INTERVIEW

Douglas Irwin

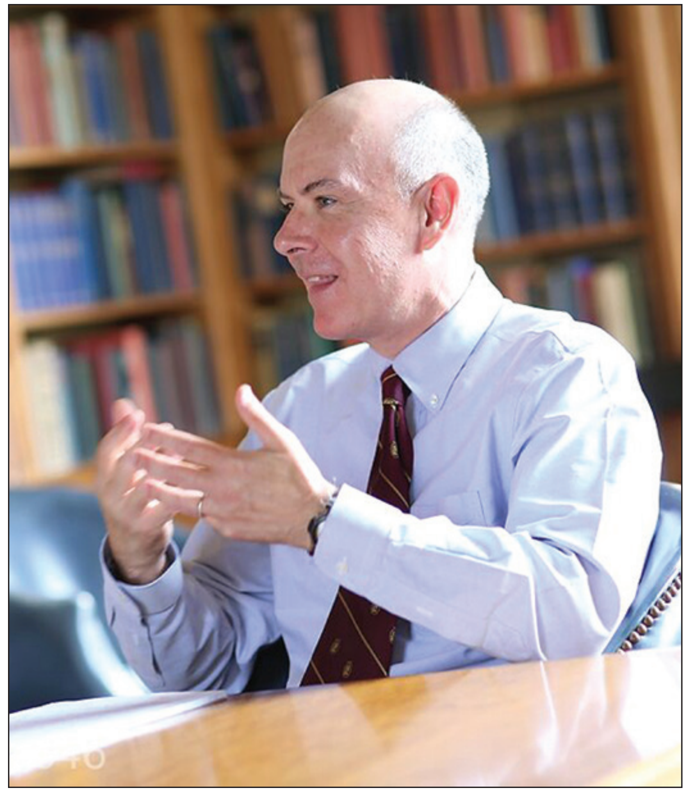
Editor's Note: *This is an abbreviated version of EF's conversation with Douglas Irwin. For additional content, go to our website: www.richmondfed.org/publications*

There is arguably no proposition more widely held among economists than the free trade of goods across countries generally benefits the citizens of both the exporting and the importing countries. Yet, support for trade often faces resistance among the public and policymakers. In the United States and other developed countries with broadly liberal trade policies, such skepticism, at least rhetorically, seems to have gained momentum recently.

Douglas Irwin, an economist at Dartmouth College, argues that nations would be well advised to retain or to adopt a commitment to free trade. The overall benefits remain large — and the costs of protectionism are often understated.

Moreover, Irwin notes, the arguments that proponents of protection frequently advance are many times questionable. For instance, he acknowledges that the United States had relatively high trade barriers during the late 19th century, a time of rapid industrialization. But it seems likely that such economic growth was due to a number of other factors instead. In other cases, Irwin argues, protectionist policies, while unwise, have not been as destructive as some have claimed. For instance, the importance of the Hawley-Smoot Tariff of 1930 to the deepening of the Great Depression generally has been overstated.

Much of Irwin's work falls at the intersection of economic history and trade theory. His most recent book is a comprehensive, more than 800-page history of U.S. trade policy, *Clashing over Commerce*. In addition to authoring and editing many other books and publishing widely in professional journals, Irwin occasionally writes for the popular press. He started his career at the Federal Reserve Board of Governors, moved to the University of Chicago's Graduate School of Business, and has been at Dartmouth since 1997. Aaron Steelman interviewed Irwin on the Dartmouth campus in August 2017.



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EF: Why did you decide to write a general history of U.S. trade policy — the first, as you note in the introduction, since the early 1930s?

Irwin: I have long had a general interest in trade and history, but what solidified my interest in U.S. trade policy in particular was spending a year at the Council of Economic Advisers (CEA) while in grad school. That was in 1986-1987, and it was a momentous period for U.S. trade policy. There were trade disputes with Japan, a lot of protectionist pressures to block imports of textiles and steel, and many other trade issues on the agenda. So that CEA experience, seeing how policy is made, and learning from people at the U.S. Trade Representative's (USTR) office, got me very interested in how U.S. trade policy functioned. And then, pretty naturally, I became very interested in looking to the past.

The last major book of this sort was *The Tariff History of the United States* by Frank Taussig. It's a great book, a classic, but it's been a long time since his last edition. And I thought it could be updated on multiple dimensions — first of all, to discuss the Great Depression and then bring it up to the present. We have also learned a lot more about the trade history that he did cover. He was writing before cliometrics, before the use of statistical methods to test a lot of the propositions he was discussing, such as the effects of protectionism in the late 19th century. In addition, economists have become interested in the political economy of policy formation. There's not a lot of political economy in Taussig, so it can be a little bit dry sometimes as he's going through changes in the wool schedule, the cotton schedule, and so on. I think people are less interested in that sort of detail than the bigger picture of how the political parties were functioning, the pressures members of Congress faced, and how we shifted toward freer trade. So that's sort of how it came together.

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More specifically, I distinctly remember being in my Chicago office in 1995 when Michael Bordo gave me a call (email was still a novelty) and asked if I would write a paper on U.S. trade policy during the Great Depression. I really hadn't worked much on U.S. trade policy up to that point, though I had the latent interest. I thought it would be a really easy paper to write because I assumed that there would be a large literature on trade policy during the Great Depression. But when I did my literature survey I discovered — to my horror — that there was almost nothing really analytical on the period. So I actually had to write something like five background papers just to write this one conference volume paper. After that, I started doing a lot of analytical and empirical work on various episodes in U.S. trade policy history. Once I had written enough papers, it became obvious that I really ought to synthesize them and turn it into a book. That was around 2000. After various delays, I came close to finishing the book in 2006, but then 2007 came, and like many economists, my work got diverted by the financial crisis and I returned to looking at issues related to the Great Depression. After more delays, I finally got back to the book around 2013 and pushed it through to completion.

EF: You argue that the United States has gone through three major eras in trade policy — and structure the book accordingly. Could you describe those?

Irwin: I tried to start the book with principles about what government officials and representatives are trying to achieve with trade policy, and it seems to me that they use it to achieve three things. First, they are trying to raise revenue. Second, they are trying to protect domestic industries from foreign competition. Third, they are sometimes bargaining with other countries to reduce tariffs or retaliating against them by raising tariffs.

Those are the three Rs: revenue, restriction, and reciprocity. When I looked at the broad canvas of U.S. history, those three categories really apply to three different periods of U.S. trade policy history. Although all three elements are always present, to some extent, the question is: Which one is dominant at any given point? From the founding of the country to the Civil War, the debate was really about using the tariff to raise revenue. Under the Articles of Confederation, Congress did not have the power to levy taxes. The federal government was broke and couldn't pay its bills, leading the country toward a crisis. So one of the major reasons for the Constitutional Convention was to give Congress the power to raise revenue. The Tariff Act of 1789 was really just a revenue measure to pay debts and to finance the spending of the federal government. Revenue remains the major issue in trade policy through the antebellum era.

Then, with the Civil War, of course, there is a transition of political power in the United States. The North becomes politically dominant, and it was the home of a lot of import-competing industries. Republicans from the North were overwhelmingly in charge of Congress, and so we get protection as a policy outcome. Once those high tariffs were in place, they become very hard to dislodge for a lot of reasons and they continue for a long time — long beyond when we actually become a net exporter of manufactured goods.

In 1929, we have another shock: the Great Depression that redistributes political power once again, this time away from the protectionist Republican Party to the more pro-trade Democratic Party, which at the time drew much of its political support from the South. Also, we have this trade war after the Hawley-Smoot Tariff of 1930, which leads many people to think trade policy should take a different direction. So President Franklin Roosevelt and Secretary of State Cordell Hull introduce the Reciprocal Trade Agreements Act (RTAA) in 1934 and we move on to this third era of reciprocity where we're willing to reduce our tariffs in conjunction with other countries reducing their trade barriers as well.

EF: The Founders could have looked to other ways to raise revenue. Was the tariff broadly seen as simply the least bad way?

Irwin: Absolutely. There was a consensus among the Founders that it was the most efficient way of raising public funds as well as the most politically acceptable. Consider sales taxes in the early post-colonial period. They were very controversial and very costly to enforce; just think of the Whiskey Rebellion. An income tax just doesn't make sense at this time for many reasons. But imports were coming into a relatively small number of ports, such as Boston, New York, Philadelphia, Baltimore, and Charleston. So it makes sense that if you have a lot of goods coming into a small number of places, you just tax them right there, which is pretty easy to do. In addition, people don't easily see the tax because it's built into the consumer price, so there is less political resistance to it.

EF: Regarding regional cleavages surrounding trade policy, how important do you think the tariff issue was to the frictions that led to the Civil War?

Irwin: You do see the argument out there that trade restrictions were one of the principal reasons the South seceded, not so much among academic historians but among others who write on the topic. I think the tariff issue had very little, if anything, to do with the Civil War. After the 1828 Tariff of Abominations, South Carolina essentially said we're not going to enforce this law and we may withdraw from the union unless the policy is changed. That precipitated a real crisis, and it was defused with the Compromise of 1833 proposed by Henry Clay, which gradually reduced tariffs. From 1833 until the Civil War, tariffs were basically on a downward path. We reduced the tariff further in 1846 and then again in 1857. A year before the Civil War, the average tariff was below 20 percent, which was about the lowest it had been in the entire antebellum period. So the South and the Democrats really held the cards in terms of trade policy right up to the Civil War.

What the revisionists of the Lost Cause group will say is, well, the Republicans assumed power and passed the Morrill Tariff in 1861 and that led to the conflict. But the only reason the Morrill Tariff passed was because most of the South had already seceded after the election of Lincoln. If their representatives had stayed in Congress, they could have stopped it. It wasn't that the South left the Union because of the Morrill Tariff; we got the Morrill Tariff because they left. In fact, it wasn't Lincoln who signed it but the Democrat James Buchanan before Lincoln took office. So I think there's basically no evidence the tariff was a major cause of the Civil War.

EF: At the end of the book you discuss how predictions for U.S trade policy have been really dire. But you offer some caution about such claims.

Irwin: It was a tricky matter for the book because I completed the manuscript in September of 2016. And I had every expectation that Hillary Clinton was going to be elected and there would be significant continuity in trade policy. When Donald Trump was elected, given his extreme rhetoric on trade, many people expected big changes in trade policy. I did have the opportunity to add a few paragraphs on Trump, and as you can see I tried to hedge my bets. If you listen to the rhetoric, it might be reasonable to think that there is a big shift coming for U.S. trade policy. But I also noted that if you look back over the past 250 years, you see that we have had these periods where trade policy sort of veers off and then eventually returns to the old status quo. For example, Democratic President Woodrow Wilson slashed tariffs dramatically and tried to introduce much freer trade, but the Congress soon reimposed high tariffs when the Republicans were returned to power. When you look at what Franklin Roosevelt did with the RTAA, the introduction of trade agreements was a policy of evolution not an overnight revolution. The Reagan administration imposed a lot of protectionist measures in the 1980s, but those restrictions soon faded away.

As a result, I try to suggest in the book's conclusion that there's still a lot of status quo bias in the system. We can't always believe the strong rhetoric, and maybe things won't change as much as promised. And so far, as of August 2017, I think Trump hasn't changed much in terms of U.S. trade policy. Yes, he pulled out of the Trans-Pacific Partnership, but maybe Hillary Clinton would have done so also; Bernie Sanders too. Trump did say he wanted to renegotiate bilateral agreements with these countries. There's no evidence we've moved forward with that but that's at least saying that he's open to the idea of trade agreements. He hasn't pulled out of the North American Free Trade Agreement (NAFTA), although the renegotiation of it is not likely to go well. He might go after China a bit, but consider his announcement: He signed an executive order for the USTR not to initiate an investigation but to look into initiating an investigation. So there's nothing there yet. I think the administration is quickly learning that there is a process, there's a reason why things operate slowly, and you have to work within the laws we have.

Also, any big change in trade policy — in any direction — is going to generate a lot of opposition. In relation to NAFTA, when you look at a map of where U.S. agricultural exports are produced, you see that a lot come from areas that the president carried and a lot head to Mexico. So hopefully government officials begin to realize pulling out of NAFTA would not only reduce imports to the United States, it would also lead to reduced market access for U.S. exporters. There are a lot of trade-offs in any policy change. It's not a black and white process of you stop imports, you create jobs here, and that's the end of the story.

Douglas Irwin

➤ Present Position

John French Professor of Economics, Dartmouth College (at Dartmouth since 1997)

➤ Previous Positions

University of Chicago Graduate School of Business (1991-1997); Board of Governors of the Federal Reserve System (1988-1991)

➤ Education

Ph.D. (1988), Columbia University; B.A. (1984), University of New Hampshire

➤ Selected Publications

Clashing over Commerce: A History of U.S. Trade Policy (University of Chicago Press, 2017); *Trade Policy Disaster: Lessons from the 1930s* (MIT Press, 2012); *Peddling Protectionism: Smoot-Hawley and the Great Depression* (Princeton University Press, 2011); *The Genesis of the GATT*, with Petros C. Mavroidis and Alan O. Sykes (Cambridge University Press, 2008); *Free Trade under Fire* (Princeton University Press, 2002); *Against the Tide: An Intellectual History of Free Trade* (Princeton University Press, 1996)

EF: What do you think about Brexit and what it portends for trends in trade policy?

Irwin: A lot of people have said that it's an indicator of an antiglobalization backlash. Yet I don't believe it represents a backlash against trade per se because Brexit proponents want to maintain Britain's access to the European Union (EU) market and have actually argued for even freer trade outside the EU. So it wasn't an anti-trade movement. I think immigration, regulatory, and sovereignty concerns about the EU were dominant.

If they go through with it, however, Britain could be making a big mistake. First, Europeans are not going to give them free and easy access as they had before. Britain has no trade negotiators because they outsourced that to the EU. So all of a sudden they're looking for qualified staff to negotiate new trade agreements. Second, trade agreements these days are much more about regulatory harmonization and coordination than tariff levels. If you were dealing with only tariffs, that would be much easier to address. But these are really complicated policy measures where you really need a lot of expertise. To pull out of the EU and try to replicate that — not just with the EU but with a whole bunch of other countries — it's going to take a long time to repair those networks. With global supply chains being so important, that can do big harm to one's country if you stand outside the system for a while and then try to get back in.

There's actually a cautionary tale here from the American Revolution. After the United States won its independence from Britain, American leaders thought that the political settlement would restore U.S. access to the markets of the British Empire. They were sorely mistaken: Britain sought to punish the United States by keeping it out of its markets, and the United States paid a hefty economic price.

EF: How would you assess the claim that more restrictive trade policies in the late 19th century fueled industrialization in the United States?

Irwin: This is one of the biggest questions in the history of U.S. trade policy: Did protectionism foster U.S. economic growth and development in the late 19th century? I'm not convinced that we can attribute America's industrial advance in the 19th century to high tariffs or protection. There are a couple points to make on this. There is certainly a correlation between high tariffs and industrial growth in the late 19th century, but we can't leave it at that. That would be a post hoc, ergo propter hoc argument. Instead, we need to know the mechanism by which high tariffs might lead to this growth. Usually the mechanism identified is that agriculture is a relatively low value added per worker sector and with the tariff you are going to shift resources into manufacturing, which is a relatively high value added per worker sector. So not only do you industrialize, but you also raise national income because you get workers into more productive activities. I have done some back of the envelope calculations about how much labor could possibly have moved across sectors as a result of the tariff, and the numbers are pretty small in terms of any possible gain. And, actually, this intersectoral switch is happening anyway. It's a natural process. A lot of the industrialization occurred prior to the Civil War, between 1840 and 1860 when we had low and declining tariffs. A lot of the growth in the late 19th century when we had high tariffs is extensive growth, not intensive growth. In addition, there are so many other things going on. We had open immigration, so there was a lot of growth in the labor force. We revamped our banking laws during the Civil War, finance became very important, and we got capital deepening. That's not because of the tariff; that's because the whole financial system of the United States was really developing.

Another point to be made is that when you look at the high productivity growth sectors in the U.S. economy in the late 19th century, John Kendrick and others have shown they're mostly in the non-traded goods, service sector. Transportation and utilities were growing very rapidly. It's hard to see how the tariff would help the non-traded goods, service sector of the economy improve its performance. Also, Steve Broadberry has done some work showing that increasing productivity in the service sector was very important to the United States catching up with Britain in the late 19th century. That, too, doesn't seem to be tariff related. All of this doesn't lend itself to an easy story where the tariffs are the key factor behind U.S. growth and industrialization.

In addition, when you look at particular manufacturing industries, such as iron and steel or textiles, once again the story doesn't seem to be particularly strong. For example, I once looked at the tinplate industry. It's true that we didn't have tinplate production until the McKinley Tariff, but the reason we didn't have it was because we had high tariffs on imported iron bar, which is an important input to tinplate. So you had a high cost of production on your intermediate goods and that hurt downstream producers. When you look at the whole tariff code in the late 19th century, it's not geared toward the production of final manufactured goods. There are high tariffs for everyone, including on intermediate goods, and you're not really helping out downstream producers when you do that.

EF: It is often asserted that the Hawley-Smoot Tariff played an important role during the Great Depression. What is your view?

Irwin: I would say most economists have been skeptical of the claim that the Hawley-Smoot Tariff led to the Great Depression or even exacerbated it to any great extent. In their *Monetary History of the United States*, Milton Friedman and Anna Schwartz hardly mention the tariff at all.

Whenever Friedman talked about the Great Depression, he always said that it was a very bad piece of legislation, but it didn't cause the Great Depression, it didn't generate 25 percent unemployment. I think that's basically true. There is something else going wrong in terms of monetary policy or other macroeconomic factors that cause depressions. Tariffs change relative prices and reallocate resources between industries but don't change the level of activity to that extent. There's a lot of evidence for that through history. For instance, in 1922 Congress passed the Fordney-McCumber Tariff, which raised tariffs more sharply than even the Hawley-Smoot tariff, and yet an economic boom followed. Now, the tariff certainly had nothing to do with that boom, as the economy was recovering from tight monetary policies after World War I. But the point is we have had a lot of tariff increases in the past that didn't lead to depressions and a lot of tariff reductions that didn't lead to booms.

My view of Hawley-Smoot is that it was unnecessary, it was ineffective, and it was harmful. It was unnecessary because it was introduced in the House at a time of almost full employment, the spring of 1929. It was ineffective because the motivation was to help out farmers, but we were a big net exporter of farm goods so the domestic price that they faced wasn't going to be affected by import duties. It was harmful because it led to a lot of retaliation against the United States, so our farm and factory exports were actually harmed.

EF: In addition to legislation like Hawley-Smoot, you and Barry Eichengreen have looked at some other factors in the rise of protectionism during the 1930s.

Irwin: Everyone knows a trade war broke out in the 1930s. But what really caused it? The standard explanation is that there was chaos and that everyone was trying to protect their own market in light of the Great Depression. We found something different. There is a very pronounced pattern in terms of which countries were adopting protectionist policies and which weren't. That hinged on something that naturally follows from Barry's work — how long you stay on the gold standard.

There's a trade-off that different countries made. If you are being confronted with a deflationary shock, you can use monetary policy to adjust to that. But if you're on the gold standard and the hands of the monetary authorities are tied, you look for other policy instruments to try to prevent gold outflows and reflate the economy. Trade policy is one of them. So what you find is some countries are breaking off the gold standard very early and they pursue reflationary monetary policies. They are able to mitigate the worst effects of the depression and they don't face as much protectionist pressure. In contrast, there are other countries that stay on the gold standard and their economies remain relatively depressed. Those are the ones precisely where the protectionist pressures are really strong, and they impose exchange controls and higher tariffs and things of that sort.

EF: Why do you think protectionism has such enduring appeal, at least rhetorically?

Irwin: I think protectionism has always had a lot of appeal because, politically, it's sort of an "us versus them" situation. You're helping out your domestic firms against foreign firms that are stealing our jobs. It is a nationalistic view that many people naturally have a desire to try to help one's neighbors first.

Also, with protectionism it's easy to see who's helped and harder to see who's hurt. There are tangible benefits to some group when you erect a trade barrier, but it's much harder to see those who are harmed or pay the price. It's a bit of a case of the seen versus the unseen. One way I try to illustrate this in my classes is to explain one of the most fundamental theorems of international economics, the Lerner Symmetry Theorem. It states that a uniform tax on imports is equivalent to a uniform tax on exports. But just think about how this plays in the public mind. If you went out into any city and asked people whether we should impose an across-the-board tariff on imports to protect jobs and stop foreign countries from taking advantage of us, a lot of people would support that. But if you went to the same people and asked whether we should impose a uniform tax on all exports, on all farm exports and manufactured exports, there would be very little support for that. But the Lerner Symmetry Theorem says they're equivalent. So it's the same policy, but how you frame it determines the response you will get.

EF: What are your thoughts on the paper by David Autor, David Dorn, and Gordon Hanson arguing that rising Chinese import competition has had significant effects on U.S. manufacturing?

Irwin: I think it's an important contribution because it shows us some of the real difficulties in terms of labor market adjustments to big shocks. The finding that people drop out of the labor force, retire early, or go on disability and don't necessarily move on to other jobs is an important finding. While I think economists will debate the number of workers who have been displaced because their estimate is based on cross-sectional evidence, which is not the ideal way to do it, we can be pretty confident that the number is big. That said, here's my take on it. First, the China shock was a one-time shock. That is, you had big growth not just in trade but in a shift of people from agriculture into industry in China, at the same time as the working-age population was growing. That's not going to repeat itself. The rural to urban transition has slowed dramatically, and the working-age population in China is now actually in decline.

It also was not an aggregate demand shock. Even though they identify significant harm to certain communities in the 1990s and 2000s, those were periods of declining unemployment in the United States. So it really draws attention to the problem with geographically concentrated production and the difficulties of getting workers to move to different locations or to different industries. In this regard, I would differentiate between the 1990s and the 2000s. Autor, Dorn, and Hanson suggest the China shock was occurring throughout this whole period, but at the end of the 1990s we had an unemployment rate below 4 percent with significant wage growth at the lower end of the wage distribution. There's actually some evidence that workers in textile mills in the South who were displaced were getting higher-paying jobs elsewhere. The 2000s is a different period, the economy was far less robust than in the 1990s, and the 2008 financial crisis just compounded the problems for displaced workers. Also in the 2000s you had huge macroeconomic imbalances in China. We had a pretty sizeable current account deficit during the 2000s, while China had a current account surplus of 10 percent of GDP. It's highly unusual for a large developing country to have a massive trade surplus like that, which raises the issue of currency manipulation and so forth. I don't think that we are going to see something like that again, in terms of trade imbalances, and if we begin to go in that direction, there should be enough warning signs and policy will be different.

In short, the China shock was a big one-off event that happened under unusual circumstances and is unlikely to be repeated. We have learned a lot from it, but going forward I don't think it changes the consensus that there are still large benefits to trade. We have always known that certain communities or certain types of workers are going to be hurt by trade. This just happened to be a pretty big example. More recent research has also provided some context or some nuance to what they found. For instance, work by Rob Feenstra and others has tried to pin down the benefits to consumers from lower prices, particularly workers at the lower end of the income spectrum. In addition, some of the China shock was due to China's unilateral reductions of tariff on inputs, which made its final goods producers much more efficient. That's not due to a change in U.S. policy — that's just China becoming more open and more efficient, which ultimately is something we want to see.

EF: I know you have just finished a massive book, but I was wondering what you are working on currently.

Irwin: I'm really excited about my next project, which is looking at the political economy of trade policy reform in developing countries. Arguably the biggest change in the world economy over the past 30 or 40 years is the increased participation of developing countries and their unilateral decisions to open up and become part of the world trading system. The biggest, of course, was China, which wasn't because of the World Trade Organization or external pressure. Rather, in 1978-1979 Deng Xiaoping decided to open up the economy. It was a unilateral decision — and that has been the story for a lot of developing countries.

There has been a lot of work looking at what happens when you go from a closed to an open economy. Sachs and Warner had a famous Brookings paper in 1995 that was improved upon by Wacziarg and Welch. And there are many others now using synthetic control methods to sort of simulate what would happen to a country if it hadn't opened up. Basically all of these papers identify pretty big effects to GDP, to investment, and obviously to trade. There is heterogeneity, of course; not everyone is going to get a big boost from it, but, on balance, a pretty significant positive impact. So the question I want to address is what was behind the decision of those countries to open up or not. What I'm doing is looking at various countries in terms of their political decisionmaking process, starting with Taiwan in the late 1950s, which was really the first developing country to open up, then Korea, then Indonesia, then Chile, and so forth. New Zealand enacts big trade reform in 1984, and there are a lot of countries in the late 1980s and early 1990s. My initial read is that it's not so much that these countries' policymakers, backed by some economist, are thinking about the comparative advantage gains from trade or things of that sort. What they're finding is that they have these import substitution policies and overvalued exchange rates, which have stifled their exports, and now their exports can't pay for their imports. And it's not that they want to keep out imports. They desperately want to import things like food and fuel and especially capital goods. But they don't have the exports to pay for them. So they need to do something to stimulate exports. That requires a devaluation, usually a big devaluation, and reducing tariffs, which through the Lerner Symmetry Theorem acts as a brake on exports.

The reason why Taiwan and Korea initially moved in a more open direction is that the United States was cutting back their foreign aid. They had huge trade deficits that were financed by U.S. foreign assistance. By the late 1950s the United States was saying we're in the postwar period now, you're not being threatened militarily, and so you're on your own. The countries realized, well, we can't cut our imports and our exports are virtually nothing. We've got to do something about this, and that's why they shifted their policy. It's fascinating to see the pressure that U.S. aid withdrawal puts on foreign officials to rethink their policies. Also, sometimes it's the International Monetary Fund (IMF) providing advice but not necessarily a club over their heads. And often there are policymakers groping for a solution who have been influenced by an economist. When you get that sort of link, you sometimes can bring about these significant changes in trade policy. So in the case of Taiwan it was Sho-Chieh Tsiang, who was then an economist at the IMF and who later taught at Rochester and Cornell. The chief economic minister asked for a memo on what they should do. Tsiang went there and said devalue and open up. That's what they did, and the results were astounding. **EF**