasury Secretary Anthony Solomon. Solomon's solution – the "trigger price mechanism." Use the Japanese production price as the trigger for starting dumping investigations.

ANTHONY SOLOMON: "Everybody in the world accepted the fact that Japanese costs of production were the lowest in the world. And, therefore, if you sold below that, then there were good grounds for suspicion that you were dumping. You were not covering your cost of production, which was the definition under the law. The idea was to meet their legitimate complaint about dumping in a way that would be less disruptive of imports that would be of some help to the steel industry, and at the same time maintain price competition, particularly in the zones above that of covering the cost of production of the most efficient producer in the world. I must tell you that a lot of economists have told me that it was a very elegant concept."

DAVID SCHOUMACHER: Elegant it may have been, but did it work?

WILLIAM BROCK: "Trigger price mechanism was an effort to sort of soft-land the U.S. steel industry, to not totally protect, but to give them some assurance that they weren't going to be undercut in prices and could continue to grow and to invest."

ANTHONY SOLOMON: "I'm rather pleased by, frankly, my ingenuity in coming up with it. It still preserved the basic comparative cost of advantage theory which underlies international trade. It solved, for a couple of years, the political problem, and avoided protectionist quota action. And all the key actors, both the domestic industry and labor on the one hand, the foreign exporters to our market on the other, all felt that it was a much better solution than what was happening without it."

DAVID SCHOUMACHER: The international steel trade speeded up in the wake of the "Trigger-price mechanism." While the TPM slowed down subsidized competition from Germany and Britain, Japan's high efficiency steel industry, and low labor cost steel producers from Korea, Argentina and Brazil, got into the game. The "trigger-price mechanism" was an effort to draw a line in a battle between fair and unfair trade practices. The war is much wider. It's not confined to the steel industry or to dumping or to any one or two countries. After the "trigger-price mechanism" expired, there was a strong drift toward protectionism in many countries, including the United States. We asked Richard Gill to comment.

(MUSIC PLAYS---COMMENT & ANALYSIS)
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RICHARD GILL: There is little question that in the mid 1980s protectionist sentiment was in the air. A suspicion arose in the United States that some foreign countries were using exports to the United States as a means of promoting the domestic growth of their own economies. They were flooding us with their goods while keeping ours out. If this suspicion were based on the existence of very high tariffs abroad, it would be fairly easy to evaluate. Unfortunately, most of the obstacles that countries place in the way of foreign imports are more subtle than that, what economists call non-tariff barriers to trade. Government subsidies, as in the case of steel, are sometimes overt, sometimes hidden and complex: complicated licensing and import procedures; special regulations concerning the standards, specifications, and testing that imported products have to meet. The magnitude of such barriers is very difficult to assess. What can be said with some confidence is that countries who are running huge trade surpluses with the United States, like Japan, should take quite seriously the effort to open their economies to American goods as much as they can. For the alternative is very likely to be increased protectionism in the Untied States, higher tariffs, more quotas, special restrictions of our own. And, in this case, although we may suffer, our trading partners will suffer too, perhaps even more seriously. The correct path is as obvious as it seems difficult to follow.

PART III

DAVID SCHOUMACHER: As Congress was considering passage of the North American Free Trade agreement in 1993, workers in the United States grew increasingly apprehensive about losing their jobs. A fierce debate raged in the U.S. What would be the impact of freer trade among the United States, Mexico and Canada?

ROSS PEROT: "Pay a dollar an hour for your labor. Have no health care…that's the most expensive single element in making a car…have no environmental controls, no pollution controls, and no retirement, and you don't care about anything but making money. There will be a giant sucking sound going south."

BILL CLINTON: "Good jobs, rewarding careers, broadened horizons for the middle-class Americans can only be secured by expanding exports and global growth."

DAVID SCHOUMACHER: NAFTA provided that, over a ten to fifteen year period, virtually all of the tariff barriers and most of the non-tariff barriers would evaporate.

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DAVID SCHOUMACHER: Since NAFTA was signed into law in 1993, has it fulfilled its promise of jobs and prosperity?

DAVID SCHOUMACHER: Kansas City Southern Railroad was started in the late 1800s by Arthur Stillwell. Stillwell's vision was to build a line from the heartland to the Gulf Coast and eventually to Mexico.

MICHAEL HAVERTY: " With our north south orientation we believed that if we could make an investment in Mexico and tie it into our line that we could develop what we called the NAFTA railroad.

DAVID SCHOUMACHER:  Kansas City Southern started operations to Mexico in June of 1997, transporting auto parts, grain, consumer products and automobiles.

MICHAEL HAVERTY:  "We have not hired more people, but you have to remember that had we not made that investment in Mexico, we would have probably had to lay off hundreds of people."

DAVID SCHOUMACHER :  The NAFTA Railroad is an example of the kind of investment and infrastructure so sorely needed in Mexico.  While the NAFTA Railroad didn't create jobs for its own operation, the fact that it could provide efficient and economical two way transportation of goods, indirectly generated jobs in other sectors on both sides of the border.

DAVID SCHOUMACHER:  Bimbo Bakeries was founded 57 years ago in a small Mexico City storefront.  It is now the largest bakery in Mexico.

DAVID SCHOUMACHER:  At about the time NAFTA was implemented, Bimbo decided conditions were ripe to have a stronger presence in the U.S., investing heavily in new facilities and acquiring such products as Entenmann's Pastries, Thomas' English Muffins, and Boboli pizza kits.

DAVID SCHOUMACHER:  Bimbo's relationship to the U.S. market is mutually beneficial as it imports much of its main ingredient supplies and equipment from the United States.

DANIEL SERVITJE:  In our case I think that jobs have been created on both sides of the border because of NAFTA.  We now have close to almost 10,000 people working in the U.S..

DANIEL SERVITJE: In Mexico we now have a much more stable economy because of NAFTA. So, certainly, our standard of living and the employment opportunities of our associates are much broader now then they were before.

LUIS DE LA CALLE: I think Bimbo is leading the way for other Mexican companies to invest in the U.S. and I think that is one of the counter intuitive results of the NAFTA.

DAVID SCHOUMACHER: Because of NAFTA, Mexico is a large recipient of direct U.S. investment, but also because of NAFTA, Mexico is becoming a large investor in the United States, averaging eight hundred million dollars per year. In addition, Mexico now buys 14% of goods the U.S. exports to the world. 35 percent of U.S. trade is with Canada and Mexico, a remarkable and deep integration. But labor representatives have concerns about the implications of free trade for workers.

THEA LEE: "It's the question of what is the set of rules that NAFTA put in place and how has that impacted average working people. One is certainly here in the United States. We've lost over half a million jobs, according to the Labor Department, just since NAFTA went into effect -- jobs which have moved to Mexico or Canada."

LUIS DE LA CALLE: "Now, you had some sectors that had experienced job losses both in Mexico and in the U.S., but these job losses, in my view, are more related to the globalization than the NAFTA. Let me give you a couple of examples. You have, for instance, in the U.S., been losing jobs in steel or textiles or apparel. Some of those jobs have actually come to Mexico, and Mexico would manufacture to find the goods that we re-export to the U.S. under the NAFTA. Those jobs, the U.S. was going to lose anyway. The question was whether those jobs would divert to China or Taiwan or they would come to Mexico. The beauty of the NAFTA was that if they came to Mexico then they will come with U.S. components."

DAVID SCHOUMACHER:  Proponents of NAFTA say that since opening U.S. markets, particularly after World War II, the country has experienced its greatest growth, its greatest improvement in jobs, and enjoyed a higher standard of living.

JIM JONES:  "I think NAFTA's been a great success no matter how you measure it.  It's been a success in improving the standards of living and creating political stability and openness in Mexico.  It's been a success at creating a net new increase in jobs in the United States.  It's been a great success in improving understanding between our two countries."

DAVID SCHOUMACHER:  So, was there a giant sucking sound of jobs going to Mexico as Ross Perot had predicted?  No.  Did it create some new jobs on both sides of the border?  Yes…the effects were positive though not huge.  How positive?  We asked Economic Analyst NARIMAN BEHRAVESH.

(MUSIC PLAYS - COMMENT AND ANALYSIS III)
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NARIMAN BEHRAVESH:  When a multi-national company from a developed country such as the U.S. chooses to produce goods in a developing country such as Mexico, the impact is very similar to international trade.

Production moves to the country with a comparative advantage in producing those goods.  As in the case of trade this benefits both the country making the investment and the country receiving the investment.  While there are some job losses, typically low-skilled workers in the country making the investment, there are more winners than losers in both countries.

Thus, investment, like trade has a positive-sum game rather than a zero-sum game.  In other words both countries benefit.

In the end, the early Maquiladora program turned out to be so successful that it was a major factor behind the establishment of the North American Free Trade Agreement or NAFTA. The combination of the Maquiladora program and NAFTA has helped Mexico to enjoy rapid growth during the last two decades. But not at the expense of the U.S., where consumers benefited from lower prices and companies trading with Mexico created new high-skilled jobs.

DAVID SCHOUMACHER: Economic principle tells us that "free trade," or at least "freer trade," will mean lower consumer prices and better living standards overall. But in the real world, the short-term world, all of us and our elected officials find it hard to turn away from the plight of those whose jobs are threatened by competition from abroad – no matter how fair that competition. For this 21st Century Edition of Economics U$A, this is David Shoumacher.

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