General Discussion: Panel on the Changing Landscape of International Trade

Chair: Susan M. Collins

Mr. Frenkel: In this discussion about the challenges to globalization and about the rise of protectionism, much was said about the failure to carry out the mechanism of compensation. I would like to make three points. First, to increase the understanding of and the support for globalization and free trade, it would be extremely important to point out some examples of success. The positive impact of openness on the standard of living is well documented. In many developing countries, millions of individuals were elevated from poverty due to access to world markets. The damage from protectionism is not confined only to developing countries, but also to industrial economies. The recent financial crisis provides a vivid example on the link between trade and growth. Specifically, in 2009, output in the industrialized countries had shrunk by 3.4 percent—the worst performance of this group of countries. At the same time, the volume of world trade in 2009 had shrunk by 10.5 percent—the worst performance in many years. This correlation should not be ignored by those who advocate protectionist policies that would reduce the volume of trade.

The second point relates to the role of China and its role in the world trading system. China has become an indispensable player in world trade, thereby reflecting the shift in the economic center of gravity toward Asia. To illustrate, during 2017, the volume of trade between China and the rest of Asia has been about twice as large as the corresponding volume of trade between China and the United States plus Europe taken together. Furthermore, China has become the most important trading partner of most of the major industrial countries in the world. For example, during 2017, approximately one-quarter of U.S. and European exports were sold to China. These facts imply that the degree of interdependence within the world economy is very high. As a result, a protectionist-induced disruption to the interrelation between China and the rest of the world, would be extremely costly.

A final note of optimism relates to the recent initiative in China of launching the Asian Infrastructure Investment Bank (AIIB), as it aims to increase the degree of integration. It is encouraging that most of the major countries have joined this multilateral bank, while it is discouraging that at this stage, neither the United States nor Japan has joined this important initiative.

Mr. Furman: I wanted to pick up on something Cathy Mann said and it's been in some of the discussion, which is the role that regional policy does or doesn't play in these. Increasingly in economics, we look at these heat maps and they're always really exciting to look at. We do it in trade; we do it in a lot of other stuff. Then our mind goes to, we need a regional policy for that. Of course, that doesn't logically follow and to give an example with some residents in this room, if we looked at a heat map of bank failures we wouldn't say the conclusion was we needed better supervisors in certain counties than we currently have. That would tell you something about national policy. I am very skeptical that we're going to be able to in practice do these regional policies well, and maybe even that in theory they work. Often we pick a policy for five little places; they cover 1 percent of the country, send politicians off to visit those five places. You've got great headlines; it looks really great, but you've barely done anything for the problem. Two, we often select those five places really badly for political reasons. Three, even when we select them really well, we then stick with those same places for decades long after it makes sense to be focusing on those places as opposed to others. Those are all the practical impediments and they just compound the theoretical public finance considerations around a world of mobility, the incidents being on fixed factors like owners of land and helping rich people in poor places. I think it's really tempting to want to do them. It's worth thinking harder about because Cathy, I think, rightly pointed out some of the limitations of tax and transfer, some limitations of education. But I think we can really fool ourselves and end up doing more harm than good in this space based on what we know right now and how things actually work in practice.

Mr. Kroszner: You talked about the growth of trade over time and we've had some periods where it's grown rapidly, some periods where it's been kind of flat. Do we have a view of what the optimal amount of world trade is?

Mr. Lane: I think that this session and the previous sessions have been fascinating, and there were recurrent observations about the world of adjustment policy. I think there's some mention in some of the papers about Dani Rodrik's generic approach. Let me just emphasize. Where I am, which is obviously a highly globalized economy, and periodically we have had towns where there's been plenty of times where the firm just leaves. Cathy Mann talked about this earlier on. What do you do with these big shocks? I think the experience of Ireland, which I think has been reasonably successful, has been not to have localized responses, but just essentially to have a national education policy. The quality of schooling does not depend on local taxes. It's a nationally funded education system. In terms of redistribution, our kind of unemployment payments are anti-poverty. There's no earnings-related component. It's not the case that people are being paid not to work. But there's a very strong redistribution so the comparison of post-tax income distribution versus pre-tax is quite sharp. Essentially what happens is below median earnings, there's very little tax burden on families who have up to fairly decent income levels, but working families don't pay much by way of net tax. What that means is that from median income onward, the tax burden is pretty stiff. But that's essentially what someone has to pay. Someone has to pay and the equilibrium is that middle/high earners pay a lot of tax. It goes back to some of the discussion of the United States, which I heard here was you need educational policies. But then of course, we know U.S. education, university education is so expensive that you need accessible education. So we have a high participation rate. It's not really in the universities, it's in vocational job training and those institutions just turn on a dime. If the hard disk industry disappears, they stop training people on hard disks and they look for something else. So we've had this trade inequality session this morning, but in the end if we all say education is so central, thinking hard about what that means, I think, is an important next step.

Ms. Forbes: This was a very nice set of presentations to get across the stylized facts of the adjustment to trade, especially building on the last paper by Nina Pavcnik. What stood out for me was that the adjustment to trade is more widespread and longer than many of us had previously believed, even though there are net benefits overall. That leads to what I found surprising. This is a room dominated by central bankers, and in the policy discussion there was a dearth of discussion of any role for central banks. Should we take this as suggesting that central bankers may be interested in these topics on an intellectual level, but there is no role for central banks in helping with these adjustment challenges?

Mr. Spriggs: I want to follow up on that question by rephrasing the question I asked from last time. So Catherine, one of the big issues you brought out was even if we could do the human capital side, we're still going to be left with the physical capital side. And a point that I know you have been very concerned about is, we just haven't seen investment come back, not in the way we would think. There's every chance I believe, if you looked at this from the aggregate perspective (recalling, you had in the United States a massive loss of capital.) from a central banker perspective, if you think that your policy is supposed to effect investment and you've had regions that have had massive loss of capital, what becomes your policy? It seems to me it becomes very complicated because it's not the traditional model of an investment dip because of typical cyclical behavior. (It is a loss of physical capital from the relocation of manufacturing.) So responding by low interest rates to try and get investment back is not the same thing in that environment. I think there should be a discussion about what this does to distort how central bank activity may go forward in trying to respond to what has been for most of this century and particularly since this downturn a very unique problem about investment.

Thank you to all the panels and to the previous panel. The labor costs (the costs borne by workers) are real. I wish that people who do trade would stop saying it's protectionism to be concerned about labor rights. For those of us who have long ago argued labor unions are not anti-global; labor unions are against this form of globalism. You need to envision a different set of rules. So whenever anyone says, "I'm concerned about labor," "Oh, you're a protectionist." These global agreements are very protectionist of capital. No one ever says, "Oh, that's protectionism." Multilateral trade agreements set up a set of common rules that currently protect capital. But, the common rules could include labor. So please do not use the term protectionism when people talk about labor. There are real costs to labor, there are real adjustments, and that needs to be considered. Hopefully from this, it's not just that you say, "Oh, how would you compensate," but how would you think of the rules differently? How would you think that the rules could be constructed to protect labor from unfair competition? How could we have a different set of playing rules? And that's not protectionism. That's a recognition that these are real costs, and if it's not done incorrectly real people pay.

Mr. Kohn: Our discussion so far has concentrated entirely on what the importing countries can do to adapt to this onrush of new manufacturing imports. But some of the issues that we face have been exacerbated by some of the actions of the exporting countries who are not always playing by the rules. I think things like export-led growth through subsidies, through not allowing your exchange rate to appreciate along with rising productivity, with not respecting intellectual property rights, and taking in effect the innovation from one country into another country without compensation is part of the broader problem we'll be discussing tomorrow about how you get surplus countries to adapt as well as deficit countries. But it's not all on the importing countries. Exporting countries have some responsibility to play by a set of rules, and to allow the market to influence rising wages in their country to alleviate some of the problems.

Mr. Blinder: I think a basic problem that we've been facing for a long time, and talked about in different ways by these four excellent presentations, is that we economists think David Ricardo got it mostly right 200 years ago. A lot of other people think he got it badly wrong, and we haven't convinced them in 200 years. I want to make two PR suggestions for our profession, but they have the advantage of being intellectually honest. One is to stop using the term "transition costs" to belittle adjustments and focus more attention on the transitions which are what almost everyone is living in almost every day of their lives, not the equilibrium states. I think that has a PR advantage, and it's also intellectually honest. That's my strongest one. My weakest one, because I'm not sure we can do it, is try to marry technology and trade into the same basket more. I mentioned that we've failed to carry the day with Ricardo's message. The anti-Luddite view of the world has, however, carried the day over the centuries, and I think it still does. Again, it's intellectually honest to marry trade to technology. A lot of trade is driven by technology; more of the disruption we see is driven by technology rather than by trade—to the extent you can separate them. If we would try to pound that point home, maybe just maybe we'd have more success than the abject failure of 200 years to sell comparative advantage.

Ms. Gopinath: It's a really interesting panel. I just wanted to speak to the point about return to protectionism, and while it's true that you've had these techtronic political events, what's interesting is that we don't really see that in measures of tariffs or policy or any changes in tariff policy despite the fact that we've had 10 years of a financial crises and all the problems that have gone along with it. Sure, trade to gross domestic product has slowed down, but there's really no reason to think that that should continue to grow over time. There's no reason to think that global value chains should continue to grow so that we have an increasing share of trade and world GDP. That just is not where we should expect things to go. So in terms of actually whether we're seeing a return to protectionism in terms of actual policies, I think that's going to be harder said than done. If you think of the border adjustment tax in the United States, that policy has quieted down partly because of the fact that there are these global value chains and there are U.S. companies that rely on foreign firms for their inputs and a tax on that is going to be costly for them.

The second point is, I agree with the view that everybody raised that it's very important to scale the labor force and to find ways of job creation. I just want to flag the fact that this is really hard. India has been one of the countries that has had the biggest decline in poverty rates, has been growing at 7 to 8 percent. They've been trying to do scaling and job creation, and that's been one area that has not really done very well.

Mr. Feldstein: Let me first reinforce what Gita Gopinath has said about her doubts about return to protectionism. There's no question that there has been a great increase in protectionist rhetoric. There's a political audience for that, but I don't see it happening in actual policies. Second, I wanted to comment on what Kristin Forbes asked in which she said, is there any role for central banks in dealing with these trade policies? Of course, central banks drive exchange rates, so that's not a general recommendation on my part although it may be appropriate in some circumstances.

Mr. Auerbach: I also wanted to pick up on the question of what the role of monetary policy is. I am recognizing Marty Feldstein's comment about exchange rates. I think the role for monetary policy here is limited, but the pressure on monetary authorities is not. When there is poor wage growth, I think there's a natural tendency to look toward whatever potential policies might be available, even if they are not particularly effective, in promoting wage growth. One can easily imagine that in a country like the United States with disappointing real wage growth certainly for a large share of the population, pressure on the Fed to push toward tighter and tighter labor markets, to push at least nominal wages up. So I can imagine, we hadn't really seen it in recent years, but one could imagine if this continuation of this leading to monetary authorities being under pressure to basically do what other government policies have not been able to do, which is to push for tighter labor markets in the hope of getting higher wage growth.

Mr. Laubach: I think this question is mostly to Cathy because she was talking about the regional aspects. Intuitively it seems logical that the cost of adjustment for those who are losing their jobs would be higher if on top of returning they also need to relocate. In thinking about Jason Furman's examples, let's call them of the discretionary variety, namely that there is a certain flash point—somebody goes there, puts some sort of program in place, and then leaves. I know that the OECD has in the past studied fiscal federalism and I'm wondering whether perhaps a more fruitful way to think about scope for action here is in that context to think more about some sort of automatic stabilizer mechanisms across regions. That might be helpful—I don't know whether there is any evidence. I would be interested in that.

Ms. Collins: I'll make a quick comment which follows up on what Alan Auerbach was saying. It does seem to me that it is important to have a discussion about the role of central banks in this context. And it may be a focus less on monetary policy and more on some of the community redevelopment activities and roles, including the Fed's ability to undertake and disseminate a range of different types of research. Some of that should be at the regional level. While I agree with the concerns Jason expressed related to how much focus one wants to place there, there are clearly regional differences in terms of what the impact has One of my big takeaways from today's discussion is an understanding of an even longer and more persistent set of geographically differentiated impacts than I had previously thought, which I find really striking. I'm going to ask our panelists to take just one minute each to give one or two highlights. Clearly we will continue this discussion over the rest of this session. Ann Harrison, would you like to start?

Ms. Harrison: I agree with all the comments. I think they're excellent, so I don't have much to say. One comment on the slowdown of global trade, is it real? It's not just that trade as a share of GDP has stalled or even declined, as we saw in both Catherine and my charts in the last couple of years, but it's also true that there's been a steady increase in the number of trade-restrictive measures adopted at the country level. And that's actually monitored by the World Trade

Organization (WTO) very carefully. It's not huge, but it's disturbing and it's also accompanied by a slowdown in the number of trade opening measures which is the flip side of that.

As far as cluster policies are concerned—shameless act of self-promotion—I have a book called *The Factory Free Economy* about this trend toward industrial countries no longer having factories. At the end we talk about some policy solutions including cluster policies, and there's a really nice paper by Philippe Martin, co-authors, evaluating the success of cluster policies in France where they show very clearly that cluster policies have not been effective. So that kind of continues along the lines of what Jason and some others were saying.

Ms. Mann: I'll make my comments using the triangle diagram that I had in the final page of my presentation. With regard to the international policies, the global policies that underpin the basic trade relationships, what Bill Spriggs was saying was right, and also Don Kohn. There are a range of international policies where the level playing field is not level, and focusing on leveling the playing field so that firms in different countries are playing by the same rules is a critical component of getting the overall trade environment to be more advantageous for workers in all of the countries. The fact is even if the level playing field was completely level, it is still the case that reallocation is going to take place because of technological change and trade. So we have the problem dealing with the transition regardless, as Alan Blinder would like us to use our terminology now, we have the challenge of the transition even if the playing field in the international environment was perfectly level.

Now the issue about national level policies versus regional policies, the issue that I think is relevant here is that regions are heterogeneous. The shocks that they absorb are also heterogeneous. The observation that we made in looking at our regional data is that the technological shocks and the trade shocks and the consumer preferences shocks are multiplicative and particularly dramatically hit certain regions. Given a situation where trade shocks, technological shocks, and preferences shocks disproportionately hit certain geographies, and population, do you believe that a national policy setting is sufficient to deal with that? And if the answer is, "Well maybe not," then considering how to create an environment where you have both national policies that are supportive of the kinds of transitions and reallocations that are necessary both of human capital and physical capital, and a little top-up somehow to manage the disproportionate costs that are absorbed in certain regions.

Mr. Schott: I also agree that many of the comments were quite good and actually give me a lot to think about. Personally, I'm trying to figure out how to translate some of these questions into what we might do in terms of research to help answer them. For example, I'm trying to develop a project with a development economist that's going to look at the micro level, how can you work with community organizations that are already dealing with workers to figure out experiments that might shed light on what works and what doesn't work, using microdata to try to figure out more in fact about what went on in firms in their investment during this period. I think that's a really interesting issue that might shed light on those kinds of adjustments. Actually, been thinking, I think Ken Rogoff raised this earlier. I live in New Haven, which was devastated in an earlier era. It lost all its manufacturing and it struck me as interesting, like what would we or should we have learned from these earlier eras when all this dislocation occurred that we did or didn't take advantage of in these kind of new things and how we might leverage that going forward. I think that's a really interesting set of issues to look at as well. Then I also agree, I forget now who said it, but with this distinction between trade and technology. Maybe it matters if it's trade and technology to answer some questions; but maybe for other questions like figuring out adjustment it doesn't matter so much; and that dichotomy kind of hampers us in some ways.

Mr. Van Reenen: Two comments. On Gita and Marty's point about the rhetoric of being anti-trade is not the same as the reality, I agree with that. I've been very relieved that there haven't been more increases of tariffs and quotas over the last 10 years than there could have been. But I don't feel very relaxed personally about that. There has been the withdrawal from the TTPA by the president, also the EU-U.S. trade deal is going to fall on the path. I think the problem is that you need to keep up the constant pressure to try and reduce trade costs through different types of things. And if the feeling is against that, then new trade deals and new types of ways of having reduced regulations or better regulations that foster trade is going to mean that that's going to be a problem. The European Union case is an example of this with Britain withdrawing.

Second thing on this local/regional thing that was brought up by many people, including Jason Furman and Philip Lane, I broadly agree that national-based policies are the best way to do this. I've always thought that. But two things to think about. In the U.K., for example, and I think this goes to the Brexit debate. The U.K. is an incredibly centralized place, and all the resentment has been built up over the years of the success of London versus the rest of the country. I think that a greater degree of decentralization toward city regions would unlock local initiative to gain some of the potential benefits from local initiatives. I think that everything in the U.K. case gets drawn away to the center, that reduces those kind of local initiatives. So some degree of decentralization could be beneficial. The evidence on local policies like policies to subsidize and support investments under European regional assistance, there's evidence that that has been relatively successful. That's the kind of investment subsidies for underperforming areas. The work that I've done with the OECD, would suggest that properly implemented, those can be ways of supporting investment and jobs in areas which are disadvantaged. So I think properly designed, some local/regional policies can be successful.