NATIONAL REVIEW

Wilbur Ross Has Made Billions of Dollars, but on Trade He Doesn't Make Sense

A questionable choice for commerce secretary

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President-elect Trump's choice for commerce secretary ticks all of the traditional boxes. He's a successful businessman. He has ideas about how to promote U.S. commercial interests. And he shares his boss's views about international trade.

Of course, those are also good reasons to be wary of Wilbur Ross. His misguided views on trade agreements and the trade deficit, in conjunction with his affinity for protectionism and backroom deal-making, will necessitate our vigilance to protect the economy and free markets from the follies of crony capitalism.

Wilbur Ross has achieved great business success, mostly from acquiring, restructuring, and selling companies. The Harvard MBA's talent for buying low and selling high is not in doubt. But since it's not credible to suggest that a billionaire businessman doesn't know what he's talking about, understanding international trade and its benefits must require an entirely different set of faculties, which he lacks. How else to explain his positions?

Ross believes trade is a zero-sum game between Team USA and Team China or Team Mexico. Exports are America's points; imports are the foreign team's points. The trade account is the scoreboard, and the deficit on that scoreboard means the United States is losing at trade.

In a recent interview, Ross characterized the proposed Trans-Pacific Partnership agreement as a "horrible deal" and elaborated by saying: "There's trade. There's sensible trade. And there's dumb trade. We've been doing a lot of dumb trade. And that's the part that's going to get fixed."

Exactly what Ross means by that is unclear, but apparently he believes trade is won or lost at the negotiating table — a place where the U.S. team is habitually outmaneuvered, in his opinion. It is bewildering to Ross that the United States would cede its economic leverage by negotiating with more than one country at a time, empowering the other parties to band together, pool resources, and resist U.S. pressure.

But that's an inaccurate reflection of the nature of trade negotiations. Each government comes to the table with a set of objectives, along with parameters guiding how far it can go to meet those objectives. Alliances between and among parties form on an issue-by-issue basis, and they tend to be fleeting. As the big dog in almost every negotiation, the United States is usually the most capable of employing these and other tactics to compel parties to agree to its positions.

Ross's preference for bilateral agreements also betrays an ignorance of the nature of production and trade. Nearly all economists, and nearly all of the economics literature, support the view that the ideal is to have more people and more countries — not fewer — connected in a free-trade area. The economic bases for trade in the first place are specialization and economies of scale. Larger markets afford us a more refined division of labor to exploit our comparative advantages so that we may produce more value among us. And they allow unit production costs to decline as producers increase output and allocate their costs over a wider base of customers.

If those concepts are foreign to Ross, he should at least be able to appreciate that a series of smaller bilateral trade agreements, as opposed to a single regional or multilateral agreement, would place larger cost burdens on traders. If we had eleven bilateral agreements with the TPP countries, each with its own set of rules, the costs of record keeping, inventory management, compliance, and trade diversion would be significantly higher than they would be under a single regional agreement with one set of rules.

Still, his preference for bilateral agreements notwithstanding, Ross heaps praise on the Central America Free Trade Agreement. Ross considers it to be America's most successful agreement because the United States registers annual trade surpluses with the CAFTA countries. (Side note to Ross: The United States runs a trade surplus with its 20 free-trade-agreement partners in aggregate.) But, contrary to Ross's views, trade surpluses are neither the objective nor the result of trade policy. They have everything to do with foreign demand for safe, dollar-denominated U.S. assets, and in that sense, the U.S. trade deficit is a seal of relatively good economic health.

In a letter to editor of the *Wall Street Journal* a few months ago, Ross wrote: "It's Econ 101 that GDP equals the sum of domestic economic activity plus 'net exports,' i.e., exports minus imports. Therefore, when we run massive and chronic trade deficits, it weakens our economy." Yikes! Ross isn't the only person who misinterprets the national income identity, but he may be the first commerce secretary to make that misinterpretation his policy North Star.

Of course, Ross was referring to: $Y = C + I + G + X – M$, the national income identity, which accounts for the disposition of GDP. It says that national output is either (C)onsumed by households; consumed by businesses as (I)nvestment; consumed by (G)overnment as public expenditures; or e(X)ported. Those are the only four channels through which national output is disposed.

What do imports have to do with GDP? Why do we subtract M, which signifies i(M)ports? We subtract M because imports are embedded in the aggregate spending of households, businesses, and governments. If we didn't subtract M, then GDP would be overstated by the value of spending on imports. But there is no inverse relationship between imports and GDP, as Ross suggests. In fact, there is a strong positive relationship between changes in the trade deficit and changes in GDP.

The dollars that go abroad to purchase foreign goods and services (imports) and foreign assets (outward investment) are matched almost perfectly by dollars coming back to the United States to purchase U.S. goods and services (exports) and U.S. assets (inward investment). Any trade deficit (net outflow of dollars) is matched by an investment surplus (net inflow of dollars). That investment inflow undergirds U.S. investment, production, and job creation. The United States balance of payments has shown trade deficits for 41 straight years — a period during which the

size of the U.S. economy tripled in real terms, real manufacturing value added quadrupled, and the number of jobs in the economy almost doubled, outpacing growth in the civilian workforce.

When asked in an interview about whether his prescriptions for trade policy were protectionist, Ross replied that protectionism is a “pejorative term.” Of course, protectionism has been integral to Ross’s business success. In the early 2000s, Ross founded International Steel Group for the purpose of purchasing several legacy steel mills, including Bethlehem, Weirton, and LTV Steel. He conditioned his acquisitions on both the imposition of steel tariffs and the transfer of steel retirees’ legacy costs from the companies’ books to the Pension Benefit Guarantee Corporation (i.e., U.S. taxpayers). He sold ISG at a large profit to Arcelor-Mittal within two years.

Likewise, Ross was a prominent advocate of textile quotas, which were important to his turning a profit for International Textile Group, essentially a replica of his steel-industry foray.

As commerce secretary, Ross will be charged with helping U.S. businesses clear some of the hurdles they face abroad. But he will also have administrative oversight — which comes with a lot of discretion (read, potential for abuse) — of the U.S. anti-dumping and countervailing duty laws, two of the most prominent implements in the protectionist tool shed.

From the Ross Commerce Department, expect to see a lot of managed trade arrangements “negotiated” under the threat of punitive tariffs. Let’s be vigilant.

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