The curious case of the protectionist dog that has not barked

By Arvind Subramanian

Good news about the world economy is scarce. Even on trade, Pascal Lamy, director-general of the World Trade Organization, recently rang alarm bells, noting that more than 100 trade-restrictive measures were implemented by the Group of 20 leading nations in the previous seven months.

But these warnings should not obscure the near miracle that is the bigger picture: the absence of serious protectionism in industrial countries in the past decade despite the impact of a huge structural trade shock from emerging markets, especially China.

Recent trade talks have focused on the new initiatives involving the US and Asia (the Trans-Pacific Partnership), the US and Europe (the Transatlantic Trade and Investment Partnership), or on the slow progress in the Doha round.

But all these have overlooked the biggest trade policy story – both a puzzle and a miracle – exemplified most dramatically by the US.

Imports from China surged from 0.5 per cent of US domestic demand in 1990 to 5.2 per cent by 2010. Yet apart from isolated anti-dumping and countervailing actions, such an unprecedented surge did not elicit a significant protectionist response.

Two comparisons from US history can help us understand this puzzle’s significance. The lack of domestic uproar against China contrasts with the heated and acrimonious debate in the US in the early 1990s against the North American Free Trade Agreement with Mexico. And actual protectionist actions against China have been negligible compared with the severity and scope of those taken against Japan in the 1980s.

In other words, in the US the protectionist dog merely whimpered (against China) when it barked loudly (against Mexico) and bit hard (at Japan). Adding further to the puzzle is the fact that the China trade shock was greater by several orders of magnitude than the threat from Mexico or Japan. What should have been a rottweiler has instead been a cuddly Labrador retriever.

There are several possible explanations for this. One is that, by the time of the China trade shock, the US had few unskilled labour-based industries left that were in direct competition with imports from China. For example, the number of workers employed in the US clothing sector declined from 900,000 in 1990 to 150,000 in 2013. So cheap Mexican goods then posed a greater problem than Chinese goods do now.

Another possibility relates to the nature of trade and the power of the trading partner. From a US perspective, trade with Japan was very different from trade with China. The former represented head-to-head competition in specific industries such as steel, cars and semiconductors. Trade with China, on the other hand, was based on differences in skills, with China exporting goods produced by relatively low-skilled workers. When their profits were threatened by Japanese competition, US companies with enormous influence in the political process fought back – successfully – by way of protectionist demands. In contrast, Beijing defanged or co-opted US companies by encouraging them to undertake foreign direct investment in China. As a result, trade actions against the country were opposed by US companies with a stake in the large and growing Chinese market.

Dani Rodrik, the Harvard economist, has argued that sustaining trade requires social insurance mechanisms to cushion the adjustment costs from liberalisation. Research shows that rising exposure to Chinese imports and the attendant impact on the labour market of reduced wages and employment led to almost $15bn of transfer payments from the government, such as unemployment, disability, retirement and healthcare benefits. This may have helped mute any protectionist response.

It is possible that murky forms of protectionism are resurfacing as Mr Lamy has warned. But, for now, the big picture offers some reassurance. If US domestic politics could survive a trade shock as great as that from China – and if the Chinese experience is unlikely to be repeated – perhaps there is cause to be optimistic about the future of trade. The best piece of good news for the world economy in
recent years may well have been the absence of bad protectionist news.

The writer is senior fellow at the Peterson Institute for International Economics and author, with Martin Kessler, of 'The Hyperglobalization of Trade and Its Future'

RELATED TOPICS United States of America, China, Global Trade, US trade, China trade