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Should We Compensate the Winners From Protectionism?

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A common critique of international trade agreements is that free trade can work, but only if we compensate the “losers” from free trade. Along these lines, Paul Krugman recently wrote: “the conventional case for trade liberalization relies on the assertion that the government could redistribute income to ensure that everyone wins.” It may be conventional wisdom among some people that the “conventional case” for trade liberalization involves redistribution, or a promise thereof. But the actual economic case for trade liberalization stands on its own, without any caveats or conditions. You may still favor redistribution, for various reasons, but if your policy goal is to make people better off economically, redistribution is not necessary as a qualifier to trade liberalization. With regard to redistribution, the real question is not whether to compensate any “losers” from free trade, but rather, whether the long-time winners from protectionism deserve extra benefits, beyond those they already received from the protectionism.

To illustrate this, it is important to understand the nature of the choice between free trade and protectionism, and the muddled policy debate that often occurs. Many trade critics are not really arguing that free trade causes job losses. They think they are, but they are not. Instead, what they are actually arguing is that a change in the status quo leads to job losses. Here, the status quo is protectionism, and the change is to free trade. What they really mean is that, after a shift from protectionism to somewhat freer trade, some people will lose their jobs.

It may be true that there are specific job losses that result from this change in the status quo (the overall number of jobs does not change much, but particular jobs will be lost), but that misses the point of the policy choice we face. The free trade vs. protectionism debate should not be about disruptions to the economy from changed policies. Changes in the status quo often result in disruption and lost jobs. If we relied on this logic, we would never change any policy, no matter how bad.

Think of a policy you really hate. If you are on the left, maybe it is fossil fuel subsidies. If you are on the right, maybe it is ethanol subsidies. Each of these policies benefits particular groups. If we abandoned those policies, these groups would “lose” something. Should they be compensated for their losses? Most people would say, “Of course not, they should just be thankful for all the subsidies they got over the years!”

In trade policy, the same logic applies. Removing protectionist trade barriers will result in some “losers,” in the form of groups who no longer benefit from the protection. But there is no reason to give them compensation for eliminating the special favors they have been given over the years.

To demonstrate further the flawed logic of focusing on changes to the status quo, think about the reverse situation. If you had free trade, but switched to protectionism, there would be many losers (more than the other way around). But no one who criticizes free trade ever mentions the issue of compensation for the losers when new protectionist measures are put in place, as they often are (through anti-dumping or safeguard measures for example).

Thus, instead of obsessing about changes to the status quo, and the withdrawal of special favors given to particular interest groups, we need to confront the choice between free trade and protectionism directly. The issue is the underlying merits to the policy choice: Which makes us better off, protectionism or free trade?

When you consider the issue this way, it is clear that free trade is better for society. The benefits of free trade far outweigh the costs. By contrast, protectionism is the reverse. The costs outweigh the benefits, as even Krugman acknowledges: “protectionism in general should reduce efficiency, and hence the economy’s potential output.” Yes, it should and it does, and thus we should not adopt protectionism as a policy, and international agreements to reduce protectionism make us better off.

Of course, economists will continue to debate the precise amount of trade liberalization’s benefits, without any resolution. That is a noble task, one they should continue pursuing. Economists’ debate over the answer, however, does not undermine the case for free trade.

So do not be fooled by trade critics’ efforts to distract you from this clear conclusion, as they point to specific people harmed by a switch from protectionism to free trade. Yes, if you suddenly withdraw tariffs, or subsidies, or any special interest favors, those special interests will be harmed. That is not in doubt. But that is not the question we should be asking if we care about overall societal welfare. If the question is, are we better off as a society with free trade or protectionism, all the arguments and evidence point to free trade as the answer.

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