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Opinion **Global trade**

Waging war on trade will be costly

The US risks reversing nine decades of hugely successful policy that lifted tens of millions out of poverty

MARTIN WOLF



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Martin Wolf APRIL 4 2023

We are living in a dividing world. These divisions have many ramifications. But not the least important of these are for global commerce. The slowdown in world trade, the shift towards economic nationalism and the growing demands in the west, and especially in the US, for decoupling from China are reshaping the global economy. It is, as yet, unclear how far this decoupling will go. It is unclear how far the inward-looking interventionism will go either. But there is no doubt this is a significant turning point, with unpredictable and, in all probability, damaging outcomes.

As an [important recent paper](#) from the Peterson Institute for International Economics by Alan Wolff, Robert Lawrence and Gary Hufbauer brings out, the hostility to trade that has increasingly seized the US risks reversing nine decades of hugely successful policy. Ever since the protectionist disaster of the early 1930s, the thrust of US policy has been towards creating an open and rules-governed trading system. These policies created a more prosperous world economy, which became the foundation of western economic (and so political) success in the cold war. They facilitated a staggering reduction in global poverty. They are the most important credential for the US claim to have been a benign hegemon.

Today, however, Donald Trump and Joe Biden, who disagree on almost everything, both agree that this has been a mistake — a swindle on American working people. Moreover, it is not just policies at the border that are changing. The US is also embracing aggressive industrial policy, backed by generous subsidies. Behind this and strengthening it, is the great power conflict with China. We are indeed entering a new world.

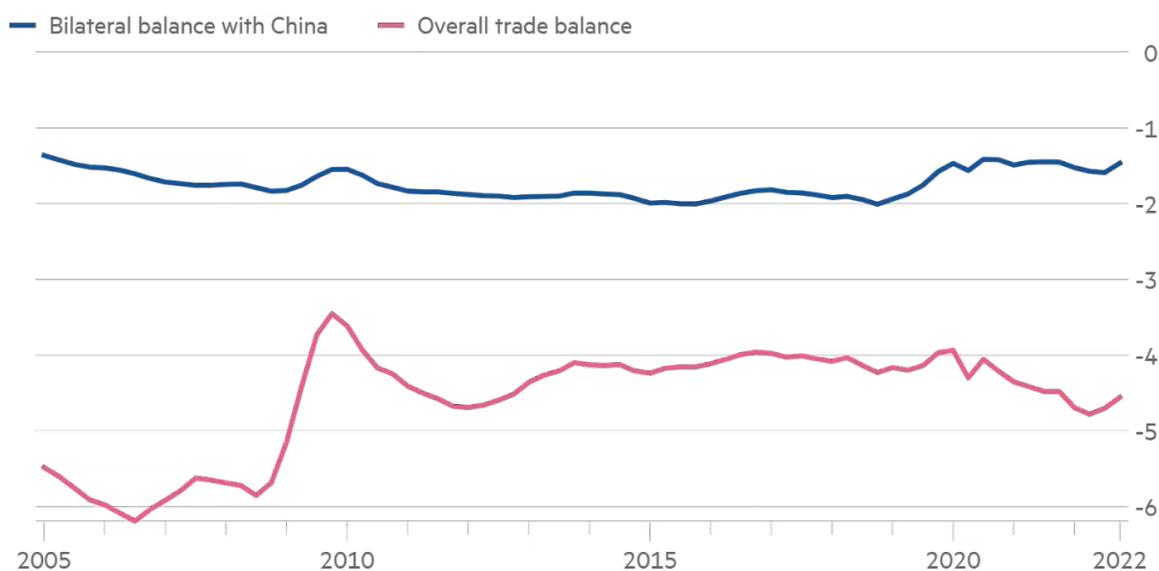
Two broad explanations can be given for this fundamental shift in US policy.

One is the rejection of “neoliberalism” — a pejorative label for market-oriented policies. But, contrary to the widespread view, it is untrue that liberal trade is a [dominant or even significant cause of the woes of the working classes of western societies](#). The principal driver of the decline of industrial employment has been rising productivity. Between 2000 and 2020, 6mn manufacturing jobs were lost in the US. But only some [1mn of that loss \(now long past\) was due to imports from China](#). The failure was not to provide any cushion for those who lost jobs and for the places in which they lived, as well as to ignore rising economic inequality.

The other explanation is the rise of a peer competitor that operates so successfully within the open world economy. That has linked up with the growing suspicion of free markets to justify decoupling from China, “reshoring” or “friendshoring” of supply chains, and interventionist and protectionist trade and industrial policies. Moreover, these new policies are not just addressed at China. “Buy America” policies are taking aim at both friend and foe.

The US bilateral trade deficit with China has diminished, but, predictably, this has not lowered its overall deficit

US trade balances, as a % of GDP



Source: Refinitiv
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This shift of policy in the world’s hegemonic power raises three big questions,

First, will these policies work in their own terms? There is [good reason to doubt this](#). [Adam Posen of the PIIE has recently argued](#) that the “self-dealing” of the current US approach will prove counterproductive, self-sufficiency is a foolish goal, competitive subsidisation is a negative-sum game, and politicisation of trade is sure to lead to wasteful outcomes.

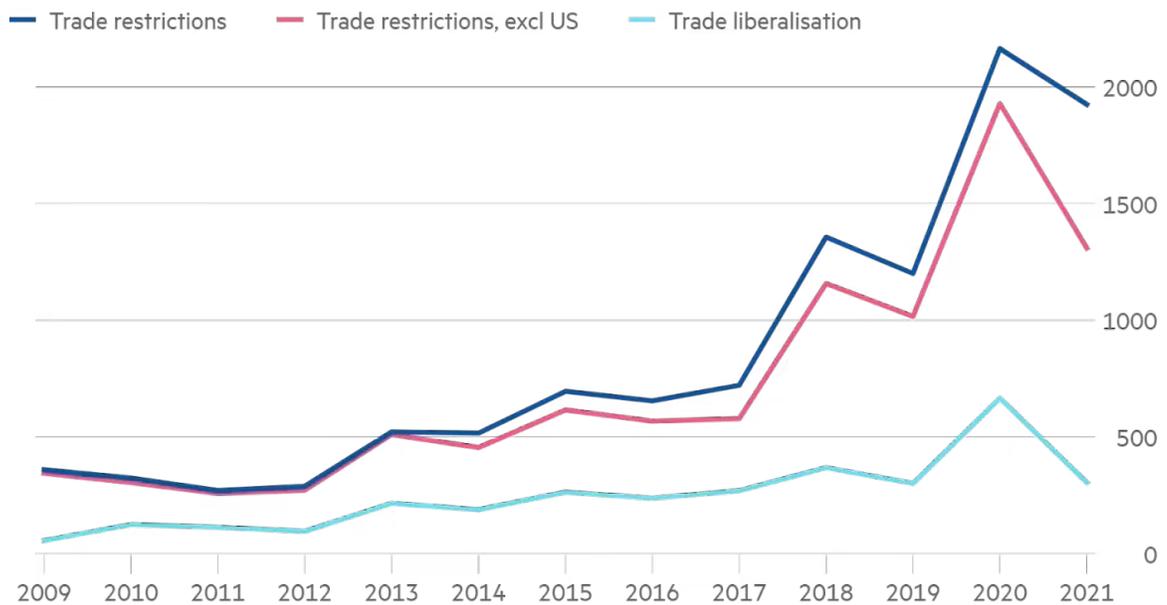
Moreover, he asserts, the focus on production is misguided; it is adoption of new technologies that matters. Not least, in deciding its policies, the US must understand that it is setting an example others will follow. Interventionists abroad will feel legitimised, making the world economy less open.

Second, what will be the impact of this shift on the world economy? [Eswar Prasad of Cornell warns](#) that “all countries, both rich and poor, will one day come to rue their inward turn”. In support, a [new book from the World Bank](#) stresses that the longer-term prospects for global economic growth are deteriorating. One of the reasons for this is the slowdown in the growth of world trade since the global financial crisis of 2007-09, worsened by post-Covid shocks and rising protectionism. Among other things, as the book notes, trade “is one of the primary channels of diffusion of new technology”. Furthermore, one should note, a more protectionist world will be one with lower elasticities of supply and so a greater propensity towards inflationary shocks.

Last but not least, how is this shift to be contained in a world of great power conflict? The obvious and rational answer is to define the exceptions to the general rules of liberal trade precisely and clearly. So, on supply chains and technology, the US and other powers should define where exactly they think the market will fail to provide them with the security they need and adjust their policies accordingly. There would need to be ongoing monitoring of relevant economic and security risks and adjustment of associated policies. At the same time, security-oriented interventionism should be as precise and non-protectionist as possible, with a view to continuing to gain from the economies of scale granted by cross-border trade.

World trade has been increasingly encumbered by restrictions

Number of new trade policy measures



Sources: Global Trade Alert Database, World Bank

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Now suppose this is impossible and that China and the US become increasingly inward-looking. What should other countries seek to do? One answer is to create a free trade agreement built upon World Trade Organization principles, but going beyond them. The kernel of such an agreement exists: the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP). This was born from the Trans-Pacific Partnership, created by Barack Obama, to be [repudiated by Trump](#). So add in the Atlantic and Indian oceans. But also leave the superpowers outside. The rest of the world can still co-operate.

martin.wolf@ft.com

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