Viewpoint

Murray Weidenbaum and Michael Munger

Protection at Any Price?

WHILE MANY TYPES of federal regulation have been reduced somewhat in recent years, one type has grown in both scope and intensity—restrictions on trade with other nations. Of course, protectionist barriers usually increase in severity during periods of high domestic unemployment, and there is no reason why the recent downturn in economic activity should have been any different. The problem is that the protectionist trend is continuing unabated during the current economic upturn.

In 1981–82, the United States imposed or negotiated higher trade barriers on a wide array of products, including bolts, screws, and heavy industrial fasteners, cement and other road construction materials, numerous carbon and specialty steel products, Japanese light trucks and motorcycles, and textiles and apparel from mainland China. More recently, explicit export subsidies, long eschewed by the United States, were put in place this spring and summer on U.S. wheat, milk, and cheese shipped to Egypt—as a means of retaliating against similar European practices. In June, following a recommendation from the International Trade Commission, President Reagan raised new barriers against a number of foreign specialty steel products such as hardened alloy tool and some types of stainless steel. Meanwhile, Congress continues to entertain the domestic content bill (S. 707 and H.R. 1234), which would require high-volume automakers, after a phase-in period, to produce domestically at least 70 percent of the value of the cars they sell in this country. This requirement would present great obstacles to Japanese auto producers.

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Who Bears the Costs?

Protectionist policies consist of tariffs, quantity limitations (quotas or bilaterally negotiated agreements), and a variety of other regulatory barriers such as "Buy American" laws, discriminatory quality standards, and the trigger price mechanism. These policies are intended to help certain industries and save certain jobs—and, indeed, they may succeed, though only in the short run. But, we should ask, at what cost and to whom? The costs take two forms: protected domestic products become more expensive, and restricted imported products become both more expensive and less available. The largest single group that bears the cost of protectionism—domestic consumers—is probably the group least aware of the costs. After all, those costs are often widely dispersed and hard to identify. Who could track down the ramifications of higher prices of bolts, cement, specialty steel, or even apparel?

Consumers are not the only group bearing the costs of U.S. trade policy. Among the other victims are U.S. producers of unprotected goods, especially producers of goods exported to other nations. They are hurt directly when foreign countries retaliate against U.S. trade barriers, and indirectly when our trade barriers succeed in limiting foreign imports and thereby make it harder for foreigners to obtain the dollars they need to buy U.S. products. Indeed, once the balance of trade readjusts, exports fall by as much as imports. Similarly, some domestic producers are hurt because they have to pay higher prices for protected inputs. Thus, for example, domestic automakers that

use protected steel have trouble competing with foreign automakers that can buy lower-priced steel on the world market. This leads U.S. automakers, like other producers in similar situations, to request protection.

While the costs that protectionism imposes on producers are probably not a trivial component of the total, only the costs borne by U.S. consumers are examined here. The burden that tariffs impose on consumers can be divided into three parts: (1) the tariff revenue itself, which is an explicit tax that transfers funds from consumers who buy the imported product to the government, (2) an implicit tax or transfer of funds from consumers to producers, reflecting the increased prices of protected domestic products, and (3) dead-weight static losses, caused by the misallocation of resources that trade barriers encourage. Quantity restrictions and other regulatory barriers raise no revenue for the government, but do impose both the second and the third of the above costs.

That trade barriers are, in effect, a tax can be seen by realizing that the government could choose to support a faltering domestic industry either by protecting its market from foreign competition or by taxing consumers and subsidizing the industry with the proceeds. In the case of all three forms of protectionism, the transfer to the protected industry is directly from the consumer, rather than from the consumer via government.

Measuring the Costs

The technique we used to estimate the total "hidden tax" borne by consumers was to assemble from the existing literature cost estimates for specific programs, and then to make additional estimates of our own for some tariffs where the required data were available. Our literature search turned up twenty-one studies giving figures for various tariffs, quotas, orderly marketing agreements, and the trigger price mechanism. Our tariff estimates were derived by taking the average U.S. tariff rates after the Tokyo Round of multilaterally negotiated reductions (as estimated by Alan V. Deardorff and Robert M. Stern, *Southern Economic Journal*, January 1983), and multiplying them by total domestic consumption. All estimates were adjusted as necessary to 1980 prices.

The results appear in Table 1—a total of $58.5 billion in costs imposed on consumers in 1980. Two aspects of this estimate should be emphasized.

First, the figure substantially understates what the consumer actually pays for protectionism because the underlying estimates are incomplete. Part of the reason for this is that they reflect the static, or short-run, costs, but not the dynamic costs. And, as Ilse Mintz explained in her pioneering study for the American Enterprise Institute,

> Dynamic costs may, in the long run, far exceed static ones. But they can be measured only on the basis of intensive and detailed studies of each of the industries affected. . . . Such studies are not available, and all one can do is to keep in mind that the static costs . . . are only part of the story [*U.S. Import Quotas: Costs and Consequences*, 1973].

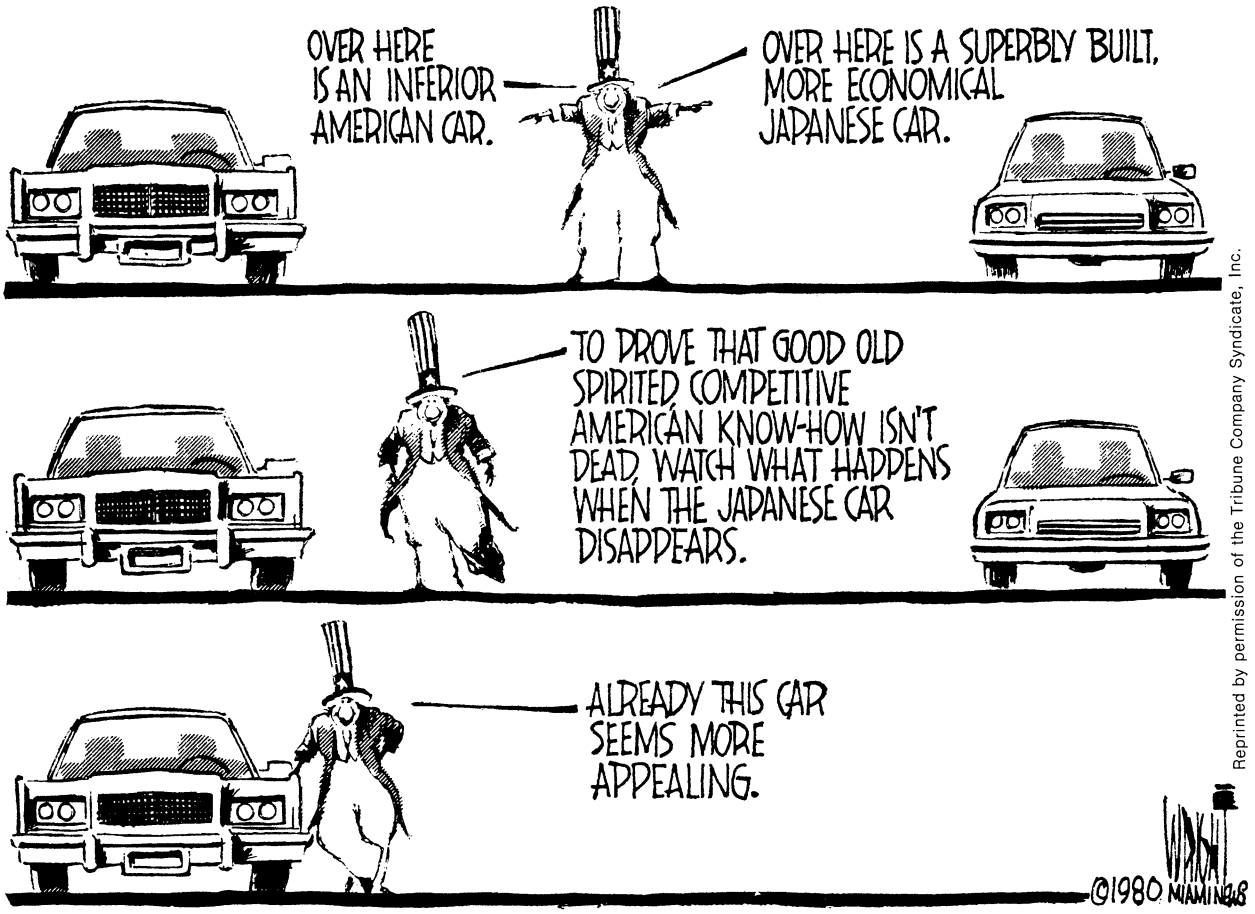
Dynamic costs include losses in capacity, innovation, or productivity that occur when firms are insulated from market forces that give impetus to corrective changes in industry structure and production methods. Trade restraints keep resources in relatively unproductive industries and increase the costs of labor and materials for industries that otherwise would have a higher competitive potential. Any industry that is insulated for a substantial period against the pressure of international markets is likely to find itself far behind its competition, saddled with obsolete methods and equipment.

Table 1

COSTS OF PROTECTIONISM TO U.S. CONSUMERS
(billions of 1980 dollars)

	Types of Restriction		
Product category	Tariffs	Quantity limitations and other barriers	Total
Textiles and apparel	$15.0	$ 3.4	$18.4
Machinery and transport equipment	15.9	—	15.9
Metals and minerals	7.3	2.8	10.1
Other manufactured products	5.5	2.6	8.1
Agricultural	2.1	3.9	6.0
TOTAL	$45.8	$12.7	$58.5

Source: Michael C. Munger, "The Costs of Protectionism."



Our overall estimate is also understated because the static cost estimates are themselves incomplete. They do not include orderly marketing agreements on autos, ball bearings, batteries, dairy products, meat, mushrooms, and tin. Nor do they include building code restrictions on ceramic tile, the fruit juice tariff (averaging 27 percent), "Buy American" limitations on government procurement, and the Jones Act rules on the use of U.S. flag vessels. While the orderly marketing agreement for mushrooms may be a trivial omission, the "voluntary" restrictions on autos, dairy products, and meats create substantial transfers of income. A significant part of this transfer comes about because foreign producers respond to quantity limitations by shifting their exports from cheaper to more expensive goods. Japanese automakers, for example, have stayed within their U.S. quota, while increasing their sales revenues, by exporting to this country larger numbers of higher-priced cars loaded with more accessories. The result is that low-income customers find fewer products available in their price range.

The second point to stress about our overall estimate is that, even though it is incomplete, it represents a significant and little-recognized burden to the consumer. Trade barrier costs of $58.5 billion in 1980 amounted to an implicit per-capita tax of $255 that year—or $1,020 for the average family of four—to protect a variety of domestic industries. If we adjust for inflation but make no allowance for the many protectionist programs that have been

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Turning to some details of our figures, the total tax or transfer associated with tariffs is about $45.8 billion, with another $12.7 billion resulting from quantity limitations and other regulatory barriers. In the product category totals, the largest cost is for textile and apparel restrictions—$18.4 billion, of which only $3.4 billion is derived from quantity limitations. Given that the textile and apparel trade is heavily affected by such quantitative pacts as the Multifiber Arrangement, the figure for these costs would probably be many times larger if they were not so difficult to estimate.

The second largest cost is for machinery and transportation equipment restrictions—at $15.9 billion. This figure does not include any costs at all for quantity restrictions on autos (the most significant omission) and other items, again because of gaps in the existing literature. The metals and minerals category of $10.2 billion includes restrictions on aluminum, copper, iron, steel, zinc, and various other metals and minerals. Fourth, restrictions on miscellaneous manufactured goods include footwear, furniture, stainless steel flatware, glass products, printing and publishing, and myriad other products. Finally, for agricultural products, quantity restrictions contribute more to the cost burden than tariffs: $3.9 billion of the agriculture total of $6 billion comes from quotas and orderly marketing agreements.

The Long-run Costs of "Saving" Jobs

In light of these large costs, it is difficult to understand the popularity of trade barriers as national policy—except in light of the politics of protectionism. All of the protectionist devices are means by which small, well-organized groups use the political process to their advantage. That the tax effects of these devices are hidden is of no small importance in explaining their attractiveness to policy makers and to business. Certainly, direct subsidization of producers leading to increased taxes—or, more likely, to increased deficits—would be very unpopular politically. Protectionist aid to industries facing strong foreign competition, on the other hand, can be rationalized by pointing the finger at foreigners. In addition, such aid does not threaten company managements with the direct government intervention that explicit subsidies would involve.

The ability of protectionist barriers to save jobs is limited and can never be viewed as more than a temporary measure. But the cost is difficult to justify even in the short run. Table 2 gives estimates of the total cost per job "saved" by five protectionist programs. The ratio of the consumer costs for those programs to the compensation paid to workers ranges from 3.5 for carbon steel to 9.3 for restrictions on footwear imports. Put simply, current protectionist policies "save" jobs at a cost to consumers that is many times what a job is worth to the worker being protected. The difference between the compensation paid and the total implicit transfer from consumers goes partly to the owners of the protected firms and partly to sheer waste (because resources are used to produce goods domestically that could be produced more cheaply elsewhere).

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Table 2

ESTIMATED ANNUAL COSTS TO CONSUMERS PER JOB PROTECTED

(1980 dollars)

Product	Average Compensation	Consumer Cost per Job Protected	Ratio of Cost to Compensation
Television receivers (tariffs and quotas)	$12,923	$ 74,155	5.7
Footwear (tariffs and quotas)	8,340	77,714	9.3
Carbon steel (tariffs and quotas)	24,329	85,272	3.5
Steel (trigger price mechanism)	24,329	110,000	4.5
Autos (proposed "domestic content" bill)	23,566	85,400	3.6

Sources: Compensation figures are from Department of Labor, "Labor Force Statistics Derived from the Current Population Survey: A Databook," vol. 1 (September 1982), adjusted to include fringe benefits. Estimates of the consumer cost per job created in television, footwear, and carbon steel are derived from Robert Crandall, in *Brookings Papers on Economic Activity*, 1978; the estimate for steel comes from Crandall, in *Regulation*, July/August 1980, and that for autos from a Council of Economic Advisers staff study.

Moreover, even these very expensive benefits to workers may be short-lived. There is, as already noted, a tendency for trade barriers to proliferate, as firms that sell products in open markets but buy materials in protected markets find they too need some form of protection. There is also the possibility of foreign retaliation. Our trading partners may succumb more readily to domestic political pressures to raise trade barriers if we have increased ours. The devastating beggar-thy-neighbor policies many nations practiced following U.S. passage of the Smoot-Hawley tariff in 1930 should serve as a vivid reminder of the global repercussions of protectionism.

Moreover, in addition to the direct consumer costs estimated here, trade barriers impose high long-run costs on the protected industry itself. Even the benefits of trade barriers to the protected industry are not unambiguous, because an industry that once sought protection as a short-run cure often ends up dependent on it for survival. Finally, and most important of all, trade barriers damage our economy's competitive strength. As William Brock, U.S. trade representative, has said: "Nations which protect their economies today will pay the costs of a decline in competitiveness tomorrow."

IN THE CURRENT ENVIRONMENT, international trade policy will not sit still. Our choice today is between further drift to global protectionism or a joint effort by the United States and its trading partners to remove the obstacles already threatening open world markets. The longer we wait, the more numerous the barriers and the more difficult the task of removing them. ■

Selected Readings

For the methodology and sources underlying the cost estimates, see Michael C. Munger, "The Costs of Protectionism: Estimates of the Hidden Tax of Trade Restraint," Washington University, Center for the Study of American Business, Working Paper no. 80, July 1983. On the politics of protectionism, see Weidenbaum, Munger, and Ronald J. Penoyer, *Toward a More Open Trade Policy*, Washington University, Center for the Study of American Business, January 1983. For cost estimates on autos and steel respectively, see "The High Cost of 'Local Content,'" Perspectives, *Regulation*, November/December 1982, and Robert Crandall, "Steel Imports," *Regulation*, July/August 1980.

Worth Noting–

In 1847, after France put a tariff on all foreign goods to help domestic industry, the economist Frédéric Bastiat responded with this tongue-in-cheek extension of the protectionist principle:

PETITION OF THE MANUFACTURERS OF CANDLES, TAPERS, LAMPS, CANDLESTICKS, REFLECTORS, SNUFFERS, EXTINGUISHERS, AND OF THE PRODUCERS OF OIL, TALLOW, RESIN, ALCOHOL, AND GENERALLY EVERYTHING CONNECTED WITH LIGHTING

To the Members of the Chamber of Deputies

Gentlemen:

. . . We are suffering from the intolerable competition of a foreign rival, enjoying, it would seem, conditions so far superior to our own for the production of light, that he absolutely inundates our national market with it at a price fabulously reduced. . . . [This rival] is none other than the sun. . . .

We demand that you pass a law ordering the closing of all windows, shutters, dormer-windows, curtains, casements, blinds, bull's-eyes, shades; in short, of all openings, holes, chinks, and fissures through which the sun is accustomed to enter houses in detriment to our fine industries. . . .

If you thus create a need for artificial light, what industry in France would not in the end prosper by it? If more tallow is consumed, more oxen and sheep will be needed. . . . If more oil is consumed, then we shall see more cultivation of the poppy, the olive-tree. . . . The same is the case with navigation: thousands of vessels will be engaged in whale fishing. . . . There is perhaps not a single Frenchman, from the wealthy stockholder to the humble matchseller, who would not profit.

Choose, but be consistent; for so long as you exclude, as you do, coal, iron, wheat, foreign textiles, in proportion as their prices approach zero, what a contradiction it would be to let in the light of the sun, whose price already stands at zero the whole day long!