President Trump's Protectionist Trade Team

A closer look at President Donald Trump's key trade advisors.

Daniel J. Ikenson

January 23, 2017

President **Donald Trump**, who assumed office on Friday, has named three trade critics in his new Administration: **Wilbur Ross** as commerce secretary, **Peter Navarro** as head of the newly created White House Trade Council and **Robert Lighthizer** as US Trade Representative.

The appointments seem to confirm fears that U.S. trade policy is descending into darkness. At the very least, it is reasonable to assume that for the foreseeable future trade policy will be overwhelmingly enforcement-oriented, while trade agreements and other forms of liberalization will be relegated to the doghouse.

Commerce Secretary: Wilbur Ross

President 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.

White House Trade And Industrial Policy Director: Peter Navarro

To those mindful of history and the laws of economics, the appointment of Peter Navarro to head the newly established National Trade Council within the White House is the latest assault on the fundamental premise that public policy should be rooted in fact and reason.

Navarro's misguided views of trade as a win-or-lose proposition and trade policy as an adjunct of warfare represent a dramatic departure from the bipartisan, pro-trade consensus that has guided U.S. policy since the end of World War II.

It's a long-standing tenet of international relations that countries that engage in cross-border trade, investment, and production are less likely to descend into conflagration. Greater interdependence raises the costs — and reduces the temptation — of war.

As the 19th century French business writer **Frederic Bastiat** is reported to have quipped, “Where goods don’t cross borders, Armies will.”

But Navarro, a Harvard-trained, University of California-Irvine business professor, fails to see trade as a mutually beneficial activity between willing parties, which reinforces the ties that bind.

Fallacies about imports and the trade deficit, as well as the myth of manufacturing decline, form the basis for Navarro’s policy prescriptions.

The quest to build “national champion” companies, protect domestic markets from foreign infiltrators, conquer foreign markets, be first at commercializing innovation are all central features of Navarro’s military/industrial policy ideal.

To Navarro, trade isn’t cooperation, but a winner-take-all competition. Trade is a battle between Team America and Team China (or whoever the foreign nemesis may be).

Trade is a zero-sum game, which produces national winners and national losers. There is no room in Navarro’s worldview to accommodate the fact that there is no monolithic national interest, but rather a broad diversity of interests that include import-competing and import-dependent producers, service providers, white-collar professionals, manual laborers, consumers and so on, who benefit or suffer the consequences of policies in different ways.

Tariffs on imported Chinese steel, for example, may benefit U.S. steel producers in the short run, but it hurts far more producers in industries that use steel in their own production, and the costs ripple throughout the economy.

The economic illiteracy that animates Navarro’s policy prescriptions is startling. In a white paper published before the election describing some of candidate Trump’s economic policies, Navarro (and co-author, Wilbur Ross, Commerce Secretary-designate) revealed the central misconception that lies at the core of his global economic worldview.

He wrote: “When net exports are negative, that is, when a country runs a trade deficit by importing more than it exports, this subtracts from growth… The structural problems driving the slow growth in the US economy over the last 15 years have primarily been the investment and net exports drivers in the GDP growth equation.”

But trade balance isn’t the objective of trade policy; economic growth is. Taxing imports would put the economy on the express lane to recession.

Some in the policy and media world are accepting the lemons and preparing to make trade policy lemonade. **Chris Hayes**, the host of MSNBC’s *All In* show recently tweeted, “I get all of the economic arguments for why a 10 percent import tariff would be bad. But I’ll confess I’m curious to see what would actually happen.”

Americans are going to have to be much less cavalier about the direction of public policy in the Trump administration.

On trade, Navarro’s voice will be one among many, so it remains uncertain how his dangerous views will hold up among the other less virulent strains of economic nationalism competing for the president’s attention.

If one assumes that Trump wants the economy to grow and create jobs, there can be no accommodation of Navarro's crazy scheme to eliminate the trade deficit and achieve "balanced trade," which would cause massive capital flight, closure of foreign markets to U.S. goods, economic meltdown, and — hopefully — open revolt by congressional Republicans to neutralize the Trump presidency.

US Trade Representative: Robert Lightizer

Former Reagan administration deputy U.S. trade representative and longtime trade-remedies attorney, Robert Lighthizer, is Trump's United States Trade Representative.

For many years, he has represented U.S. steel companies, America's most trade-litigious industry, filing dozens of antidumping and countervailing duty petitions to keep foreign steel out of the United States. Some of the cases in which Lighthizer was involved were brought before WTO dispute settlement, where the panels and Appellate Body ruled that the United States was administering its antidumping law in ways that violated U.S. commitments under the WTO Antidumping Agreement.

Perhaps, as a result of those experiences, Lighthizer has been a strident critic of the WTO's dispute settlement body, which he accuses of overreach and usurpation of U.S. sovereignty. (Here is a debate from 10 years ago between Lighthizer and me on the merits of the WTO.) The fact is that there may be somewhat of a pro-complainant "bias" at the WTO because governments don't bring cases to dispute settlement unless they are reasonably certain of victory. There is a selection bias. When the United States is the complainant, it wins most of the issues in most of the cases. When the United States is the defendant, it loses most of the issues in most of the cases. It just so happens that the United States has had to defend its indefensible antidumping regime many times at the WTO, and in most cases it has lost. Antidumping litigation is Lighthizer's bread and butter.

Lighthizer has advocated for the formal establishment of a committee composed of retired federal judges to review WTO dispute panel and Appellate Body findings that are adverse to the U.S. government's position. While that is not, in and of itself, necessarily provocative, the ultimate purpose of such a committee would be to collect evidence that the WTO has an anti-American bias, which might be used to advocate WTO withdrawal. The Uruguay Round Agreements Act, which was passed by the U.S. Congress in 1994, contains a provision that effectively requires Congress to vote every five years on whether the United States should remain a member of the WTO.

From Lighthizer's view, this process would send a signal to the WTO and its members that if the United States doesn't get its way, it might bolt the system. And that would give the United States some extra leverage, which might deter the filing of formal complaints and add a corrupting political dimension to dispute settlement determinations. Or, perhaps worse, Lighthizer could use his perch at USTR to lobby Congress to vote for WTO withdrawal.

Lighthizer fancies himself a conservative, although he is more aptly characterized as an economic nationalist with deep disdain for free trade. He has argued that true conservatives throughout American history have been suspicious of free trade and favored protectionism. He proudly notes that **Ronald Reagan** – often pegged as a free trader – imposed all sorts of

protectionist measures against imported cars, motorcycles, steel, textiles, and sugar. And all of these measures were "successful," he claims.

Despite conclusions reached after the appointments of Ross and Navarro, USTR's role in formulating trade policy won't be diminished, but dramatically altered. Enforcement will be the mantra and, I suspect, much of the enforcement effort will be directed at China, Mexico, and developing countries alleged to be the destinations for massive amounts of U.S. outsourcing. But the targets may change when the Trump administration comes to realize that most U.S. outward investment goes, not to China or Mexico, but to Europe. Actually, the EU is likely to come under greater scrutiny because Trump and the GOP Congress want to overhaul the tax code, and some of the changes being considered may run afoul of U.S. WTO obligations, possibly prompting complaints from Brussels. Having added leverage to suppress formal EU complaints about border tax adjustments seems like it would dovetail neatly with Trump's approach.

Whether and how long the imbalance between enforcement and liberalization persists will be determined, in part, by how provocative and unilateral U.S. enforcement efforts become. Raising import barriers will have an immediate and deleterious impact on the U.S. economy, especially on manufacturers who rely heavily on imported intermediate goods and capital equipment. Raising those barriers unilaterally – or in circumvention of WTO rules – would likely spark retaliation, which would reduce export revenues and exacerbate the economic damage.

My best guess remains that Trump doesn't want to kill the economy, will eventually recognize the folly of this approach, and will reverse course before too long. But, buckle up. It's going to be a bumpy ride.

Dan Ikenson is director of Cato's Herbert A. Stiefel Center for Trade Policy Studies, where he coordinates and conducts research on all manner of international trade and investment policy. He is coauthor of the book Antidumping Exposed: The Devilish Details of Unfair Trade Law. *This column is based on different columns by Ikenson that were merged and edited by* Latinvex *with permission from the author.*