The tariff is but one of many government-imposed . . .

BARRIERS to World Commerce

WILLIAM H. PETERSON

It is the maxim of every prudent master of a family, never to attempt to make at home what it will cost him more to make than to buy. . . . What is prudence in the conduct of every private family can scarce be folly in that of a great kingdom.

ADAM SMITH, *Wealth of Nations*

"WE NOMINATE for oblivion," declared President Eisenhower in a speech last May, referring to certain economic illusions. Among the President's nominees for oblivion was "the notion that we can export without importing."

In view of the newly-extended Reciprocal Trade Agreements Act, another idea that ought to be added to the oblivion list is the illusion that lower tariffs, however desirable in themselves, *necessarily* mean freer trade; for the stated purpose of the Reciprocal Trade Program is freer trade through lower tariffs.

The four-year extension to the Reciprocal Trade Act emerged from the legislative mill riddled with "escape clauses," "peril points," and many other protectionist compromises. Congressmen from areas where local industries are vulnerable to foreign competition – textiles, chemicals, china, electrical manufacturing, nonferrous metals, bituminous coal, domestic oil, whiskey distillation, and so on – generally got the protection they sought, usually in the name of such old reliable arguments as "fight the recession and national defense."

At least three questions arise: A basic one – which is best for America, free trade or protection? Another – will the lower tariffs achieved under the newly-extended

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Reciprocal Trade Program mean greater trade? And, finally – if we are in an all-out neck-and-neck race with communism and economic and military proficiency is of crucial importance, would greater trade result in higher proficiency?

Free Trade or Protection?

Let us seek the answer to the first of these questions: *Which is best for America, free trade or protection?* The question might be rephrased more broadly: Which is best for America, freedom or compulsion? For in the act of protection lies the act of compulsion (a moral issue not to be treated in this discussion). Under protection consumers are no longer free; their choice is denied. Economic democracy breaks down; the rule of the few decides. To buy the foreign product consumers are compelled to pay a penalty, being forced in effect to do business with a high-cost domestic producer. As a result, the consumer pays more and gets less. The resources of the economy are prevented from flowing into the most productive industries; instead, much of the nation's resources are locked in inefficient, high-cost, protected industries. With the exception of the protected investors and managements, everyone loses.

Protected investors and managements disagree. Armed with political influence and specious arguments, the protectionists have gotten many "protective" tariff walls and numerous other trade restrictions as well. The protectionists plead, for example, that high American wages constitute an obstacle to trade – but fail to note that wage *rates* are hardly as significant as unit wage *costs*, which may be relatively low for the American producer who is heavily mechanized, as compared to a foreign producer with little but flesh and blood workers.

Again, the protectionists plead that their industries and workers "must be saved" for the sake of prosperity – but fail to note that the preservation of inefficient industries drains resources, capital, and labor from the more productive industries, with unhappy consequences to national production and hence real wages – prosperity.

Item: Canada, a country which ranks second among the highest wage-paying countries of the world, is Uncle Sam's best customer. Similarly the United States, the highest wage-paying country in the world, is Canada's best customer.

Item: Western Europe, though much smaller in physical size and with fewer people but with higher wage levels by far than in Africa and Asia, sends the United States more goods and absorbs more

American goods in international trade than do the great populated low-wage land masses of Asia and Africa combined, including the Middle East.

Reasonable conclusion: High wages, rather than being a deterrent to American trade in particular and world trade in general, reflect greater ability to trade.

This empirical proof is supported in economic logic by David Ricardo's Law of Comparative Cost (1817). In his discussion, Ricardo included a hypothetical example of trade between Portugal and England. Suppose the Portuguese could make cloth more cheaply (i.e., Portuguese wages were lower) than the English, contended Ricardo, would Portuguese capital go into cloth?

In the long run, no, said the classical economist. For with Portuguese capital yielding a higher return on wine, capital would gravitate to wine and in the course of events cloth would be imported from England.

Hence, Ricardo's "law": Capital, unhampered, flows to industries of highest return, and costs should not be compared *between* countries but *within* countries.

Free Trade Defined

The case for free trade becomes, by logical inference, the case against protection. What is free trade? Two boys swapping tops for marbles is free trade. A retailer paying cash for supplies from a wholesaler is free trade. Free trade is simply voluntary exchange unhampered by government intervention. It is the secret of American well-being: 48, now 49, sovereignties in a colossal free trade area. It is the very heart of a market economy. It is part of the human make-up, what Smith called "the propensity to truck, barter, and exchange."

Free trade is, in a word, exchange – free exchange, along a two-way street for buyers and sellers. But many believe it is better to sell than to buy, for selling involves a seller's profit. One man's profit, according to this belief, means another man's loss. The idea of encouraging selling and discouraging buying, then, is extended to international trade. (Here, however, selling becomes exporting and buying becomes importing.) So, according to the old mercantilist doctrine, a "favorable balance of trade" is a country's trade whose exports exceed its imports – i.e., its sales abroad are greater than its purchases abroad.

The "favorable balance of trade" doctrine, still popular, is false. No buyer would buy if he knew he were going to lose. Quite the contrary, the buyer buys because he's convinced he gains. Adam Smith

knew this (see quotation, page 5). Ben Franklin expressed the *mutual* gain of trade as follows:

"In transactions of trade it is not to be supposed that, as in gaming, what one party gains the other must necessarily lose. The gain to each may be equal. If A has more corn than he can consume but wants cattle, and B has more cattle but wants corn, exchange is gain to each; thereby the common stock of comforts of life is increased."

Division of Labor

Free trade both causes and is caused by what Adam Smith called "division of labor." Division of labor – i.e., specialization of production – enables enormous increases in productivity. (Probably every reader of these words is in some way a *specialized* producer.) Of further importance to international trade is that specialization applies not only to people but also to land and natural resources. Examples of people, land, and resources specialization come to mind – Brazilian coffee, Irish linen, Swiss watches, Chilean nitrates, French wine, and so on. Yet division of labor without trade, or trade without division of labor, is incongruous if not impossible. Like Tin Pan Alley's "Love and Marriage," trade and division of labor go together like "a horse and carriage."

The formula for free trade, then, could be constructed as follows: Free trade = international division of labor = greater regional productivity = greater trade = higher levels of living.

The Reciprocal Trade Program

What of the second question: *Will the lower tariffs achieved under the newly extended Reciprocal Trade Program necessarily mean freer and hence greater trade?*

Our answer, in brief, is No.

Certainly freer trade is the stated aim of the Reciprocal Trade Agreements Program. The Program, founded in the 1930's under Cordell Hull, works through the principle of a swap. Through diplomatic channels, the United States will lower its tariff on, say, Commodity X, which Ruritanians sell in the U.S., providing Ruritania will lower its tariff on Good Y, which Americans sell in Ruritania. So, presumably, with the quid pro quo of each country met, lower tariffs are in the offing.

The Program is open to criticism on two counts:

First, the Program, based as it is on reciprocity, seems to assume that tariff reductions can go forward here in America only if commensurate favors are extended abroad. This places, in Washington and in Geneva, Switzerland (headquarters of the UN's international

tariff agency, GATT), heavy bureaucratic expense, license, and power over American industry.

The arbitrary and political power of bureaucrats in the State Department at home and abroad is enormous: Supposing a corporation has supported the "wrong" party in a political campaign or otherwise fallen out of favor with the powers-that-be, is there not the danger that the winning party could "sacrifice" the corporation in tariff negotiations with other countries – perhaps by removing protective tariffs on the industry or by increasing the protection to a competing industry as a form of hidden subsidy?

Moreover, the decisions of bureaucrats in the State Department and in GATT are reached in secrecy; and in GATT, American negotiators have but one vote in the international voting. Thus, for example, Ghana gets one vote, the United States one vote – a precarious position for American industry.

Perhaps more importantly, the goal of free trade frequently gets side-tracked under bureaucratic management. Trade and tariff concessions become a form of foreign aid and get tangled in international politics. The basic interests of the American consumer and the efficient American producer, both of whom stand to gain by free trade, are relegated to secondary consideration. What is needed in place of the philosophy of reciprocity, in short, is a thoroughgoing philosophy of free trade.

Secondly, the Reciprocal Trade Program comes under criticism because it virtually ignores the hard fact of world commerce that tariffs are but one means of restricting trade. There are, unfortunately, many others. Low tariffs or even no tariffs in a country can be completely obviated by *nontariff* trade restrictions. It is the main purpose of this essay to look over the more important of these nontariff trade restrictions, including:

1. Exchange controls
2. Bilateral trade agreements
3. State trading
4. Import quotas
5. Foreign aid
6. Cartels and international commodity agreements
7. Preferential trade treatment
8. Inflation and other monetary manipulation
9. Other statist measures

EXCHANGE CONTROL

Exchange control is a state monopoly over foreign exchange. As a modern practice it was initiated by Dr. Hjalmar Schacht, Hitler's finance wizard and exchange controller. The objective of Dr. Schacht was autarchy – economic self-sufficiency – to enable

Germany to wage war. When that war came, the Allies felt exchange control was necessary for their own total mobilization. The resulting bureaucracy became a powerful lobby for the perpetuation of exchange control. Today, more than 13 years after the war, and despite the fact that the chief end of the International Monetary Fund was the abolition of exchange control, exchange control persists throughout most of the world. In other words, most of the world currencies lack free convertibility. (The U.S. is a happy exception.)

Convertibility Defined

Just what is convertibility? It's the unhampered freedom to exchange at market prices one national currency for another, whether in coin, paper currency, or debits and credits to bank deposit balances. When it exists, convertibility greatly facilitates international trade and investment by making international payments easier. For countless years it did exist – the quiet and successful lubricant of private enterprise. But no longer.

Today the American businessman considering, say, a plant location in Britain, a franchised dealer in France, or closing a sale in Spain has to worry, aside from all his other problems, about inconvertibility, i.e., exchange control. So in London the businessman checks with the Exchange Equalization Account Office. In Paris with the Office des Changes, in Madrid with the Centro Oficial de Contratacion de Moneda.

In all these cases he, like his European counterpart, finds he has to do business with a state monopoly with its usual trappings of red tape and bureaucracy. These are bad enough, but what really worries him is the suspicion that he may end up with far fewer dollars than he had first figured on.

In some countries as many as thirty different kinds of money with varying exchange rates will prevail at one time. There's "tourist" money, "import" money, "export" money, and many subvariations of each breakdown. In "import" money, for example, it is not uncommon for a country to classify its imports in importance as, say, "critical," "necessary," "marginal," and "unnecessary," and then to build up the foreign exchange rates for each import category as its relative importance diminishes.

Political Determinations

In all these cases bureaucracy – not the market – decides the crucial question of who gets what and how much. Perhaps it's theoretically possible that an all-wise and

wholly impartial exchange control system could duplicate the success of private enterprise – speed the trader or traveler on his way with a minimum of delay and without favoritism or any rigging in the rates of exchange. But such is not the case in practice. In practice, for instance, there is the operation of the Brazilian exchange controllers who force Brazilian coffee producers to convert their dollars into Brazilian cruzeiros at artificial "official" rates. Thus are the Brazilian coffee producers deprived of a big chunk of the world market coffee price. This exchange control action inevitably discourages Brazilian coffee producers and ultimately hurts coffee consumers the world over.

Item: In 1945 the International Monetary Fund was established with a view toward world convertibility of currencies. Yet, 13 years later, of the 64 national members of the Fund, only 11 countries – all in the Western Hemisphere, including the U.S. and Canada – maintain convertibility, i.e., the absence of exchange control. Of the nine countries who are not members of the IMF, excluding the Soviet Bloc countries, Liberia is the only one that has no exchange control.

Licenses, priorities, quotas for imports and subsidies for exports, interstate clearing arrangements, shunting transactions, blocked currencies, balance of payments difficulties – all given to frequent breakdowns – manifest the creaking machinery of exchange control. The ill-designed machinery can hardly help but clutter and choke trade and investment across international boundaries.

"Dollar Shortage"

The crowning evidence of the futility of exchange control is seen in the long-persistent plaint of a "dollar shortage" or, as it is now euphemistically called, the "illiquidity problem." When other governments overprice their currencies in terms of dollars, dollars, in obedience with Gresham's Law, become scarce – i.e., "short." Like all other price-fixing arrangements, then, the exchange controllers must resort to rationing dollars, thereby placing international trade under an incredibly complicated system of licensing, quotas, and controls. "Dollar shortage," indeed! Better than $60 billion of postwar foreign aid has in no way relieved the "shortage." The clamor is for more.

Canada is proof of the efficacy of convertibility. On December 14, 1951, Canada completely dropped exchange control. Immediately the outward flow of funds and investment *from* Canada was reversed *into* Canada. Assured that their profits would not be embargoed in

Canada, world investors moved large amounts of capital into Canadian industry and mining. The Canadian dollar began to rise against the American dollar and now has surpassed it in value – a dramatic instance attesting to the potential of a free market in currencies and the vigor of private "foreign aid."

BILATERALISM

A basic characteristic of free trade is indirect exchange. While international trade consists of swapping goods and services among nations, rarely does the individual trader in one country swap goods and services directly with a trader in another country. Instead, foreign exchange is used as payment for the traded goods and services.

The volume of foreign exchange receipts and payments may add up to a deficit balance of payments incurred by traders of Nation A in its dealings with traders of Nation B. However, Nation A uses its surplus balance of payments achieved in its dealings with Nation C to meet its deficit with B. The same technique of a "triangular" settlement holds for B and C. Such international trade and payments is called "multilateralism."

Contrasted against multilateralism is bilateralism, another modern practice dating back to the ingenious Dr. Schacht. Bilateralism is a throw-back to barter, for it involves two countries agreeing for a certain period of time to buy and sell to each other in approximately equal amounts and usually at predetermined prices. Bilateral trade treaties become economic strait jackets as countries commit themselves to dealing with only certain other countries for as long as five-year terms, regardless of the adverse economic and political conditions that hold or may develop.

As an example of bilateralism, note the one-year bilateral trade agreement signed by Japan and Formosa, retroactive to April 1, 1958. The agreement provides for an exchange of goods worth $85,250,000 each way. The principal Japansese goods to be exported under the agreement include fertilizer, machinery, iron, railway rolling stock, ships, and textiles. The chief Japanese imports from Formosa will include crude sugar, rice, canned pineapple, and salt.

Supposing the United States government concluded a similar bilateral agreement but in a far greater amount with, say, the government of Mexico, what would this mean for American consumers? Clearly, consumer freedom would be violated and competition in the imported items listed in the

agreement would be delimited. Of the listed items, only Mexican imports would be admitted. Furthermore, since American consumers are also, broadly speaking, producers, American overseas markets and competition would also be delimited. Thus, coming and going, producing and consuming, American consumers would be bound by a rigid, unalterable, governmental decree.

Again, as in exchange control, it should be seen that bilateralism involves bureaucratic management and political judgments. Importers and exporters in the affected countries are not free to deal with the best sources and markets throughout the world. Price and quality considerations are secondary to political considerations. Since buyers are forced to turn to relatively unattractive sources and sellers to relatively unattractive markets, international buying and selling tend to diminish. International division of labor is stymied. World commerce is hurt. Consumers in the bilateral countries and to a degree in the rest of the world lose.

STATE TRADING

State trading is international trade by governments. Usually the governments have title to the goods in trade. Sometimes the governments have no title but take an active role in negotiations over the terms of trade, and this also constitutes state trading.

The clearest examples of state trading are found in the Soviet bloc countries. Inasmuch as a "comrade" in a "people's democracy" is prevented by law from holding title to commercial goods, trading within the bloc is on a state-to-state basis – in a simple single transaction, one government exports, the other imports.

The USSR, which in April 1918 nationalized foreign trade, has created various state agencies to handle its foreign trade transactions. On the export side, for example, is Soyuzugelexport (coal) and Soyuzneftexport (oil), and on the import side are such agencies as Soyuzemtimport (steel products) and Textilimport (textiles). In most of the major countries of the world, the Soviet government has established state trading agencies or "trade delegations." In the United States, the official Soviet state trading agency is the Amtorg Trading Corporation, chartered under New York State law in 1924 and presently located at 49 West 37th Street in New York City. Amtorg has been relatively quiescent, with the cold war and its having figured in a sensational Congressional investigation of subversion following World War II.

Outside the Soviet bloc, state

trading is much less on a state-to-state basis than it is on a mixed basis — one party is governmental and the other is private. Almost half of the foreign trade of Argentina, for example, has been operated by a government bureaucracy, IAPI. Britain, France, Italy are among the many countries with nationalized industries, which almost inevitably forces these countries into state trading. The British government, for example, monopolizes the importation of several commodities and foodstuffs through exclusive bulk trade agreements with other countries. The French government has been buying about one-third of France's imports.

Stockpiling Operations

The United States is not immune. The American government has for the past generation been purchasing strategic and nonstrategic commodities on its own account for stockpiling and price-support purposes. Copper, lead, and zinc, regarded as critical defense industries, have long been the beneficiaries of government purchases, as well as government tariffs.

In exporting, the American government is engaged in a giant overseas surplus agricultural commodity disposal program, one of the repercussions of the government's "parity" farm price supports. So the U.S. government "sells"— dumps, say many foreign producers — its surplus wheat, corn, cheese, cotton, and other commodities abroad at knockdown prices. Ironically, these prices often are much lower than those paid by American citizens. And while the law (PL 480) governing such sales proclaims that no disturbance of world markets and prices is to occur because of the American disposal operation, disturbances have been inevitable. Formal protests to the U.S. have been registered by Australia, Brazil, Canada, Denmark, Burma, Netherlands, Mexico, New Zealand, Argentina, and Uruguay.

Item: In 1958 the New England Governors Textile Committee formally protested the discriminatory action of the U.S. government for selling cotton to foreign textile mills, especially in Japan, at far lower prices than those paid by New England textile manufacturers.

The troubles with state trading are many. It is an outright denial of free trade. It carries all the evils of monopoly. It suffers all the ills natural for bureaucracy and socialized industries. It is, more often than not, noneconomic and discriminatory, forever weighing political and military considerations. It tends to incur interna-

tional ill will. With international division of labor and free trade stymied, consumers in the affected state trading nations in particular and consumers the world over in general, come out on the short end.

IMPORT QUOTAS

To the protectionist-minded government, tariffs are faulty in a number of respects and this accounts for the rise of nontariff restrictions. One of the faults of tariffs is the absence of any accurate control over the volume of imports. Technically there is no limit to the amount of foreign goods an importer can bring in if he's willing to pay the penalty. While this problem can generally be met by prohibitively high duties on the protected goods, many governments prefer to impose precise quantitative restrictions.

These restrictions – import quotas – are usually for one-year periods and are expressed in physical terms: tons, board feet, gallons, units, as the case may be. Ruritania, for example, may declare: We will admit but 10 million bushels of foreign wheat in 1959. Such quotas may be set globally, by countries, or through import licensing. Global quotas simply specify limits which may be imported from the rest of the world, which means that the closest countries, geographically, will have the jump on those furthest away. Country quotas eliminate this discriminatory feature by allocating the quantitative restrictions to each exporting nation according to the base-period method. Country quotas also discriminate, however; this time against those nations whose export industries are fairly new and hence could not qualify under an old base. Import licensing frequently imposes limits on the amounts of specified goods which may be brought into the country, and the licenses themselves are not uncommonly restricted to favored importers.

Item: The United Kingdom, before 1939, used to import freely American products now heavily restricted by import quotas. For example, in a recent year, the U.K. admitted the following quantity of appliances from one company: one dishwasher, 35 electric ranges, 25 deep freezes, 19 washers and dryers, and 194 refrigerators. In the same year, only 650 American cars of all makes were permitted to be imported into Britain while British cars were exported to the U.S. by the tens of thousands.

Import quotas have not been common in America. Of late, though, the U.S. government has been establishing quotas on farm imports, especially on sugar, cereals, and dairy products. Also, the Eisenhower Administration has

set a so-called "voluntary" oil import quota system for the American oil industry. The system had been demanded by domestic oil and coal interests. The Administration declares it to be a "defense" measure. Practically all of the major oil companies with overseas oil fields have now "agreed" to specified limits on crude oil imports assigned to each oil concern. Political and economic repercussions have quickly redounded to the U.S. from such oil-exporting nations as Venezuela, Canada, and Middle Eastern countries.

Quantitative restrictions are hardly calculated to spread good will among nations. They constitute a crass form of protection. Retaliation is usually quick. France initiated the modern quota system early during the Great Depression, and by 1937 more than 25 other countries had some kind of quota system in operation. Quotas impede international division of labor. They require costly, arbitrary, bureaucratic, discriminatory management. They discriminate against both foreign suppliers and domestic importers, as well as against the nation's consumers who must foot the bill with higher prices and bigger taxes.

FOREIGN AID

In his foreign aid message to Congress in February 1958, President Eisenhower requested a $3.9 billion program of military, economic, and technical assistance to "the free world" for the government's accounting year, 1959. The President emphasized the role of fostering international trade that foreign aid was to play. Said the President:

"[The aided countries] must have technical assistance to train their manpower, to explore their resources, and to use them productively. They must have supplementary capital from abroad for investment in agriculture, power, transportation, and industry. They must have help to tide them over economic difficulties that threaten their stability and cohesion. *They must have increasing trade with availability of necessary imports and growing markets over the long term.*" [Italics added]

It is not feasible at this point to explore the case for foreign aid, which in postwar credits extended by the U.S. abroad amount to more than $60 billion. But it is to the point to note that foreign aid tends to preclude free trade and private investment.

Certainly, foreign aid disrupts normal world trade patterns. Most American aid credits – about three-fourths – must be spent in the United States. Many of the aided countries would prefer to spend these credits elsewhere.

They do not, as a rule, wish to import from their principal creditor nation, and most assuredly they would rather buy where terms are most favorable. Other supplier nations, especially those whose prices are lower than those of the U.S., resent the spectacle of their actual or potential customers being supplied gratis or at subsidized prices, however attractive this might be to the aided consumers.

Item: Between 1946 and 1956 it is estimated that $60 billion in American credits were transferred to "the free world" in foreign aid, two-thirds of it in so-called economic aid. This figure amounts to 40 per cent of the value of the American exports during the same period which totaled $155 billions.

It is important, too, to note that U.S.-provided steel mills, railroads, electric generating stations, jute mills, canning plants, and so on are not sanctioned through market forces and unhampered international division of labor but rather through the decisions of bureaucratic management both in the U.S. and in the recipient countries. Investment errors of great magnitude are likely under such circumstances.

Moreover, aid is a government-to-government matter. Private enterprise in recipient countries is discouraged. So is private investment from overseas. Governments already hostile toward capitalism resent as degrading charity the aid they will nonetheless accept. With an almost assured flow of aid dollars (aided countries can always threaten to turn toward the communists), recipient nations are anything but moved toward creating conditions conducive to private property and free enterprise —the foundations for free trade.

Foreign Aid Nurtures Socialism

The crowning result of foreign aid, then, is that the U.S. has inadvertently nurtured socialism in order to fight its blood brother, communism. Socialized industries, notorious for their inefficiency, will hardly fare well in world markets. And inasmuch as socialized industries are not subject to the sovereignty of the consumer, it follows they will not be eliminated from the competitive race. Rather, their governments will likely cut off foreign competition through protection and, if there is to be "international trade" engage in state trading. Consumers in the protected country will lose and so will the consumers of the world at large because of this interference with the international division of labor.

It follows, also, that the corollary of foreign trade, foreign investment, is similarly hampered by foreign aid. Capital is timid. It

will hardly venture into lands where governments are "establishing" industries and where private property is suspect and subject to nationalization.

"Trade, not aid," so worshiped in the abstract, should be the reality instead of the de facto "aid, not trade."

CARTELS AND INTERNATIONAL COMMODITY AGREEMENTS

Cartels and international commodity agreements amount to monopolies on an international scale. These arrangements aim at price-fixing and market allocation and hence are highly restrictive of international trade. They are the antithesis of free trade.

Cartels are quasi-private arrangements between two or more business firms in different countries to reduce or eliminate competition. The privacy of the arrangements tends to be short-lived. Sooner or later, a cartel must have government protection, for otherwise "outsiders" would flood the cartel's markets and "wreck" prices. This would be wonderful for consumers but poison for the cartel.

Cartels are illegal in the United States under the Sherman Antitrust Act of 1890. This restraint has been diluted by the Webb-Pomerene Act of 1918 and the government's participation in commodity cartels euphemistically called "international commodity agreements." The Webb-Pomerene Act provided that American companies could form "export associations" and fix export prices and quantities.

Item: Two American airline companies, Trans World Airlines and Pan American, although regarded by the government as regulated private utilities, participate in an international airline cartel, the International Air Transport Association, most of whose members are nationalized. The Association sets prices, determines operating conditions, and, to an extent, allocates markets.

International commodity agreements are essentially cartels, invariably started by governments. Ordinary cartels are private agreements ultimately requiring public support. International commodity agreements are public agreements from the outset. Each, cartel and international commodity agreement, is aimed straight at the heart of free trade and international competition. Their main purpose is price-fixing or "stabilization." This purpose has led to governmental controls over production and marketing. To court public favor, controls are generally declared necessary to achieve an "orderly marketing of staple com-

modities," or some such objective.

Commodity agreements have been tried for wheat, sugar, wool, rubber, tin, cocoa, coffee, and other items. The history of such agreements shows anything but success in "stabilizing" prices and controlling production and marketing. Certainly consumers have little, if anything, to gain from the operation of commodity agreements. Yet the United States participates as a producing nation in two big current commodity agreements, the International Wheat Agreement and the International Sugar Agreement. The cost of the latter to American sugar consumers, who are forced to support inefficient domestic sugar cane and beet sugar producers, has been estimated at 50 per cent over the world sugar price.[1]

The results of cartels and international commodity agreements are the same: International competition and investment are stifled. International division of labor accordingly suffers. Consumers the world over are losers. Power politics intervene. "German cartels," to quote from Professor Michael Heilperin in his *The Trade of Nations* (New York: Knopf, 1947. p. 87), "greatly encouraged and later controlled by the state, became the handmaiden of power politics."

[1]Poirot, Paul L., "Flies in the Sugar Bowl" in *The Freeman*, May 1956, p. 6.

PREFERENTIAL TREATMENT

The point of trade restrictions is to impose preferential treatment — almost always a preference for domestic producers, and occasionally for favored foreign producers. Tariffs, of course, are a form of preferential treatment. In 1953 Switzerland, for example, increased her tariff on American nylon stockings by 300 per cent, but this may have been in retaliation against recent increases in the American tariff on Swiss watches.

President Eisenhower expressed this preference to the Canadian Parliament last July, as follows:

"Neither of our countries is a 'free trader'. . . . Each of us feels a responsibility to provide some protection to particular sectors of our economy which may be in distress. . . . We have taken some actions of this sort. So has Canada."

The President might have illustrated American protection through preferential treatment by pointing to a U.S. government order a few years ago to two Pittsburgh companies for generators and transformers for the Chief Joseph Dam on the Columbia River. The order amounted to $6,300,000. Yet a British concern had offered to supply the same equipment for $5,300,000. How did our government justify its paying some one-fifth more than the Brit-

ish price? It invoked the "Buy American" Act of 1933, which authorizes the government to pay more for American products when such orders would create work in areas of "substantial unemployment" or when "national security" is threatened. (Note: After much delay and political discussion, the order was withdrawn from the two Pittsburgh companies and awarded to the British company.)

Item: Many countries in effect embargo American cars through the simple expedient of imposing weight or power limits on cars and trucks for use on their highways. Through this technique Bermuda, for example, excludes imports from the American automotive industry.

Similarly, the U.S. government subsidizes American shipbuilding and shipping on the theory that these are industries critical for national defense. However, in this regard, the U.S. is little different from most of the world in such preferential treatment of shipping. "Peril points" and "escape clauses" are prime examples of American preferential treatment. "Peril points," initiated in the 1948 Extension Act, permit the U.S. Tariff Commission to review each rate on the "bargaining list" and determine at what point further tariff reduction would "injure" American producers. "Escape clauses," an extension of the peril point idea, unilaterally allow the United States or its treaty countries to suspend or modify a tariff concession in any trade treaty with another country when "increased imports threaten serious injury to the domestic industry."

Canada, too, as the President observed, has also hewed to preferential treatment. Canada and other British Commonwealth countries, for example, utilize what they call "imperial preferences," meaning that goods moving between Commonwealth countries may enter at a lower duty rate than the same goods originating from countries outside the Commonwealth. Imperial preferences got their start, in part, as retaliation against the American Smoot-Hawley Tariff of 1930 which raised American tariffs to an all-time high. Britain, again at least partly because of retaliation, deserted her traditional free trade banner with her highly protectionist Import Duties Act of 1932.

"Common Market" Schemes

Preferential treatment of sorts is one of the aims of common market schemes such as Benelux (Belgium, the Netherlands, and Luxembourg) and the just-launched European Common Market. To be sure, common markets (sometimes called customs unions) widen the area of free trade within the com-

mon market countries. And this is a good thing, as far as it goes. Regional division of labor will be broadened, and greater trade should result. In trade relations with countries outside the common market, though, common market authorities are likely to erect a tariff wall higher than the average tariff level prior to the formation of the common market.

This is a danger for the European Common Market in particular. France, a Common Market member, has long been a notoriously protectionist country. France thus may force the Common Market tariff wall to great heights. For America, this would be an irony. America has been one of the chief sponsors of the European Common Market; it may be one of the chief losers by it, with American goods shunted by Common Market tariffs from European consumption. Moreover, there is now talk in world capitals of a South American common market, a Central American common market, a North European common market, and a Far Eastern common market, all of which conceivably could isolate the U.S. in international trade.

Preferential treatment, it must be emphasized, is not the preferences of individuals and trading groups freely deciding what to buy, when, where, and how. Preferential treatment is treatment enforced by governments, exerting their authority over international trade. International division of labor and international trade and investment are certain to suffer as a consequence.

INFLATION AND OTHER MONETARY MANIPULATION

If the nineteenth century was an era of the gold standard, free trade, and monetary stability, the twentieth century has been an era of managed currency, protection, and monetary instability. This instability – i.e., violent inflation – has boded ill for international trade, which wholly depends on international payments. Inflation – the expansion of money and credit – distorts "official" exchange rates. Domestically, it tends to set in motion a flight from currency into goods. Externally, it tends to cause another flight: a flight of "hot money" fleeing to foreign sanctuaries where inflation is relatively quiescent. Inflation ultimately causes domestic prices to rise with the result that foreign importers are strongly inclined to shop harder for better bargains elsewhere.

True, gold still continues to serve as an international medium of exchange, though on a very limited basis. Today practically all the nations of the West, including

the U.S., avoid gold – the historical lubricant of free trade – as a domestic standard; i.e., gold redeemability is no longer a right accorded to citizens of the West.

This *political* "flight" from gold has received important intellectual support from the late Lord Keynes who once referred to gold as a "barbarous relic." It was Keynes who sanctioned the notions of "full employment" and manipulated monetary systems.

Endless Intervention

What does monetary manipulation have to do with restrictions on international trade? Just this: Full employment policies are nationalistic policies. If falling foreign demand hurts the export industries and causes unemployment at home, political authorities contend that the restoration of the "full employment equilibrium" requires import restrictions to "protect" domestic markets and to "create" employment. A further Keynesian requirement: inflation, the forced expansion of money and credit. For in "mature" economies, argue the Keynesians, less-than-full employment is inevitable unless some "socialization" of demand and investment (i.e., inflation) takes place.

The past generation has been one of fantastic inflation the world over. Governments spend and spend, pumping out ever more money. One Keynesian admitted in the London *Economist* a few years ago: "Inflation is nine-tenths of any practical full employment policy."

Little wonder, then, inflating governments soon face balance of payments difficulties. Exports, loaded with inflated costs, fare less well in world markets and shrink in volume. Imports become relatively cheaper in the domestic market and grow. The government, somewhat bewildered, first applies exchange control to mask inflation and maintain the fiction of "official" exchange rates. Then to cheapen its exports and regain world markets, the government comes to the inevitable: devaluation. But, later, still more inflation, and the cycle of "re-evaluation" (i.e., devaluation) repeats itself.

Inflation, in short, is the handmaiden of exchange control and protection. It generally spells death for free trade.

OTHER STATIST MEASURES

Monetary manipulation (inflation) is but one form of government intervention in economic activity. Would that it were the only one! Unfortunately there are many others, all of which contribute to the rationale and hence the machinery of protection. Among them are price controls, monopolistic and

militant labor unionism, various open and hidden subsidies, "planning," and nationalization. All of these constitute direct or indirect interference on the part of government with the free forces of supply and demand. Bureaucratic management and political judgments go into ascendancy. Inefficiency, as noted by C. Northcote Parkinson in his splendid essay, "Parkinson's Law," becomes inevitable. And with the inefficiency comes higher costs, pushing domestic prices ever higher and thereby worsening foreign trade positions. Further intervention then becomes inevitable, for governments are inherently not prone to admit their failures. Protection is *the* almost certain answer to the failures of intervention. Intervention breeds intervention, in short.

Consider the matter of nationalization. When Mexico, for example, nationalized the foreign investments in its oil industries in 1938, it was the second largest oil producing country in the world. Foreign investments, quickly and understandably, came to practically a complete halt in Mexico. Mexican technology was, to put it mildly, inadequate to face the many problems imposed by nationalization. Today the Mexican oil industry stands ninth in world production. The abortive nationalization of the Anglo-Iranian Oil Company property by Premier Mossadegh of Iran during the early 1950's affords another example of the futility, but never-dying vitality, of intervention.

Subsidy of exports is another form of state intervention, a form going back to the mercantilistic policies of the seventeenth and eighteenth centuries. Subsidy is regarded as a form of economic warfare. Outright bounties are rare. But various indirect means of subsidizing export industries are common. France, for instance, employs the following export devices:

Refund of fiscal, payroll, and social security taxes
Exemption from production tax
Credit volume limitations waived for exports
Lower discount rate on export commercial paper
Government loans to boost export production

Price Controls

Take the matter of price controls. Usually the basis for price controls is the advertent or inadvertent policy of inflation by the government. The result of inflation is rising prices. "This is an intolerable situation," declares the President of Ruritania, asserting that "profiteering" must stop. So to stop the "profiteering," the Ruritanian government doesn't

stop the monetary expansion but institutes price controls. Complications arise. For example, manufacturers using commodities and supplies from overseas quickly find themselves in a dilemma. They tell their overseas suppliers that they are sorry but domestic prices are under control and Ruritanian manufacturers can no longer pay the world price for commodities and supplies from overseas. Meanwhile, the price controllers are also in a dilemma: If they allow their manufacturers to pay higher world prices (for other countries are also inflating their credit and currencies), how will the domestic price "ceilings" be maintained? A possible answer in the "protectionist psychology": bilateral trade agreements, a reversion to barter. The point is that intervention and protection go hand-in-hand.

Item: Between World War II and 1955, France and Britain engaged in an increasing trend of state intervention. Relatively speaking, West Germany and Switzerland engaged in a decreasing trend of state intervention. France's tariff level advanced about 35 per cent and Britain's by about 40 per cent. Switzerland's tariff level, however, fell by about 35 per cent and West Germany's by some 70 per cent. West Germany's "recovery" from World War II is world-renowned; Great Britain and France limp along.

Whatever the intervention, then, free international trade is likely to suffer. Exporters, finding themselves underpriced in foreign markets, demand a subsidy. Labor unions, finding employers losing orders because of foreign competition, demand that their governments undertake "appropriate action," i.e., protection. Planning officials, finding the free give-and-take of international trade upsetting their planning targets, demand "controls" over international trade. Almost all of these demands spring from prior intervention. All of these demands add up to calls for protection.

Item: In February 1958, the American Tariff League, Inc., a protectionist lobby, listed the following major nontariff trade restrictions used by 89 nations of the world:

	No. of countries
Advance Deposit for Imports	13
Exchange Licenses	33
Exchange Tax	9
Existence of Blocked Nonresident Accounts	10
Export Licenses	46
Forced Exchange of Payments Received in Foreign Currency	47
Import Licenses	62
Import Quotas, Agricultural	9
Import Quotas, Non-agricultural	8
Multiple Exchange Rates	23

Preferential Exchange Systems..16
Preferential Trade Systems 21
Restrictions on Incoming Capital Movements 28
Restrictions on Outgoing Capital Movements 36
Restrictions on Payments for Invisible Imports 45
State Trading 13

In addition, the League says there are 20 other distinct forms of nontariff restrictions, including discriminatory taxation on nonresident investments (4 countries), bond required of importer by government (1 country), import embargo (5 countries), and surcharge on exchange (6 countries).

Not Aid to Trade

We reach the answer to our second question – will the lower tariffs achieved under the newly extended Reciprocal Trade Program necessarily mean freer and hence greater trade? The answer: No. While "the free world" deplores the protectionism of the United States, a policy we need not be proud of nor one designed to increase the economic well-being of the nation, the fact remains that our allies are far more protectionist than we. The protection is far less today in the form of prohibitive tariff walls but rather through a bewildering variety of nontariff devices.

Trade and Productivity

Now for the last of our three questions: *If we are in an all-out neck-and-neck race with communism and economic and military proficiency are of crucial importance, would greater trade result in higher proficiency?*

Our answer, in brief, is Yes.

The rule to remember is that what hurts consumers hurts business, and what hurts business hurts proficiency. After all, what is proficiency? Simply the power to produce. The power to produce is best determined by free trade, and not by bureaucratic decree. The power to produce is a corollary of the power to trade. Thus the more trade the more production, and the more production the more trade.

Protection, on the other hand, is aimed at the power to trade. In this, the protectionist government does indeed aid *some* industries, but only at the expense of *all* industry. Under protection, all domestic industry is deprived of markets at home and abroad. All domestic industry is hurt by the higher costs of labor and materials. Thus by restricting the power to trade and locking in inefficiency, the protectionist government restricts the power to produce.

This means, in turn, that consumers will have less, for produc-

tion constitutes the sole means of consumption. The power to produce, after all, is the power to consume.

National Defense

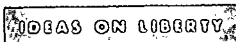
One more point: Our final question implies the consideration of war. Which is the harbinger of war, free trade or protection? Protection, it will be remembered, is frequently imposed as a "defense" measure. We protect, say the protectionists, to be ready for war. But what of the aggression involved in protection? Stopping goods and services, interfering with the movement of and payment for international trade – these actions hardly are likely to foster international good will. Autarchy may well mean self-sufficiency, the basis for a war footing. But free trade means civilized, peaceful cooperation among free peoples.

In sum: Protection breeds animosity. Trade breeds friendship.

Item: The Tariff of 1828, in the South known as the Tariff of Abominations, touched off great Southern animosity and South Carolina's Doctrine of Nullification. The Civil War followed in the wake.

Item: Beginning in the 1920's and accelerating during the 1930's, increasing protection against Japanese imports was a policy of the American government. The policy was hardly calculated to incur the good will of Japan. In 1941: Pearl Harbor. In 1954, by way of contrast, the American government advanced as one of the reasons for the extension of the Reciprocal Trade Program: "to improve Japan's trading prospects in the world, an essential element to stability in the whole Far Eastern situation."

Item: The nineteenth century was a century of free trade and relative peace. The twentieth century, so far, has been a century of protection and war. • • •



Competition Is the Mainspring

IT SHOULD NEVER BE FORGOTTEN, however, that to argue for higher tariffs is automatically to argue against greater competition . . . For free competition, and not some particular industry, is the mainspring of this economy. To the extent it is diminished, the economy, and consequently the defense effort, must needs suffer.

Wall Street Journal, March 28, 1955