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U.S. FOREIGN TRADE POLICY: HISTORY AND REFORM

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ABSTRACT

An examination of U.S. foreign trade policy reveals significant policy inconsistencies over the decades, although there has been a post-World War Two trend towards trade liberalization. U.S. leadership in the formation of the GATT agreement and the WTO has been important in this regard, as have been concerted U.S. efforts to enter into viable bilateral and multilateral agreements with trading partners. There is ample room for improvement in U.S. trade policy in the future if political conflict can be minimized and if a consistent core of policy principles can be identified and followed.

Keywords: Foreign Trade Policy, Comparative Advantage in Trade, World Trade Organization (WTO), General Agreement on Tariffs and Trade (GATT), Multinational Enterprises (MNEs).

1. INTRODUCTION

Few issues generate as much coverage, interest, as well as misinformation in national political campaigns as a country's foreign trade policy. Support for or criticism of established policies highlight the impact on GDP growth and stability, as well as on consumer welfare, labor market efficiency, worker welfare, and on corporate earnings. Debates focus on whether specific sets of policy measures have a positive or a negative effect on a country's overall economic welfare.

The purpose of this article is to examine the history of U.S foreign trade policy with a focus on the positive and negative spillover effects. This historical analysis is followed with an examination of the arguments used in support of free trade as well as those used in support of trade restrictions. Finally, based on the evidence, an attempt will be made to structure a set of policy reforms needed to capture the benefits of trade liberalization and to minimize the negative effects.

2. A BRIEF HISTORY OF U.S. INTERNATIONAL TRADE POLICY

The primary authority in U.S. international trade policy is the U.S. Congress. The legislative branch of government was granted by the U.S. Constitution the power to levy trade restrictions and to regulate foreign commerce. However, some authority has been delegated to the executive branch of government over the decades (Akhtar et al 2024).

Although concerted efforts have been made to liberalize trade during the post World War Two era, earlier periods of U.S. history reveal significant measures of trade restrictions. For example, it is estimated that in tariffs were imposed in the 1790s at relatively low levels but rose significantly by the second decade of the 19th century (Halloran, 2019).

In early U.S. history, leading patriots and political leaders, such as Alexander Hamilton, Thomas Jefferson, and James Madison, were in favor of using import tariffs in support of U.S. manufacturing development and to help fund the public debt (Magness, 2023). An early statement endorsing this appears in Hamilton's Report of Manufactures in 1791. (Irwin, 2024). Jefferson and Madison were in favor of more restrictive trade measures, particularly those aimed at Great Britain (Halloran, 2019). These measures were embodied in the Embargo Act of 1807, which was designed to force Great Britain to relax its restrictions on U.S. trade (Staff of Wikipedia, 2024).

It is apparent that throughout the 20th century U.S. trade policy was essentially a case of "economic nationalism" motivated not only by a desire to protect U.S. infant industries but also by a sense of economic and geopolitical security aimed primarily at European trading partners. There was a fear of being victimized by European trade policies in general (Palen, 2024).

The most draconian trade policy restrictions occurred under the Jefferson presidency. The U.S. Congress, following the Jefferson initiative, imposed a nearly total trade embargo from 1807 t0 1809. International commerce was essentially closed down, inflicting a heavy cost on the U.S. economy, estimated to be approximately 5% of GDP during this two-year period (Irwin, 2024). U.S. tariff policy remained generally restrictive until the four-decade period from 1830 to1860 when reform measures in Congress produced a secular decline in tariff restrictions.

The most significant U.S. government commitment to trade liberalization during this period was the Compromise Tariff Act of 1833. This enactment reflected a regional tension that existed in the U.S. at the time. The northern states with manufacturing industries to protect predictably favored high tariffs, while the southern states with agricultural exports to protect favored fewer trade restrictions. The west was a swing region, and the region supported the 1833 tariff compromise bill, as the result of infrastructure spending directed at western states financed by the U.S. government. (Irwin,2024). Also see (Palen, 2024).

Examples of the post-World War Two commitment to foreign trade liberalization occurred in the 1960s and1970s. The U.S. championed the expansion of GATT during this period beginning with the Kennedy Round of 1964-1967, which cleared the way for significant tariff reductions. In addition, the GATT Tokyo Round during the 1970s established sanctions against trade restriction measures, including such non-tariff barriers as voluntary export restraints (Harrell, 2024). Also, see (Casey, 2024).

Commitments to trade liberalization continued into the late 1980s and early 1990s with U.S. participation in the establishment of the North American Free Trade Association (NAFTA, the signing of free trade agreements (FTAs) with more than a dozen countries, and the establishment of the African Growth and Opportunity Act (AGOA). (Harrell, 2024). Also see (Halloran, 2019).

Although the 20th century has witnessed a long-term trend toward trade policy liberalization in the U.S., there have been periods of retreat from free trade commitments, particularly in recent years.

Perhaps, the final major chapter in the post-World War Two commitment to trade policy liberalization was the Trans-Pacific Partnership (TPP), negotiated by the Obama administration in 2016, which involved a trade pact between several nations in the Western Hemisphere and Asia (Harrell, 2024).

However, reluctance on the part of the U.S. Congress to ratify the agreement provided evidence that official governments attitudes about free trade were becoming more negative. The final "nail in the coffin" occurred when Donald Trump withdrew the U.S. from the TPP shortly after he took office in 2017 (Solis,1917).

Several factors indicate that Donald Trump's propensity to use tariffs to restrict trade, evident during his first administration, will continue during his second presidency. First, there is evidence that American citizens are becoming more sensitive about job losses relating to imports, which is affecting attitudes about free trade. Secondly, Donald Trump's promise to impose high tariffs on imports from Mexico, Canada, and China appeals to those Americans who do not buy into the "comparative advantage" argument for free trade Thirdly, the growing strength of the Chinese economy which has economic, political, and military implications for the U.S. also leads American citizens to endorse Trump's anti- China trade position (Goldman, 2024). Also see (Pitas, 2024).

3. ARGUMENTS IN SUPPORT OF TRADE LIBRALIZATIION

It is not surprising that a recent survey of U.S. economists reported that 93 percent support free trade and oppose trade restrictions (Lincicome, 2019). Economists, of course, pray at the altar of efficiency, and this is precisely what free trade promotes. If countries are able to produce and export those goods from industries where the countries have a comparative advantage, and import goods where a comparative disadvantage exist, then resources are allocated from inefficient import substitute industries to efficient export industries.

Beyond the global effects on efficiency, international trade, if free, generates consumer gains from imports as cheaper products become available from oversees producers. It is argued that free trade generates “consumer surplus” permitting consumers to afford more essential products by working fewer hours than would be the case in a closed economy (Michaely, 1989). A Peterson Institute study in 2017 revealed that expanded trade between 1950 and 2026 produced significant benefits for U.S. households. During this time span, U.S. GDP per capita increased by approximately $7000, and U.S. GDP per household by approximately $1800. (Staff of Peterson Institute, 2017).

Strong evidence exists to support the conclusion that the business sector in the U.S. has also benefitted from periods of trade liberalization. The opportunity to acquire cheaper raw materials and intermediate products from efficient producers overseas permits a wider profit margin or market expansion by offering consumers cheaper finished goods prices (Shu and Steinwender, 2019).

Because of the benefits of free trade accruing to U.S. businesses, additional positive spillover effects have been captured by U.S. labor. Business expansion has generated more jobs, and business profits, combined with consumer surplus, have increased real wages over the years (Boudreaux and Ghei, 2018).

Certainly, the U.S. is a leader in the global economy in the areas of high technology and corporate managerial skills This not to say, however, that the U.S. leads in all areas of the above. In an era of free trade and free capital flows, there is much to learn by U.S. businesses from imported new technology and up-to-date managerial skills.

The importation of new technology and new managerial techniques in a free trade environment certainly promotes economic growth and development for the importing country. Market expansion is another positive effect of free trade. Producers in importing countries gain access to a larger pool of raw materials and intermediate goods, as well as to a larger pool of potential customers. Furthermore, consumers under conditions of free trade can gain access to a wider variety of cheaper and higher quality goods, thereby stimulating spending and economic growth (Shu and Steinwender, 2019).

4. ARGUMENTS AGAINST TRADE LIIBRALIZATION

In an “Adam Smith “world of perfect competition governed only by comparative advantage in a global economy where governments do not try to manage or manipulate trade for nationalistic objectives, free trade makes sense. However, such a world does not exist and never has. Free trade only works when the international movement of goods and resources occur within a framework of rules, regulations, laws, and customs (Culberson, 1989).

Governments use foreign trade to promote domestic objectives, such as growth, development, employment, and stability. This is often achieved through promoting balance-of-payment surpluses through such policies as exchange controls, local content requirements and subsidies. Surpluses can be promoted by subsiding exports and restricting imports.

Another argument against trade liberalization is the claim that unrestricted trade puts companies from developed countries in direct competition with low wage countries with lower standards of living than in the case of more industrialized countries. The criticism is made that open trade does not necessarily put companies, such as in the U.S., in direct competition with foreign companies on a level “playing field”. Rather, U.S. companies are often in competition with the governments of foreign nations and lose not because of economic inefficiency but rather because of government imposed subsidies and restrictions (Culberson, 1986).

The argument against free trade can also be made against free international capital flows. One cannot assume, for example, that foreign direct investment in manufacturing industries flows overseas because of favorable productivity/wage rates conditions in the labor markets of host countries. Rather, it is not uncommon for U.S. multinational enterprises (MNEs) to export U.S. jobs overseas, attracted by foreign government sponsored subsidies, tax relief, or other artificial incentives. Thus, as the result of this type of capital movement, lower wage countries experience a rise in wage levels and living standards, while the opposite occurs in capital exporting nations (Casey, 2017).

Another argument against free global capital flows focusses on the motivation that some MNEs have in moving operations in ways to escape regulations that reduce profitability. Of course, there are good and bad regulations. Good regulations include those designed to protect the environment and to promote good labor practices.

If MNEs are motivated to move operations to those countries where good regulations are lax or nonexistent, then they are being rewarded for ignoring pollution controls and fair labor practices (Harris, 2004).

In arguing that free trade is bad for the environment, some conclude that MNEs from the industrialized world often find it to be advantageous to invest in lessor developed countries (LDCs), where environmental protection laws are typically weak, leading to local and even global environmental damage. Furthermore, it is also argued that moving goods and resources from the industrialized world to the developing world requires travel over significant distances. It is estimated that approximately 90 percent of such trade use shipping to reach their destinations, which reportedly is responsible for 3 percent of global gas emissions (Magnin and Hansen, 2024). Also see (Harris, 2004).

In reference to the propensity on the part of MNEs to invest in LDCs, there is the argument of hidden "real" costs. Cheap production costs in LDCs often come at a high human cost. In countries lacking in effective labor protection laws, workers are often forced to work under dangerous and inhumane conditions (Magnin and Hansen, 2024).

5. U.S. FOREIGN TRADE POLICY REFORM

As in the case of all policy objectives, U.S. foreign trade policy should be structured to capture the positive externalities of measures and to minimize the negative externalities. Reform measures recommended in this section of the article are designed to promote the above.

The recommended principles/objectives should include the following:

1) Promotion of a free trade global environment in support of those U.S. export industries enjoying a comparative advantage in trade.
2) Use of countervailing duties in response to trade with countries whose governments interfere with the free flow of trade by the use of exchange controls, export subsidies, or local content requirements.
3) Continued support for the strengthening of the World Trade Organization (WTO) pact, particularly in the area of enforcement given the growing concern about the noncompliance of some members.
4) Tax relief support for those import substitute industries, formerly protected by tariffs or other measures that are seeking to transition to other more viable businesses.
5) Tax relief support for U.S. workers who lose their jobs in import substitute industries that succumb to international competition.
6) Offering of assistance to workers in import substitute industries, no longer protected, in the development of new job skills.

In reviewing the history of U.S. trade policy, appropriate policy implementation has been hampered by inconsistent policy formulation. This has typically occurred with political change in the executive branch of the U.S. government, in the legislative branch, or in both. One goal should be to reduce the effect of purely political influences on foreign trade policy formulation as much as possible.

This is not to say that no policy revisions should ever occur. Policy changes may be needed as changes take place in the socio-political and economic environment globally or in the U.S. However, changes should only take place with the aforementioned core principles in mind.

In monitoring conditions that may call for adjustments in trade policy formulation or implementation, ongoing cooperation is essential between the executive and legislative branches of the U.S. government. Ongoing efforts are needed in conducting cost/benefit analyses in the face of new global realities.

8. CONCLUDING THOUGHTS

In the examination of long-term trends in U.S. foreign trade policy, it is clear that the post-World War Two period has witnessed significant trade liberalization efforts, particularly in the U.S. leadership role in supporting the WTO rules-based trading system as well as its institutional predecessor, namely the GATT agreement. The U.S. has also been active in forming bilateral and multilateral trade pacts with its trading partners. This trend is in contrast to earlier periods in U.S. trade policy when import duties and other restrictions were used to protect U.S. infant industries and internal industry growth.

Closer inspection of U.S. trade policy, however, does reveal significant short-term variation around this secular trend. Changes in policy have been particularly apparent when the political winds have changed in Washington, D.C., involving shifts in party dominance either in the executive or in the legislative branch of government (Swanson, 2024). Policy consistency would certainly be promoted if the influence of political pressure could be reduced in policy formulation or reformulation. It is naïve, of course, to expect a significant reduction in the influence of politics on trade policy, given the fact that this issue typically plays a major role in national political campaigns.

Changes in trade formulation or reformulation are not necessarily the byproducts of political pressure. New approaches may be dictated by economic, political, or social conditions globally, including in the U.S. As indicated above in the article, foreign trade policy in the U. S. or elsewhere should not be “cast in concrete “. Policy makers should respond to changes in the times. However, efforts should be made by policy makers to establish a central core of principles, examined above in this article, which would be designed to inject some stability and consistency in the future formulation or reformulation of foreign trade policy.

9. MANAGERIAL IMPLICATIONS

The international trade policies of countries, including the U.S., have important effects on the decision-making of private businesses. Combined with global foreign investment policies, trade policies govern whether businesses deem it to be more potentially profitable to produce at home and serve foreign markets as exporters, to serve the markets as foreign direct investors, or to enter into joint ventures with foreign firms.

Industries with the most at stake with the nature and direction of foreign trade policy, namely, whether the policy is permissive or restrictive, are export industries and import substitute industries. Predictably, political and corporate leaders in regions where there is export dependency favor open trade and trade liberalization using arguments based on comparative advantage and economic efficiency. On the other hand, where young industries are import substitutes, trade restrictions are promoted based on the infant industry argument among other perceived negative externalities of free trade.

10. RECOMMENDATIONS FOR FUTURE STUDY

1) There is a need for future studies in examining the historical interaction of the executive and legislative branches of the U.S. government during the formulation or reformulation of U.S. trade policy.
2) There is a related need for future studies in examining the historical politicalization of U.S. trade policy.
3) Empirical studies are needed in measuring the impact on export industries of periods of trade liberalization in U.S. trade policy history.
4) Empirical studies are also needed in measuring the impact on U.S. import substitute industries of periods of trade restriction in U.S. trade policy history.
5) In support of U.S. labor interests, there is the need for studies that measure the employment effect of trade policy, contrasting periods of trade liberalization with periods of significant trade restriction.
6) Finally, formal cost benefit analyses are needed in examining significant changes in U.S. trade policy over its history.

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