The Elemental Case for Free Trade

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The case for free trade is simple.

First, nothing about political borders justifies treating trades that cross those borders differently than trades that don't. Whatever benefits result from you trading with someone in Kentucky are no less available when you trade with someone in Korea. Whatever *problems* – real or imaginary – are caused by you trading with someone in Korea are no less likely when you trade with someone in Kentucky.

Second, all economic activity is ultimately justified by how much it enables us to expand our *consumption*, not by how much it enables us to expand our production. Consumption is the end; production is the *means*. Of course, production is an essential means; we cannot expand consumption without expanding production. But production it is not the ultimate purpose for economic activity. If you disbelieve me, ask yourself how much you'd pay for a sawdust-nail-'n'-cardboard pie that took its well-meaning baker several days to produce? If you answer "nothing," then you get this point.

Third, specialization expands output. And the greater the amount of specialization, the greater the output. A medical profession made up only of family physicians will save fewer lives and reduce less pain than a medical profession made up of specialists such as neurosurgeons, podiatrists, ophthalmologists, and – my favorite (because many years ago one of these saved my young son's life) – pediatric gastroenterologists.

Fourth, specialization requires trade. A Manhattan-based pediatric gastroenterologist today enjoys a high standard of living, but only because many people willingly pay him to specialize in that highly specialized line of work *and* willingly accept his money in exchange for what they produce. This physician is rich only because he trades with others. If farmers, carpenters, tailors, and airline pilots were unwilling to trade with him, he'd have no time to practice pediatric gastroenterology. He'd instead have to grow his own food, build his own home, and make his own clothing. He, and the rest of us, would be much poorer.

Fifth, specialization increases with the size of the market. The greater the number of consumers and producers, the larger is the scope for each producer to focus on a narrow specialization. This fact is why large cities have niche restaurants, such as vegan Lebanese, and highly specialized physicians, such as pediatric gastroenterologists, while small towns don't feature restaurants and trades so highly specialized.

Points four and five working together spark self-reinforcing improvement: more trade promotes more specialization which, in turn, promotes more trade. Economies grow and standards of living improve.

Sixth, expanding the area of trade – increasing the size of the market – results in what economists call "increasing returns." Doubling the number of people who trade freely with Americans causes the GDP of this larger economy to *more than* double. *Per-capita* GDP rises for all of these people who trade freely with each other. Again, compare medical care with nothing but family physicians to medical care with many specialists.

Seventh, there's no limit to the degree to which labor can specialize and to which, as a result, total output can expand *and expand at an increasing rate – that is, exhibit increasing returns.* Put differently, the degree to which labor can specialize and cause total output to expand isn't limited to, or defined by, the size of any particular country. Nor does the size of any particular country define a point beyond which the growth of specialization and output slows or becomes less reliable.

That is, even in a country as geographically large and as heavily populated as the United States, nothing in economic theory or history suggests that expanding the boundaries of our trading patterns externally – that is, beyond our borders – results in less expansion of our consumption and production than when we expand the boundaries of our trading patterns internally. We in Georgia or Virginia stand to gain just as much by expanding our trade with Mexicans as we stand to gain by expanding our trade with New Mexicans. There's no reason not to have a *global* economy without economic boundaries.

Eighth, economic competition is good and it works just as effectively *across* political boundaries as it does *within* political boundaries. Competition disciplines firms, it spurs entrepreneurial creativity, and it discovers and encourages – much like a process of natural selection – what works best economically. Importantly, the competition that comes from free trade directs workers and other resources into those lines of productive activities at which each is most efficient. There's simply no reason to neuter with trade restrictions the competition that comes from abroad simply because that competition isn't home-grown.

Ninth, as Julian Simon taught, human beings in market economies are the ultimate resource. The ultimate resource isn't land or petroleum or deposits of iron ore or of gold; it's not factories or software or tractors; it's not inventories of wheat or of rolled steel or of cash on hand. It's human creativity and ingenuity. Indeed, it's only because human creativity made them so that petroleum and iron ore and wheat and you name it are resources. Without human creativity these things would be mere raw materials, mere stuff, that's no more valuable or useful to human beings than they are to antelopes and hamsters.

And yet human creativity is one of the few resources that has consistently gotten more scarce over the course of the past 250 years.

We know that human creativity has gotten more scarce because its market price has risen enormously over the past few centuries in the market-oriented world. For example, the real hourly pay of the average American worker is today about *60* times higher than it was in 1790.[1]

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[1] Calculated from data found at: https://www.measuringworth.com/datasets/uswage/result.php
and adjusted for inflation using:
http://data.bls.gov/cgi-bin/cpicalc.pl

This rise in the price of labor signals that it is has become more scarce *relative to the demand for human labor.*

In contrast, most other resources and productive inputs – including energy, metals, and transportation services – have become, and are still becoming, less scarce, if we judge them (as we should) by the trends in their real prices. They're becoming less scarce precisely because we have more creative human beings contributing to the market economy.

Free trade maximizes the ability of the people of a country both to contribute their own creativity and effort to the global economy and to tap into the creativity and effort of the billions of other ultimate resources that reside in other countries. We tap into that creativity directly when we offshore productive tasks to foreign workers. We tap into it indirectly when we buy goods produced by foreign workers and entrepreneurs. Why would we wish to artificially reduce our and our fellow citizens' access to supplies of the ultimate resource?

Tenth, restrictions on trade inevitably are driven by special-interest-group politics. Even if a sound theoretical case can be made for trade restrictions, it's simply unrealistic to expect the state to be guided by that case. Instead, the state will only to use that case as cover to create monopoly privileges for politically influential producer groups.

That's it. That's the elemental case for free trade.

But there's a second part to the case for free trade. It's the part that's been constructed in response to the multitude of misunderstandings that have arisen over the centuries with regard to trade.

This second part to the case for free trade is the longer part. The reason is that the capacity for misunderstanding and mischaracterizing trade is enormous. Many falsehoods require many corrections.

Here I've time only to mention a few pieces of this second part of the case for free trade.

First, over the long-run free trade causes no net loss of jobs. Put differently – and harkening back to a point made above – *any* change in consumer spending causes some workers to lose jobs while creating jobs for other workers. International trade isn't unique on this front. The jobs lost today to imports are replaced tomorrow by other jobs.

And these other jobs are, overall, better than the lost jobs because they are the ones at which the workers in the country have a comparative advantage. The jobs lost are ones at which the workers have a comparative disadvantage.

If you worry that the loss of particular jobs today cannot be made up for by the creation of new jobs, consider that in 1950 the size of the U.S. workforce was 60 million, with roughly 59 million jobs. Today, the size of the workforce is about 160 million, with about 152,000 jobs. In 66 years, the number of workers and the number of jobs in America have each increased by a bit more than 150 percent. The rate of unemployment today is not-too-shabby five percent.

The number of jobs is determined not by the freedom of trade but by the size of the labor force and by flexibility of labor markets. What free trade does is to replace bad jobs with good jobs; protectionism protects bad jobs by preventing the creation of good ones.

Another objection to free trade is that it is undesirable if it creates trade deficits. This is an egregious fallacy, because another name for trade deficits is "capital surpluses." Every cent of a U.S. trade deficit is a cent invested by foreigners in America or in dollar-denominated assets. These investments not only return the dollars to the U.S., they also signal that the U.S. is a relatively attractive place to invest *and* by enlarging our capital stock, they enrich us.

If commenters started referring not to "our trade deficit" but to "our capital surplus" – an exactly equivalent term – there'd be much less misunderstanding and mischief.

Finally here, it's a myth that high-wage Americans can't compete against low-wage foreigners.

Specialization arises according to *comparative* advantage, which doesn't stop operating as the wages of workers in a nation rise relative to wages elsewhere. But this point is esoteric. Another point is that low wages reflect low productivity. Americans' wages are higher than Chinese wages because American workers on average are more productive than Chinese workers. So next time someone says "We can't compete against low-wage foreigners," translate that claim into its equivalent: "We can't compete against low-*productivity* foreigners." The latter claim sounds as silly as it really is.

There is no good argument against free trade.