Book Reviews

Peddling Protectionism: Smoot-Hawley and the Great Depression
Douglas A. Irwin
Princeton, N.J.: Princeton University Press, 2011, 244 pp.

Let me preface this review with a confession: As an advocate of free trade, I love to link the 1930 Smoot-Hawley tariff bill with the Great Depression at every opportunity. More than 80 years after its passage, the bill still evokes negative feelings about protectionism.

After reading Douglas Irwin's *Peddling Protectionism: Smoot-Hawley and the Great Depression,* I can see I need to curb my enthusiasm. Irwin does not defend the bill, far from it. He concludes that it failed to achieve its objectives and that it did, in an incremental way, make the Great Depression worse. But in the careful language of the professional economist and historian that he is, Irwin documents in rich and often colorful detail that the most infamous trade bill in American history had less impact than either its advocates or its opponents understood at the time or understand today. Even so, the story of Smoot-Hawley offers valuable lessons for today as our politicians seek to craft U.S. trade policy in the 21st century.

Irwin is superbly qualified to write the definitive history of what was officially the Trade Act of 1930. A professor of economics at Dartmouth College, he has authored *Against the Tide: An Intellectual History of Free Trade* (1996), and *Free Trade under Fire* (3rd ed., 2009).

Peddling Protectionism is a gem of a book, both concise and thorough. It offers telling and frequently amusing details and sound

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economic analysis, yet it is readable and accessible for the non-economist. It contains one simple formula and dozens of helpful and illuminating charts, cartoons, and photos. The author tackles the subject in four chapters: on the domestic politics of Smoot-Hawley, on its economic impact, on foreign reaction to it, and finally on its aftermath and legacy.

Many misunderstand the origins of the law. It was not a response to an economic downturn or to lobbying by U.S. industry. It was first proposed in 1928 as an election-year plan by Republicans to appease farmers, who were suffering through years of low commodity prices despite the otherwise booming economy.

In a perennial lesson for modern-day lawmakers, the process quickly became a special-interest feeding frenzy. American manufacturers soon joined farmers to plead for tariff protection no matter how dominant their domestic market share. Vote trading and vote buying were rampant. One of the chief ringleaders was Senator Joseph Grundy (R-Pa.), former president of his state's Manufacturers' Association. As Irwin coolly observes, "Without apology or embarrassment, Grundy implied that any organization that made campaign contributions was entitled to get its money back in the form of a higher tariff on their products" (p. 64).

Throughout 1929 and into the spring of 1930, the bill moved first through the House Ways and Means Committee, chaired by Representative Willis Hawley (R-Ore.), and then through the Senate Finance Committee, chaired by Senator Reed Smoot (R-Utah). The Finance Committee heard from more than 1,000 witnesses, resulting in 8,618 pages of testimony published in 18 volumes. The full Senate alone cast 257 roll call votes on different tariffs, sometimes readjusting the same tariff multiple times. Senator Smoot even targeted the importation of books deemed to be obscene, such as *Lady Chatterley's Lover,* which resulted in the newspaper headline "Smoot Smites Smut."

The final bill, signed by President Hoover in June 1930, was more than 200 pages and set specific rates, almost all of them far higher than before, for more than 3,300 tariffs. The bill's final passage brought, not cheers, but sighs of relief and resignation from exhausted lawmakers. What emerged was one of the ugliest, most unwieldy pieces of legislation in American history.

As contradictory as it sounds, Smoot-Hawley caused a steep hike in tariff rates with but a modest impact on the U.S. economy, whether for good or ill. It raised the average level of tariffs on dutiable imports by 15 to 18 percent, a significant increase that came on top of the tariff hikes in the 1922 Fordney-McCumber bill. The Smoot-Hawley rate hike was then compounded by the ongoing deflation of import prices. Since many of the tariffs were imposed on a per item basis (e.g., 10 cents per bushel), as prices fell, the percentage rate of the tariff rose even further. In fact, as Irwin calculates, the deflationary effects ended up being twice as large as the actual rate changes, resulting in a hike in the average effective tariff rate from 40 percent in 1929 to a peak of 59 percent in 1932.

What mitigated the impact of Smoot-Hawley was the small size of the trade sector at the time. Only a third of total imports to the United States in 1930 were subject to duties, and those dutiable imports represented only 1.4 percent of GDP. Irwin calculates that the tariff bill caused a 5 percent drop in total U.S. imports, not enough of a shock to cause much of a change in the U.S. economy, and certainly not a depression with 25 percent unemployment and a one-third fall in output. Like others, the author attributes the Great Depression to monetary and financial factors.

None of this gets Smoot-Hawley off the hook as bad economic policy. There is no evidence that the bill delivered on its promise of net job creation or a return to prosperity. Even on Keynesian terms it was a net loser because exports fell even more rapidly than imports. Declining foreign income put the biggest dent in U.S. exports, but Smoot-Hawley also deprived foreign exporters of dollar earnings, driving up the value of the dollar and making U.S. exports less competitive. And as Irwin examines in a separate chapter, the bill incited foreign retaliation, which further stifled U.S. exports.

Arguably the worst effect of Smoot-Hawley was the way it poisoned our commercial relations with major trade partners. The bill marked an abdication of U.S. leadership at a critical moment for the world economy. While members of the League of Nations were trying to negotiate a "tariff truce," Smoot-Hawley was interpreted by the rest of the world as a declaration of war.

Tariffs were bound to go up worldwide under the political pressure of the spreading depression, but Smoot-Hawley only accelerated the trend while making the United States a special target of discriminatory trade retaliation. The harshest response came from Canada. Smoot-Hawley was seen up north as a betrayal of the pro-American liberal government and led directly to the election of a conservative government determined to reorient itself toward Great Britain. As a result, Canadian tariffs on U.S. products rose sharply, leading to a big drop in U.S. exports to our top market.

Across Europe, tariffs soared against key American exports such as automobiles, sewing machines, razor blades, and typewriters. The end result: America's share of global trade declined sharply into the early 1930s.

Again, Smoot-Hawley was not the only or even the main reason tariffs rose worldwide, "But the real damage," according to Irwin, "came from the fact that the resentment caused by Smoot-Hawley led other countries to form preferential trading blocs that discriminated against the United States. Discrimination against U.S. goods in export markets, notably imperial preferences, diverted world trade away from the United States and made the economic recovery from the Great Depression more difficult" (pp. 220–21).

Smoot, Hawley, and Hoover were all swept from office in 1932 by the Democratic tide. Determined to change course on trade, President Roosevelt and the new Congress enacted the Reciprocal Trade Agreements Act of 1934. The act authorized the executive branch to negotiate agreements with other countries to reduce trade barriers by up to 50 percent. FDR's pro-trade Secretary of State Cordell Hull signed agreements with a dozen countries, largely reversing the economic and diplomatic damage caused by Smoot-Hawley.

The General Agreement on Tariffs and Trade of 1947 codified the principles of nondiscriminatory trade between the United States and its major trading partners, and within a decade trade liberalization enjoyed bipartisan congressional support. Since Smoot-Hawley, the average U.S. tariff on dutiable imports has fallen from 45 percent in 1930 to less than 5 percent in 2010. For those of us who care about limited government and free markets, that is truly good news.

Irwin offers four reasons why it is unlikely a bill like Smoot-Hawley will ever intrude on trade policy again. First, policymakers have other policy instruments to respond to downturns: farm price supports and unemployment insurance along with fiscal and monetary policy. Second, the regime of floating exchange rates tends to offset any short-term Keynesian kick from trade barriers.

Third, the U.S. economy is much more integrated with the global economy than it was in 1930, which has created political constituencies for continued openness and raised the potential cost and disruption from turning back. A fourth and final reason is that American participation in the World Trade Organization and other trade agreements has built the threat of retaliation into the system and made it less likely that Congress will strike out on its own to unilaterally engineer tariff hikes in response to special interests.

So after reading this fascinating book, my opening confession remains real if half-hearted. As Irwin wisely summarizes (p. 221), "In the end, we can conclude that the stigma of Smoot-Hawley is well deserved. It failed to achieve its domestic goal of helping farmers and it backfired against the United States around the world. It should always be remembered as a warning about the adverse consequences of poorly considered trade policies."

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Robust Political Economy: Classical Liberalism and the Future of Public Policy
Mark Pennington
Cheltenham and Northampton, UK: Edward Elgar, 2010, 320 pp.

Pennington undertakes a needed effort to provide a systematic, analytic critique of recent efforts to discredit what he terms "classical liberal economics." His is effectively the standard but hard-to-sell proposition that prescient impartial counselors—Plato's philosopher kings—have failed to emerge from the development of modern knowledge. In particular, Pennington makes good use of Hayek's radical contrast between the competitive testing of concepts in a spontaneous market order and the construction of solutions by government monopolies. As Pennington's conclusions nicely summarize, skepticism of limited government is high and fostered by those who are seeking rents from intervention. Thus, ideas that committed libertarians see as obviously absurd need systematic debunking for a broader audience. Pennington, therefore, pretends that he is treating serious arguments and confronts them respectfully.

Pennington divides his exposition into two parts. The first tackles four purportedly important challenges to classical liberalism: (1) "new" (actually 1970s) market-failure arguments such as those by Joseph Stiglitz and George Akerlof; (2) the calls of some philosophers for fostering communal discussion; (3) related concerns over "social capital"; and (4) critiques rooted in equalitarian philosophies. Pennington then turns to three policy issues—the welfare state, economic development, and environmental regulation—including discussions of why each of the new interventionist philosophies does not help the case for government action.

Against the market failure argument, Pennington notes that departures from the assumptions of textbook perfect competition do not inevitably imply that governments can fruitfully intervene to improve outcomes. Quite the contrary. He correctly argues that the case against the newer theories becomes stronger when markets are less than perfect. The key departures are absence of perfect information and perfect foresight (or markets to hedge all uncertainties). Pennington recognizes that, in such situations of flying blind, the multiple efforts of private businesses subject to market tests are far more likely to produce good solutions than the single efforts of planners freed from penalty by their ability to tax. Similarly, he criticizes arguments for intervention when success depends on the rise of a network of users as also suffering from unrealistic assumptions about government competence. As a bonus, he correctly dismisses the Richard Thaler-Cass Sunstein idea of libertarian paternalism as another effort to repackage old fallacies about the superior knowledge of "experts."

His second concept of communitarianism denounces individualism for undermining the development of dialogue to generate a consensus on controversial issues. Pennington argues that communitarianism substitutes monopolistic decisions for decentralized ones and imposes high costs of participation on most individuals. He generously ignores the preposterous nature of the concept and is content to argue that the communication can deepen rather than lessen fissures. Issues remain thorny over many millennia because no clear answer is evident. To think otherwise is delusional. Hayek is appropriately cited as presenting the superior view of values emerging spontaneously from numerous individual decisions.

I wondered if Pennington was mischaracterizing those criticized, but a look at journal articles and reviews of the leading books showed that Pennington was correct. He adds that these critics overlook classic liberalism's stress on the virtues of voluntary cooperation. It takes for granted that we must interact with others and that continued interaction requires display of reliability. The communitarians' view of individualism as selfish, asocial decisionmaking is, however, not only presented, but gratuitously and incorrectly called what neoclassical economists believe. Hayek is presented as the savior who spelled out that individuals live in a society and recognize their interconnection.

The third target of social capital is even more delectable—the absurd ideas that the ability of people to interact with each other has demonstrably deteriorated and the government can and should correct this. Pennington takes good advantage of the vacuity of the argument and tellingly explains its faults. First, marketplace participation, contrary to Stiglitz's implicit assumption, is a continuous process so that trust must be earned and maintained. Second, the market allows radically different forms of reaction to rise, persist, decline, and be replaced. Third, choosing winners in institutional design is another task not to be delegated to governments. Fourth, government interference may actually suppress social interaction.

Pennington adds something to the massive debate over income distribution. He starts by a deadpan description of three views of equality. John Rawls, Pennington's first example, alone has inspired a massive literature including Robert Nozick's effort to deny that any redistribution was valid. Pennington well describes how Rawls justifies his difference principle by claiming that it would be chosen by impartial parties to the social contract. My reaction from reading Rawls and his critics is that Rawls designed an imagined meeting of minds to ensure his outcome and, thus, was effectively assuming the result. Pennington suggests that these specifications do not guarantee Rawls's outcome. By adding Ronald Dworkin and Iris Young into the mix, Pennington shows that the definition of what is to be redistributed degenerates into such broad generalities as to be inoperable. Dworkin calls for compensation for lesser competence. Young wants to ensure that alternative outlooks are evenly treated.

For me, simply seeing these viewpoints made their inanity obvious. Pennington dutifully develops the rebuttal that the proposed programs are ill-suited for implementation. An overly long discussion of why these ideas have no chance of acceptance, let alone successful implementation, follows. Pennington turns to discussing the disincentive effects of equalization and the ambiguity introduced by Rawls and Dworkin by recognizing the tradeoff and the need to moderate equality to preserve incentives. Depending on how great are the consequences of redistribution on productivity, these theories can lead to anything from nonintervention to throughgoing massive redistribution (assuming we can agree what comprises the tangible and intangible assets that are to be redistributed).

In treating all three applications (the welfare state, economic development, and environmental regulation), Pennington starts with the classical-liberal viewpoint, turns to market-failure objections, the drawbacks of such attacks, the communitarian complaints and their defects, and then the egalitarian case and its limitations. The first two are easy targets, and Pennington neatly treats them. Environmentalism is trickier, and Pennington falters. Given the inherent weaknesses of the three alternative evaluation principles, the efforts to refute them in all three cases seem repetitive.

The critique of the welfare state shows that the concept encompasses two dubious objectives. First, it tries to lessen inequality. It also makes public things such as housing, medicine, and education that would be better supplied privately. Classical liberals believe that *private* provision of poverty alleviation, health, and education has worked well but public efforts have not. The refutation of market-failure rationales then presents the analytic case for preferring private actions. Poverty aid becomes more direct; the external benefits from education and health care are not large enough to offset the inefficiencies introduced by government intervention. The essence of his communitarian and equalitarian arguments is that their inherent incoherence prevents useful criticism of the liberal case.

His chapter on economic development reiterates familiar points about the failure of foreign aid. He begins by recalling that the theory and practice of development suggest that spontaneous free-market development of supporting institutions leads to sustained growth. The market-failure discussion presents 1950s arguments and their 21st century revivals about the need for simultaneous development of vital institutions. He correctly argues that this applies dubious theories of path dependence from the 1980s. Such theories hold that when networks of institutions and consumers must develop, free markets may lock in inefficient institutional choices. However, evidence of real lock-ins does not exist. The communitarians largely fear the undermining of traditional cultures, which Pennington charitably does not note is intellectual protectionism. Young wants dialogue to eliminate conflicts. Pennington dutifully again develops the case that free-market exchange is workable and centralized-accord design is not. Finally, some egalitarians propose worldwide redistribution.

Pennington counters that given the questionability of redistribution within nations and differences among them, extension to the world is unfeasible.

Analysis of environmentalism is complicated by the difficulties of devising a market solution for any widespread harmful environmental impact, the mendacity with which environmentalists claim crises, their ever-changing positions on the nature of the problems and solutions, and the ineptitude with which governments respond. Pennington's conceptual approach does not fully confront these complexities. The government failure is well noted, the distinction among action areas is too fragmented, and the hyperboles of advocacy are left unnoticed.

The environmental chapter starts with the telling point that environmental policies suffer from the lack of decentralized information to inform decisionmaking. He well develops the point that so-called market-based policies suffer as much as command-and-control regulations from having no knowledge to indicate the proper level at which a control tax or damage limit should be set. He argues that judicious assignment of property rights would be a preferable approach to asserting state control. The distinction among different kinds of environmental problems is made too tacitly. The gamut of included issues that Pennington notes ranges from resource depletion to climate change. He ultimately recognizes that a property rights regime appropriate to controlling climate change is not evident. However, treatment of the other areas is fragmented. Thus, whether resource depletion extends to the realms of minerals and other land uses is not noted despite overwhelming evidence that market solutions are preferable. The nod to arguments that some resources are so plentiful that charges are inappropriate ignores the practical unreality of that assertion and does not connect to his broad point that governments are unreliable. Uncrowded bridges and parks are rare outside economics textbooks. He does show awareness that property-right design solutions can be and have been applied to common pool resources.

Yet another problem is that his treatment of Ronald Coase's classic article on "The Problem of Social Cost" turns to others for discussion of the situation when transaction costs are large. Coase's treatment is superior in noting first that intervention has costs that may exceed the direct benefits of the action and second that given the limitations of government, intervention may worsen the situation. Pennington does note that even democratic governments often adopt environmentally harmful policies such as agricultural subsidies.

The market-failure section presents and answers arguments that the state is needed at a minimum to create and regulate institutional design and that some environmental impacts are too big to treat privately. He responds again that competitive development is preferable to constructivist solutions. A concluding subsection on global warming delineates between the apparent need for global accord and the insurmountable difficulties of reaching such an agreement.

The communitarian section sets up and knocks down the view that certain values are too precious and difficult to measure and are best left to consensus. The invalidity of these views necessarily carries over to environmental virtues.

In turning to equalitarianism, he notes the complaints that the rich pollute more and replies that growth also increases the demand for a better environment, leads to cleaner technologies including ones developed to respond to environmental regulations, and thus allows latecomers to develop both without going through initial pollution and with greater ability to reduce pollution.

Pennington's discussion neglects the much-documented hyperbole that characterizes the environmental movement. It overreaches by intruding into areas such as land use including extraction of so-called exhaustible resources in which markets are clearly superior. The modern history of unjustified cries of concern starts with the Sierra Club's false assertion that dams on the Colorado River would flood the Grand Canyon. The anti-nuclear and acid-rain cases are further examples as are the monstrously wasteful hazardous-waste-site cleanup and the control of arsenic and other unimportant pollutants. The calls on climate-change policy seem similar.

Pennington provides an excellent analytic refutation of these new interventionists. In most cases, this meets the arguments on their own ground. However, I came to my pro-market stance from extended study of public policies. I agree with George Stigler's 1956 observation (in the *Quarterly Journal of Economics*) that theory can prove anything and that only empirical testing can resolve the issues. I am also aware of Mises's warning that the facts can be similarly interpreted. Nevertheless, I am less distressed over Stiglitz's love of models of total empirical irrelevance than over how his extended experience as a governmental insider heightened his devotion to interventionist views that are extreme even in the economics mainstream. As noted, the book's neglect of experience is most telling in the environmental realm.

A less problematic aspect of the book is that, presumably because of its British roots, the regulatory state appears cursorily. Consequently, the demonstrable failures of regulation are neglected. Pennington does have a chapter endnote citing the regulatory failures associated with the 2008 financial panic but pays minute attention to the fiascos regarding network industries at the Federal Communications Commission and in the Microsoft antitrust cases.

Pennington does excessively display the tendencies that have unnecessarily undermined contemporary work in Austrian economics. Rather than agree with Stigler's warning about the limits to what theory can settle or Milton Friedman's reminder that theories are deliberate simplifications to isolate what is essential, Austrians incessantly criticize the unrealism of theory. The book wisely avoids the impulse of Rothbard and his followers to denounce any views less stringent than those of Mises. However, Pennington does drop in too many hints of his discontent with mainstream theory, essentially for simplifying too much.

Pennington's references are valuable, often in unusual ways. In several instances, examining a reference led to much useful additional information. As Pennington notes, the concept of "robust political economy" is not original. The concept traces back to a 2004 article by Peter Boettke and Peter Leeson in the *Journal of Markets and Morality*. It was further developed in a 2006 issue of the *Review of Austrian Economics*.

However, Pennington makes too many dubious assertions. Perhaps the worse is that Chicago economists believe that the economy corresponds to the idealized textbook model (p. 17). That assertion corresponds to nothing I have seen from Chicago economists and conflicts with much well-known Chicago work. Pennington subsequently (pp. 44–45) asserts that the Chicago School's belief in rationality leads to approval, as by Demsetz, of market-generated departures from the assumptions of perfect competition. Pennington optimistically makes a 1948 article by Hayek a precursor of Schumpeter's idea of creative destruction, a 1942 elaboration of ideas he first published in 1924. He surprisingly starts his discussion of economic development by asserting that concerns over the issue have dominated "recent discussions" of classical liberalism.

Despite these drawbacks, the book is a worthwhile introduction to classical liberalism. Certainly, the serious newcomer will benefit greatly. While most of the criticisms of liberalism attacked by Pennington are well discussed and countered elsewhere, he provides a more comprehensive treatment with fruitful use of libertarian thought. This makes the book worthy of attention by committed classical liberals. While it is not for casual readers, the book could serve as the basis of a lively undergraduate seminar.

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America Identified: Biometric Technology and Society
Lisa S. Nelson
Cambridge, Mass.: MIT Press, 2010, 266 pp.

Lisa Nelson's *America Identified: Biometric Technology and Society* is a slow and careful examination of a formidably broad landscape—at least until she springs to her conclusions. Among them: "Individual liberty must be reconceptualized to account for the use of data by individuals for communication, transactions, and networking." It's a scholar's way of saying, "Move over, sovereign individual. Experts are going to handle this."

Nothing about biometrics commands this outcome. Given her ideological choices, Nelson could reach the same result with reference to any modern technology—and many consumer products and services. Indeed, for its titular emphasis on biometrics, the book is very light on the technologies that permit machines to identify humans with improving accuracy.

Nobody could capture all the issues arising from the interplay between biometrics and "society." The book progresses earnestly from chapter to broad-themed chapter, examining security, privacy, anonymity, trust, and paternalism in loose relation to biometrics. Evidence from public opinion research occasionally punctuates the vast expense between an important emerging technology and the philosophical questions Nelson seems to prefer.

The book has insight, or at least a new way of expressing an important insight: Nelson regularly refers to the "currency of personal information," suggesting that personal information is a modern medium of exchange. But calling it "currency" suggests to the liberty-minded reader that personal information is something individuals should have the power to control. Don't be too sure.

Privacy is a central value in debates about machine-readable biometrics (and all other digital technologies). Nelson dabbles with treating privacy as a property-like interest, but finds that this view too often places privacy in opposition to "the attainment of a benefit or a common good." So she casts her lot with another approach, treating privacy as "a dimension of social freedom" that "must be a factor in contemplation of policy." Nelson is channeling Amitai Etzioni, who helpfully demonstrated through his book *The Limits of Privacy* that pulling privacy from its grounding in individual rights hands it over to those who will often subordinate it to "the common good."

Nelson seizes on exceptions in John Stuart Mill's articulation of individual rights and responsibilities to argue for collective decision-making about biometrics. She assumes that the public doesn't know, and can't know, enough to regulate technology, while unnamed others can—for the presumed good of maximizing participation in the information economy. In particular, "The individual can know neither the range of future choices nor the harms to be avoided, making paternalistic intervention an attractive option that has the effect of preserving the common good and individual liberty because it enhances the currency of personal information."

Nelson broaches a host of policy issues where public opinion research shows support for paternalism: identity theft, security against terrorism, and control of illegal aliens. But none of these subjects get the analysis they should receive. She makes no mention of identity theft's roots in a uniform, government-created numbering system. The book is silent on the role of U.S. foreign policy in fostering terrorist blowback or U.S. authorities' routine inflation of terrorist threats. The need for "control of illegal aliens"—and for biometrics to do it—is also an arguable result of "paternal" U.S. government policy.

Would biometrics do anything to help in these areas? What are the consequences if government identification policy aimed at preventing identity fraud rivets people even more firmly to social, economic, and governmental machinery? (I treated this topic in my 2006 book *Identity Crisis: How Identification Is Overused and Misunderstood*). The terrorist discovery problem is not fixed by identifying people en masse. It's done by discovering terrorist plots, after which identifying participants is easy. A biometric national identity system would be another of many overreactions that terrorism seeks. (See *Terrorizing Ourselves: Why U.S. Counterterrorism Policy Is Failing and How to Fix It*.) And "internal enforcement" of immigration law through employer background checks is a policy that has been failing since it originated in 1986. Consider in this regard Cato Policy Analysis No. 612: "Electronic Employment Eligibility Verification: Franz Kafka's Solution to Illegal Immigration."

Nelson has not set out to answer all the justification or implementation issues for biometrics, of course, but the moral standing of various technologies and programs turns on questions like these, and more. Her exploration covers too vast a territory in too short a book.

As a survey of some problems in biometrics and their uses, *America Identified: Biometric Technology and Society* is an able, sincere effort. But it does more to open discussion than to settle any of the debates around identification technologies and programs. Those debates will continue for some time to come.

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