

## THE PROGRESS REPORT

### **More Free Trade**

By Fred E. Foldvary

President Clinton has visited South America in an attempt to move forward efforts towards extending NAFTA to South America and to boost American exports to Latin America. The prospect of reducing trade barriers with Latin America stirs up fears of further losses of jobs and industry to areas with cheaper labor. The basic question is, does free trade help or hinder the American economy? When a high-wage industrialized country trades with a low-wage less developed one, does the high-wage country become worse off?

These are ancient questions. Henry George wrote the book *Protection or Free Trade* in 1886, yet reading it makes one realize how little things have changed since then. Americans were worried about competition from cheap labor then as now. Somehow, the American economy has managed to survive despite this competition.

Henry George pointed out that those who fear that American wages will drop with free trade fail to ask the primary question: what determines the level of wages in the first place? The answer is that wages are determined by the productivity of labor. American wages are high because of the high level of technology and the relatively efficient organization of production. U.S. wages would be even higher if wage taxes and excessive regulations were eliminated. Free trade will not reduce the technology of U.S. industry, nor will it discombobulate our organization. If the aim of the critics is to increase American wages, why are they not advocating shifting taxes from wages to land rent? As Henry George said, true free trade includes the elimination of domestic as well as international barriers.

There is another reason why free trade would not hurt wages. Suppose China could produce everything cheaper than the U.S. Would all American industry collapse? No. If it takes 2 labor hours to make \$100 worth of computer and 3 hours to make \$100 worth of televisions in the U.S., and 1.5 hours to make \$100 of computers and 1 hour to make \$100 of television in China, would both be made in China? No, because China won't sell unless it can get something in return. Even though China has an absolute advantage, each country can still gain by concentrating on its comparative advantage. If the U.S. only makes computers and trades them for televisions, the U.S. saves 1 labor hour per \$200 of output, and if China only makes televisions, China saves a half hour of labor. Workers in the U.S. television industry would be out of work, but they could then shift to the computer industry.

There are gains from trade when any voluntary exchange takes place. The global movement to reduce trade barriers has contributed to the global economic boom we are enjoying. The problem with NAFTA, the World Trade Organization, and other trade agreements is that they are not pure free trade. Many special interests are being paid off and given privileges in order to pass the agreement through Congress. The agreements are complex and full of exceptions. Some fear that the clauses protecting the environment are not thorough enough and are not being well enough enforced. Local government may be unduly restricted.

The question is then whether the overall effects of trade agreements are beneficial or harmful. The GATT and NAFTA agreements have led to more trade and more prosperity. The rejection of further trade liberalization can have negative international political consequences. Latin America, for example, is now trading more with Europe and less with the U.S. It is probably better to keep on reducing trade barriers, and then eliminate the complexities, restrictions, and loopholes later.