AFTER THE KENNEDY ROUND: ALTERNATIVES FOR U.S. TRADE POLICY

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FOREWORD

Edward G. Posniak, Chief Economist of the United States - Japan Trade Council since 1961, died suddenly of a heart attack on January 20, 1968. The accompanying article, reprinted from the February 1 issue of the Journal of Commerce, gives some indication of the high esteem in which Mr. Posniak was held by those familiar with his efforts over the years on behalf of a liberal trade policy.

In the fall of 1967 the U. S. - Japan Trade Council submitted to the Senate Finance Committee a paper written by Mr. Posniak entitled, "After the Kennedy Round—Alternatives for U. S. Trade Policy" which we believe made a useful contribution to an understanding of the damage to the economy which would result from the adoption of protectionist trade policies. The Finance Committee has recently published this paper as part of its over-all review of U. S. trade policy, and it is reproduced herein exactly as printed.

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Newsletter

World Trade

Economist Posniak Slashes Through The Rhetoric on Protectionism With a Single Question

—WASHINGTON

Reams of reportage and analysis have been written in recent months on "protectionism"—its good and evil, depending on the vantage point.

Among those who believe it hardly a fit policy for the United States, nobody—as far as we are aware—has put the argument with more telling logic than Edward G. Posniak, in a paper filed recently with the Senate Finance Committee.

Mr. Posniak, chief economist of the U. S.-Japan Trade Council, took a long, broad view and then knifed through all the rhetoric with, in effect, this question—how can those seeking special protection rationally claim the United States cannot compete with foreigners when at the very same time they dismiss the threat of foreign retaliation because the United States has just too much to offer the world?

It is one of those quick, startling comments that take you back because it was there all the time, unseen. It was another Ed Posniak analytical gem.

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Several Groups Active

There are several associations active here in the foreign trade field, on both sides of the fence. The U. S. - Japan Trade Council, the largest staffed, possibly is also the most active and effective. For instance, it was the group that ignited the effort that led to defeat of a potentially dangerous "Buy American" bill in Pennsylvania.

As the council's chief economist, Ed Posniak conceived the broad policy papers and the wide array of informative pamphlets the council publishes on major foreign trade matters, especially as they relate to the United States and Japan.

The last paper Ed authored has not yet been generally circulated. It was the one in which he posed the protectionist philosophic dilemma for the Finance Committee. More broadly, it dealt with a question on many people's minds now—"After the Kennedy Round — Alternatives for U. S. Trade Policy."

Ed concluded that there were three basic possibilities—protectionism, regionalism or a multilateral, nondiscriminatory trade policy under the auspices of the General Agreement on Tariffs and Trade (GATT). He chose unhesitatingly for the third.

Stake in 'Third World'

He reasoned that the broad, liberal approach is inherent to the U. S. national interest for economic as well as political progress. Protectionism obviously implies isolationism, and regionalism, he said, ignores the "imperative of universality" — that this country is both an Atlantic and Pacific power, a good neighbor to south and north, and that it has a vast stake in "the third world."

Mr. Posniak throughly endorsed proposals that the United States soon launch into new international trade negotiations, because, he said, this clearly would advance the U. S. national interest.

The United States, he stressed, has more to gain than lose in future negotiations for removing nontariff trade barriers and to promote agricultural trade.

This is so because the United States has relatively fewer nontariff barriers than other countries, especially those in Europe. And the United States is by far the largest exporter of agricultural products in the world.

Such evident common sense in a world too prone to bluster and obscurities.

Many here will miss the late Ed Posniak, the man and his thought.

R. L.

COMPENDIUM OF PAPERS ON LEGISLATIVE OVERSIGHT REVIEW OF U.S. TRADE POLICIES

COMMITTEE ON FINANCE
UNITED STATES SENATE
RUSSELL B. LONG, *Chairman*

AFTER THE KENNEDY ROUND—ALTERNATIVES FOR U.S. TRADE POLICY

(By Edward G. Posniak, chief economist, United States-Japan Trade Council)[1]

SUMMARY

Following the successful conclusion of the Kennedy round there appear to be three basic alternatives for U.S. foreign trade policy:

(1) Forward to freer trade on a multilateral and nondiscriminatory basis—a direct continuation of the U.S. trade policy since 1934.

(2) Sideways toward regionalism and the "sphere of influence" concept—a radical departure from established trade policy.

(3) Backward toward protectionism—a reversion to the Smoot-Hawley era of trade contraction and economic nationalism.

The first course means concentrating on nontariff trade barriers, where a bare beginning was made in the Kennedy round; on agricultural trade; on greater access to industrialized markets for the underdeveloped countries; and perhaps on freer trade in sections dominated by multinational corporations. These are more in the national interest of the United States than of any other country.

Regionalism ignores the United States interest in Asia and Africa and is incompatible with the position of the United States as a world power.

A return to protectionism would invite retaliation and trade war; would promote domestic inflation and discourage economic growth; and would adversely affect the U.S. balance of payments.

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[1] Mr. Posniak passed away on Jan. 20, 1968.

The only trade policy that makes sense for the United States is a multilateral and nondiscriminatory policy under the auspices of GATT.

STATEMENT

A negotiation as complex and protracted as the Kennedy round, involving so many different commercial, economic, and political facets, is obviously difficult to evaluate in simple terms. Yet the sixth round of tariff negotiations under the General Agreement on Tariffs and Trade (GATT) was a very significant achievement from several points of view.

The fact that, contrary to earlier pessimistic expectations, an average tariff cut of 35 percent was achieved with respect to some $40 billion of world trade is certainly an impressive accomplishment. Tariffs will be reduced, over a 5-year period, on a much larger proportion of the world's dutiable trade than in any of the five previous GATT rounds of tariff negotiations. Particularly important is the fact that the tariff cuts of the Kennedy round will minimize the discrimination against U.S. exports involved in the common external tariff of the European Economic Community (EEC).

In contrast to earlier GATT negotiations, the Kennedy round was conducted on a "linear" or across-the-board basis, rather than on an item-by-item basis. This was the breakthrough in negotiating technique that was largely responsible for achieving as high an average tariff cut as 35 percent. Had it not been for the many exceptions made for so-called sensitive import items (like textiles, for example), an even higher average tariff cut would have been possible, approximating the 50-percent reduction authorized in the Trade Expansion Act of 1962.

Again in contrast to the previous GATT negotiations, which were confined to tariffs, the Kennedy round took at least the first steps in dealing with the problem of nontariff trade barriers. In this context the International Antidumping Code and the abolition of the American selling price and of the European road taxes are of particular significance. In tackling nontariff barriers for the first time, the Kennedy round pointed the way to what is clearly the main task of trade liberalization in the years to come. For as tariff levels are progressively lowered and reduced in significance, nontariff barriers become proportionately more important. And, it might be added, interest groups increasingly tend to seek protection in the form of import quotas and other nontariff devices.

It is true that, except for the International Grains Agreement, the Kennedy round's results in liberalizing trade in agricultural products were somewhat less than had been hoped for. This was a direct result of the fact that agriculture in virtually ever country of the world is a highly protected and fairly rigidly controlled sector of the economy, more for social and political reasons than for purely economic ones. In particular, the common agricultural policy painfully hammered out by the six EEC countries is an inward-looking and restrictive kind of policy. Its variable import levy on agricultural imports from outside the EEC is an essentially protectionist device, aimed at maintaining domestic production regardless of world market patterns.

This shortcoming of the Kennedy round with respect to liberalizing agricultural trade, however, only increases the importance, from the

standpoint of the U.S. national interest, of proceeding on the road to further trade liberalization. As in the case of nontariff trade barriers, it is clearly not an argument for standing still or going back but, on the contrary, for pressing ahead. This is equally true with regard to trade with the less developed countries, which view the results of the Kennedy round as falling short of their expectations.

The most widespread criticism of the Kennedy round in this country has come from import-sensitive industries—largely those labor-intensive industries which are least efficient and thus least competitive in world trade, in terms of comparative advantage. The criticism, largely emanating from sources claiming increased import competition, is that the United States has failed to obtain full reciprocity in the negotiation; that is, that it has actually been the loser in terms of tariff concessions granted and received.

It is interesting to note that the same criticism of alleged lack of reciprocity and potential damage has been heard with equal vigor in other countries that were our negotiating partners in the Kennedy round. Surely, if the United States had struck as bad a bargain as some critics maintain, our trading partners should have been unanimously delighted by the results. In point of fact, a reading of the foreign press (notably the European press) indicates that they have not.

As the Morgan Guaranty Trust Co.'s survey for September 1967 concludes:

> The Kennedy Round's true claim to success is not expressible in quantitative terms. The essence of the achievement rather is that the Geneva negotiators succeeded in restoring forward momentum to the international march toward freer world trading conditions that began three decades ago. And multilateralism was urgently in need of just such a boost, since for more than a decade the most dramatic innovations in trading arrangements have all been bloc-oriented.

ALTERNATIVES FOR U.S. TRADE POLICY

Following the successful conclusion of the Kennedy round there appear to be three basic alternatives for U.S. foreign trade policy. Reduced to their simplest terms, they may be summed up as follows: The first is, in effect, forward to freer trade, on a multilateral and nondiscriminatory basis, under GATT, the General Agreement on Tariffs and Trade. This is a direct continuation of the established policy pursued by the United States since the first Reciprocal Trade Agreements Act of 1934, associated with the name of Cordell Hull.

The second alternative—in effect, sideways toward regionalism and the "sphere of influence" concept—would represent a radical departure from established trade policy. Presumably, it would have to be adopted only if circumstances have changed so drastically as to make our longstanding policy of multilateralism and nondiscrimination unworkable or no longer in the national interest.

The final alternative—in effect, backward toward protectionism—obviously represents a complete reversal of everything this country has stood for in the last 33 years. Its adoption would signify a reversion to the Smoot-Hawley era of trade contraction and economic nationalism, if not isolationism. It would be a clear signal to the rest of the world that the United States has gone back, at least in economic terms, to the concept of a "fortress America."

These three basic alternatives for U.S. trade policy are examined in sequence below.

Since this is the traditional U.S. foreign trade policy, pursued since 1934 and culminating in the Kennedy round, it can be stated in a few words. This policy implies continued multilateral trade negotiations under GATT auspices, involving perhaps a new round of tariff negotiations in 5 years or so, once the tariff cuts of the Kennedy round—to become effective over a 5-year period—have been absorbed and digested. And it is suggested that they will be absorbed and digested with far less of a traumatic impact on domestic industries than the present hue and cry would lead one to believe. This prediction is based on recent experience in both the EEC and EFTA (European Free Trade Association), where the reduction of internal tariffs to zero—as distinct from an average 35-percent tariff reduction over a 5-year period, as in the Kennedy round—has been accompanied by very little dislocation of domestic industries, certainly far less than had been anticipated.

In the immediate future, this "forward policy" would mean concentrating on (1) nontariff barriers, where a bare beginning has been made in the Kennedy round, especially in the International Antidumping Code; (2) trade in agricultural commodities, where the Kennedy round has made only small progress, largely because of the inflexible and restrictive Common Agricultural Policy of the EEC; (3) arrangements with the less-developed countries designed to facilitate their access to the markets of industrial countries, notably in manufactured products; and (4) perhaps moving toward free trade in certain industrial sectors characterized by multinational corporations, large-scale exports, and a high rate of technology in capital-intensive industries.

It should be emphasized that all of these approaches toward freer world trade are more in the national interest of the United States than that of any other country. This is true because this country is the most powerful and most productive economy in the world, because its interests in foreign trade and foreign investments are worldwide, because it has the largest volume of trade and the biggest export surplus of any country in the world, and because, as a result, it has more to gain and less to lose from freer trade than anyone else.

Points (1) and (2) above—the reduction of nontariff barriers and the freeing of world trade in agricultural commodities—are most particularly in the clear national interest of the United States because (*a*) this country has relatively fewer nontariff barriers than other countries, notably in Europe, and (*b*) the United States is by far the largest exporter of agricultural commodities in the world. All of the foregoing would seem to be self-evident and would hardly deserve emphasis, except that the current protectionist offensive has tended to obfuscate these basic truths. This may be a time therefore when, in the words of Oliver Wendell Holmes, "the vindication of the obvious is more important than the elucidation of the obscure."

Sideways toward regionalism

Some students of trade policy believe that in today's world of regional trade blocs, such as the EEC and EFTA as well as the Latin American Free Trade Association (LAFTA) and the Central American Common Market (CACM), multilateralism is obsolete and the

United States should take the lead in forming a free trade area or common market of its own, to be joined by one or another set of countries. Four or five main variants of this idea may be distinguished, although there are others.

Perhaps the most influential school of thought argues for concentration on Latin America, that is, for a modified free trade area of the United States, and the Central and South American Republics. This idea was initially proposed by the late Will Clayton, Under Secretary of State in the Truman administration, who argued for one-way abolition of U.S. tariffs vis-a-vis our Latin American neighbors, at least with respect to agricultural products, on the ground that elimination of Latin American tariffs on U.S. products would expose these countries to intolerable competition. The general proposition of an American free trade area has many proponents, notably among U.S. corporations with extensive investment and trade interests in Latin America. It suffers from at least one serious defect: most Latin Americans themselves do not want it, fearing domination by the "colossus of the North." Another drawback is that a free trade area confined to certain products (in this instance agricultural products) would not be compatible with the provisions of GATT with respect to customs unions.

Another influential school of thought looks north rather than south and favors a free trade area between the United States and Canada. It points to the recent United States-Canadian Auto Agreement as a step in the right direction and recommends its extension to other industries. The foremost proponent of this idea today is David Rockefeller of the Chase Manhattan Bank, as well as the American-Canadian Committee of the National Planning Association. The notion suffers from the same defect as the proposed free trade area with Latin America: few influential Canadians will really want complete free trade between the United States and Canada, fearing domination by the "colossus of the South." Again, to be compatible with GATT, the customs union would have to cover trade in all products and could not be confined to certain industries, as advocated by most of its proponents.

A somewhat broader version involves, in addition to the United States and Canada, the United Kingdom and perhaps the rest of the EFTA countries (Austria, Denmark, Norway, Portugal, Sweden, Switzerland, and perhaps Finland, which is an associate member of EFAT). This idea was propounded at a recent United States-United Kingdom-Canadian meeting at Ditchley (England). One of the weaknesses of this proposal is that the British circles favoring it are not influential. More important British elements see it not even as a second-best solution in the event their current attempt to join the EEC fails. The Government of the United Kingdom as well as its leading economic interest groups, as represented in the Confederation of British Industries, are clearly committeed to this latter course, come hell or high water or General de Gaulle.[1] The proposal of the United States-

[1] This statement of fact does not imply that the author views Britain's entry into the EEC as being necessarily in the U.S. national interest. For one thing, Britain s entry into the EEC—followed presumably by Ireland, Denmark, Norway, and Austria, if not other EFTA members as well—would clearly extend the area of trade discrimination against U.S. exports by an enlarged EEC. Even the assumed political benefits of such a fusion of EEC and EFTA, in terms of a stronger, united Europe linked with the United States in an "Atlantic partnership," seem at best debatable. If such benefits were realized, France under de Gaulle would clearly never stand for it. If unrealized, the trend may well be away from the United States, toward Europe as a "third force."

United Kingdom-Canada free trade area under present circumstances is, therefore, totally unrealistic.

Finally, some would broaden the free trade area concept still further, to include the United States, United Kingdom, EFTA, Canada, and perhaps Japan. What this amounts to, of course, is an anti-EEC trade area, involving more or less open trade warfare against the European Community. What such a rift between "the Anglo-Saxons"—to use General de Gaulle's favorite term—and the heartland of Western Europe would do to the U.S. foreign policy of NATO and the Atlantic Alliance can be left to the reader's imagination. But in addition such a free trade area would clearly be regarded by the developing countries as a "rich man's club," thus accentuating still further the rift between the industrial north and the underdeveloped south of the world and negating U.S. influence in the "third world."

All of the above alternatives, except perhaps one version of the last one, have one thing in common: they ignore Asia. They also appear to ignore Africa, presumably leaving it to become the private preserve of the EEC. In his recent testimony before the Subcommittee on Foreign Economic Policy of the Joint Economic Committee, former Under Secretary of State George Ball implicitly favored this "sphere of influence" approach as the most realistic course of action, suggesting that the United States should treat Latin America as its area of major interest, while leaving Africa to the EEC.

It is not necessary to argue the merits of a sphere-of-influence policy versus a global policy to demonstrate the incontrovertible fact that the United States is not a power whose interests are confined to Latin America or Canada or even Europe. It is also a Pacific power, and it has definite economic and political interests in Africa. Again, one need not get involved in the current debate over "overcommitment" to agree that none of the free trade area proposals discussed fit the reality of America's role in world affairs. Only a multilateral trade policy fits the requirements of U.S. foreign policy, with its many interests in all parts of the globe. There are sound foreign policy reasons why the United States has pursued this multilateral policy for the last 33 years. There appear to be no cogent reasons why it should depart from it now.

Perhaps a word should be said at this point about one other alternative approach, although it has received far less consideration than the ones discussed and is not a free trade area or customs union, as are the others. This is the idea of an Asian-Pacific Community, advanced by Japanese Foreign Minister Miki and advocated in this country by Representative Richard Hanna of California, among others. The salient fact about this proposal is that its proponents do not regard it as another trade bloc, either in the form of a common market or of a free trade area.[2] Instead, they view it as a community for the economic development of the underdeveloped countries of Southeast Asia, using the capital and technology of the area's advanced countries; namely, the United States, Canada, Japan, Australia, and New Zealand. As a

[2] This was made quite clear in the address by the Chairman of the Japanese Economic Mission to the Midwest, Mr. Kikawada, delivered in Washington on June 30, 1967: "When we speak of a Pacific Community, we emphatically do not mean an inward-looking and restrictive trading area, tending to divide the world still further into rival trade blocs. Regional cooperation through trade and aid, mutual assistance and self-help, joint investments, and other forms of economic cooperation—this is what I have in mind when I speak of a Pacific Community."

result, this proposal does not suffer from the inherent vice of all the others; that is, that of being an exclusive, divisive, and discriminatory trade bloc.

The discussion so far has been centered primarily on the foreign policy aspects of the various free trade areas proposed. What about their economic impact on the trade of the United States? A recent study at Michigan State University[3] sheds some light on this subject, though the projections are necessarily highly conjectural. Comparing the effect of alternative trade arrangements on U.S. external trade, the study arrives at the following summary table:

[In millions of dollars]

Trade arrangement	Change in United States		
	Imports	Exports	Trade balance
Atlantic free trade area (AFTA)	+2,183	+2,488	+300
European integration	----------	−450	−450
AFTA without the EEC	+1,500	+1,900	+400
50 percent MFN tariff reduction	+1,150	+1,300	+150

The Atlantic free trade area, as visualized in this study, comprises the United States, Canada, the EEC, EFTA, and Japan. "European integration" is defined as a merger of the EEC and EFTA. The difference between this alternative and the next (an Atlantic free trade area without the EEC) is that the latter contemplates a free trade area between the United States, Canada, EFTA, and Japan, whereas the former does not. As to "50 percent MFN tariff reduction," it means the kind of multilateral negotiation concluded in the Kennedy round, except that its average tariff cut was only about 35 percent.

These calculations indicate that an Atlantic free trade area, with or without the EEC, would tend to have the most favorable impact on the U.S. trade balance, while European integration as such would probably exert the most unfavorable effect. While the gain to the U.S. trade balance from a 50-percent tariff reduction under the most-favored-nation clause would be more modest, it should be noted that the increase in U.S. imports under this alternative would also be far smaller than in an Atlantic free trade area, especially one that includes the EEC. Thus, a 50-percent MFN tariff reduction would presumably require far less domestic adjustments and encounter less protectionist resistance than an Atlantic free trade area.

As the author of the MSU study is at pains to note, "the effect of a certain policy on the U.S. external trade position is not the paramount factor in determining its desirability." He correctly emphasizes that "the choice among available alternatives will probably rest mainly on political considerations."

As the previous discussion indicates, none of the free trade area proposals advocated in recent years meets the requirements of U.S. foreign policy; that is, the imperatives of avoiding a split between America and Europe, of taking into account U.S. national interests in Asia, Latin America, and Africa, and of preventing a still larger gap between the advanced industrial countries and the third world.

[3] "Alternative Commercial Policies—Their Effect on the American Economy," by Mordechai E. Kreinin, MSU International Business and Economic Studies, 1967, especially p. 74.

Backward toward protectionism

Back to protectionism after 33 years of successful efforts at trade expansion through a liberal trade policy, culminating in the success of the Kennedy round, seems on the face of it like an inconceivable if not an irrational alternative from the standpoint of the U.S. national interest. And yet it is frighteningly clear today that it might be adopted by default unless the current protectionist onslaught against freer trade is decisively defeated.

To be sure, virtually no one explicitly advocates a return to the Smoot-Hawley era. Proponents of restrictive legislation merely seek to "help" the particular segment of industry or agriculture in which they are interested against import injury, real or imagined. They generally profess merely to seek an "exception" for their particular industry, leaving trade policy in general otherwise unchanged. But the number of commodities involved in the pending quota bills (which have been estimated by the President's special representative for trade negotiations to affect some $12 billion worth of imports, or almost half the U.S. total) makes it quite clear that these "exceptions" would become the new policy.

It is true that these bills generally seek import quotas rather than high tariffs. But most economists agree that quotas are far worse than tariffs because they distort the normal patterns of trade and do not permit market forces to operate freely. As Prof. Gottfried Haberler, of Harvard, has said, "Anyone who asks for * * * quotas * * * in effect asks for Government handouts and, whether he knows it or not, demands the replacement of the businessman and market forces by public officials and Government fiat." [4]

In fairness to the proponents of import quota legislation is should be noted that some of them explain it in terms of reaction against damage suffered by American exporters at the hands of the EEC, notably on account of its variable levy on agricultural imports. To this extent one should perhaps refer to them as "neoprotectionists" as distinguished from the old-fashioned variety.

But how realistic is this neoprotectionist school of thought? Do they really believe that the enactment of massive quota legislation by this country would show the EEC the error of its ways and convert it to a more liberal trade policy? Clearly, the likely outcome instead is a wave of retaliation by the EEC, as indicated by the notes of protest already lodged by all six EEC countries with the State Department. This, surely, is a prescription for an all-out trade war between America and Europe, which would make the famous "chicken war" of a few years ago seem like an insignificant trifle.

If the neoprotectionists are in earnest about wanting to achieve a more liberal trade policy abroad, and especially on the part of the EEC, the way to go about it is surely by embarking on a new round of negotiations aimed at nontariff barriers. If the neoprotectionists prefer retaliation to negotiation, one must ask whether their references to the iniquities of the EEC are a rationalization for protectionism of the old-fashioned variety.

That this reactionary trend back to Smoot-Hawley should emerge in the wake of the most far-reaching and successful round of GATT negotiations ever conducted may seem, at first sight, paradoxical. But it is precisely the fact that these negotiations are concluded, together with the fact that the negotiating authority of the Trade Expansion Act has expired, which gives the opponents of freer trade a field day. Protectionist lobbies appear to have labored long and hard to nullify the tariff reductions achieved in the Kennedy round by means of import quotas. On the sound strategic principle that one should yell before one is bitten, they have been pushing restrictive proposals long before they are feeling any damage from tariff reductions—much less before they can document such damage.

[4] Meeting Foreign Competition at Home and Abroad, Proceedings of the First 1961 Economic Institute, Feb. 15, 1961, Chamber of Commerce of the United States, p. 13.

So much for the origins of the current protectionist counteroffensive. What about its probable consequences? The most obvious and likely result of a U.S. relapse into protectionism is the prospect of retaliation from abroad. In recent weeks every one of our major trading partners—the EEC, the United Kingdom, Canada, the Scandanavian countries, Japan, Latin America, and so forth—has explicitly warned the United States that if the import quota bills were to become law, they would have no alternative except to retaliate against us. And under GATT, they would have a perfect right to retaliate (or seek compensation) for injuries suffered, just as the United States retaliated against the EEC in the "chicken war" by raising tariffs on French brandy and German Volkswagen buses. As the President's Special Representative for Trade Negotiations has pointed out repeatedly, such retaliation would not be necessarily directed against the industries affected by import quotas—such as steel, textiles and so forth—but rather against those American industries most vulnerable because they are most dependent on exports, which cover a wide range of products from agriculture to machinery.

This process of retaliation would almost inevitably escalate into a trade war—a trade war incompatible with either our alliances or our prosperity. In the thirties this kind of economic nationalism and trade contraction was accompanied by a worldwide depression. Such a depression would be even more likely today, simply because the world economy has grown far more interdependent, as shown by the expansion of world trade, the growth of American investments abroad, and the rise of multinational corporations.

In terms of foreign policy, retaliation and trade war between this country and the rest of the world would inevitably result in the isolation of the United States and the abdication of its world role. It is quite clear that protectionism in economic affairs has as its logical counterpart isolationism in foreign policy. It would be almost impossible to pursue one without achieving the other. Thus, the choice between alternative trade policies is in actuality a choice between conflicting foreign policies. And yet this inevitable correlation has not been clearly recognized and faced thus far; there are many—far too many—voices clamoring for protection but very few, if any, advocating a return to isolationism.

The domestic economic implications of a return to protectionism are equally serious. For one thing, protection breeds inflation because, by impeding imports, it restricts competition, favors monopoly and oligopoly, and drives the price level upward. This is of special importance at a time like the present, when inflationary forces in the domestic economy are again on the upswing. It is of particular significance when basic industries like steel and textiles clamor for protection, since their price levels tend to affect the rest of the economy and since imports thus far have been one of the few restraining factors in their price behavior.

Protection, in addition to raising prices, restricts the free choice of the consumer by limiting the range of imported goods available. Thus, the consumer becomes more than ever the forgotten man—and woman—of the American economy. If the legislative voice of the American consumers were proportionate to their numbers, we would hear less about protectionism and more about the need to keep prices down.

In essence, of course, protection means sacrificing the most efficient American industries—those best able to compete in foreign markets and thus vulnerable to foreign retaliation—in favor of the least efficient, which are to be shielded from competition by import quotas. Such a policy is clearly to the detriment of the Nation's welfare as a whole and of its rate of economic growth in particular. To sacrifice the most dynamic sectors of the American economy for the benefit of the stagnant ones is a recipe for disaster.

Finally, a most important aspect of protectionism is its impact on the U.S. balance of payments. In his letter to the Senate Finance Committee, of October 18, 1967, the Secretary of the Treasury has pointed out that "a country with a large trade surplus is uniquely vulnerable to the adverse effects of a quota war." This is true because of three side effects of import quotas: the feedback effect, the retaliation effect, and the competitive loss effect. As to the first, experience suggests that for each $1 billion reduction in our imports, the United States loses more than $500 million of exports—even in the absence of retaliatory action, simply for lack of dollars abroad with which to buy in this country. The retaliation effect has been discussed above, and the Secretary estimates that "loss of U.S. exports for these two reasons alone might well exceed any reduction in our imports resulting from the proposed quotas." As to the competitive loss effect, imposition of the quotas would encourage higher domestic prices and tend to make U.S. products less competitive in foreign markets. The combined impact of these three side effects cannot be predicted exactly, but the Treasury's judgment is that "the ratio would be considerably greater than one for one." The Secretary concludes: "In summary, the proposed quotas would hurt our trade balance and, therefore, our balance of payments."

In conclusion, the Secretary's letter emphasizes the importance for the United States of "maintaining an open economy—that is, one free from widespread quotas and other barriers to trade." He points out that "we cannot hope to produce in a highly protected domestic market and sell successfully in highly competitive international markets." Herein perhaps lies the crux of the difference between the proponents of a liberal trade policy and the advocates of protectionism: Do we believe in an open competitive economy or do we go back to mercantilism, that is, an economy sheltered, protected, subsidized, and supervised by an omnipotent government?

CONCLUSION

If it is agreed that U.S. trade policy cannot be evaluated except in the context of U.S. foreign policy and the national interest of the United States, then it is suggested that the only trade policy that makes sense is a multilateral and nondiscriminatory liberal trade policy

under the auspices of GATT. It is no accident that this is exactly the trade policy that the United States has successfully pursued for the last 33 years—a period in which U.S. exports have risen from less than $3 billion to more than $30 billion a year, and the U.S. trade surplus from zero to almost $5 billion.

It is evident that the various regional free trade areas proposed—whether oriented south toward Latin America, north toward Canada, east toward Europe, or west toward Asia—fail to take into account the imperative of universality imposed by the requirements of U.S. foreign policy. They all ignore the fact that the United States is both an Atlantic and a Pacific power, a good neighbor to the South and to the North, and that it has a vast stake in the economic stability and political orientation of the third world. For this reason the United States should be the last country in the world to contemplate an exclusive trade bloc with one set of countries or another. Regionalism, if it ever comes to that, would only be a last resort for the United States and it would clearly entail a radical reorientation of U.S. foreign policy.

As to the final alternative—back to protectionism—it is difficult to regard such a trade policy as a serious proposal worthy of earnest consideration. This is implicitly admitted by the proponents of import quotas themselves, because they insist on presenting their proposals in terms of exceptions from a liberal trade policy—exceptions, to be sure, which would become the new policy if even a few of their proposals were to be enacted into law. Protectionism, it would seem, is not so much a reasoned and deliberate policy as simply an accidental end result—the cumulative product of a little protection here and a little protection there. Unfortunately, as experience shows, a little protection is like a little pregnancy.

Since the case for a return to Smoot-Hawley is so weak, it may seem odd that the voices speaking out for protection are so numerous. It is well to remember that in this particular instance the whole is much less than the sum of its parts. What does seem strange indeed is the psychology of protectionism, which combines a queer sense of omnipotence with an even odder feeling of impotence. The sense of omnipotence is evident in the illusion that this country can unilaterally impose quotas on virtually half of its imports and the rest of the world will not dare to retaliate. The feeling of impotence is inherent in the delusion that this country—the most dynamic and productive economy in the world—cannot compete with foreign imports. It is hard to tell which assumption is more quixotic.