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PROTECTION, NOT A CRASHING STOCK MARKET, IS THE SPECTER OF 1929

(Updating *Issue Bulletin* No. 130, "S. 490: Protectionism's Dangerous Loaded Gun," June 16, 1987.)

The stock market crash of October 1929 may have provoked a financial economic crisis, but it was trade protectionism and higher taxes which followed that turned the crash into the Great Depression. Apparently learning nothing from history, Congress today seems bent on repeating history. Fears of current protectionist trade legislation no doubt contributed to the crash of October 1987, and enactment of the legislation would certainly lead to recession. If Congress wishes to reassure the financial community and avoid economic disaster, it should scrap the ill-conceived trade bill.

The one thousand-page trade bill is currently being ironed out in joint committees of Congress which include 199 members--each with powerful constituencies eyeing their votes. Predictably, the bill is a nearly incomprehensible jumble of protectionist prescriptions and special interest regulations and handouts. Example: sugar producers, already heavily subsidized and protected, would gain yet new subsidies from the U.S. Treasury. Example: federal restrictions would be placed on layoffs and factory closings, making American businesses even less competitive. Little wonder that investors on Wall Street have been voting with their pocketbooks against this legislation.

Arbitrary Definitions. Parts of the trade bill are explicitly protectionist. Example: the Gephardt Amendment would mandate trade retaliation against countries with arbitrarily defined "excessive" trade surpluses. Example: another part of the bill would limit severely the President's discretion to judge whether an industry harmed by imports warrents protection. The Reagan Administration is working to remove such measures from the bill. The danger is that much of the legislation, which redefines trade laws to make it easier for certain inefficient American firms to restrict imports, will remain.

Despite all the rhetoric about the need for "fair" trade, the bill seeks not fairness but special favors for some American firms, with little regard for the American consumer. Example: the formula used to determine whether a foreign industry is dumping--that is, selling its product below its own costs of production--is rigged by the Hollings Amendment to make the price of an item appear lower in the U.S. so that dumping can be "proved" even where it does not exist. Example: another provision redefines an "industry" for purposes of determining injury due to imports. An industry's profitable foreign operations would be excluded from the definition so that a healthy U.S. industry might appear "sick" under U.S. trade law and thus receive trade protection. Example: a provision allows a U.S. industry suffering economic harm due to a recession to obtain protection from imports, even when imports are not the primary cause of its problems. Much of the trade bill consists of such provisions to make it easier for special interest business groups to restrict the freedom of American consumers to purchase the goods they want.

In 1929, fears generated by the congressional consideration of the Smoot-Hawley tariff bill contributed to the market crash. While by 1930 the market had regained all the ground it had lost, U.S. policy makers had not regained their economic sense. They enacted Smoot-Hawley that year and President Herbert Hoover signed the tariff into law, ignoring a petition by 1,028 leading economists urging him to veto the bill. Backing protection was Senator James Eli Watson, an Indiana Republican, who predicted that the U.S. "will be on the upgrade financially, economically, and commercially." In fact, the result was the Great Depression. Between 1929 and the tariff's repeal in 1934, an international trade war caused U.S. exports and imports to plunge by 66 percent, pushing unemployment to nearly 30 percent and cutting the Gross National Product by half.

Economists' Warnings. Today there is virtually no expert, academic, or intellectual support for protectionism. An open letter, signed last year by every living past chairman of the President's Council of Economic Advisors since 1953, Democrat and Republican, liberal and conservative, blasted the myths that protectionism saves U.S. jobs, reduces the trade deficit, and strengthens the industrial base. By failing to heed the lessons of history and the warnings of nearly every independent economist, protectionists in Congress poorly serve their constituents and the country as a whole by inviting economic disaster.

A few pro-trade provisions of the bill, such as the granting of authority for the Administration to negotiate trade liberalization under the General Agreement on Tariffs and Trade and approval of a harmonized system of international tariff accounting, are economically useful. These could be enacted through separate legislation. The rest of the bill is dangerous to America's economic interests. If Congress wishes to avoid the mistakes of 1929 and restore confidence to U.S. financial markets, it could do no better than to scrap the current self-destructive trade legislation.

Edward L. Hudgins, Ph.D.
Walker Senior Policy Analyst
in Economics and Director of
The Center for International Economic Growth