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Implications of the Results of Individual Studies

Anne O. Krueger

The experience with protectionist pressures and protection in the seven industries reported on here, along with the cross-section evidence gleaned from International Trade Administration–International Trade Commission (ITA-ITC) cases, suggest a number of hypotheses.

For economists, some of the important lessons emerge from conclusions regarding the determinants of protection. The Staiger-Wolak findings, the analysis of decisions regarding lumber, the determinants of influence in affecting NAFTA, and, indeed, all the other studies point strongly to the influence of political strength (generally unrelated to considerations of static or dynamic efficiency and even to income distribution arguments often heard) as a major determinant of protection. This appears to be so even for the administered protection processes, which in theory are governed by legal considerations set out in law.¹

From the perspective of politicians and policymakers, this conclusion will hardly appear surprising. From the viewpoint of the public interest, however, it raises significant questions as to the feasibility of devising institutions or mechanisms which can differentiate between those seeking protection out of narrow self-interest and those cases in which industrial protection might be warranted because of the sorts of considerations to which the “new trade theory” points. For economists concerned with framing policy, therefore, questions as to the capacity of the political process to be constrained in ways which enable trade policy to respond to broader interests must be addressed.

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1. But the law itself permits the International Trade Commission only to consider factors *within the industry* in determining outcomes: from the viewpoint of economic theory, evaluation should surely take into account the effects on the American economy as a whole, and not simply on the industry receiving protection.

In the volume arising out of the project, these and related issues are dealt with at much greater length. Here the focus is on the findings from the individual studies relevant for the policy-making community regarding current trade policy formulation and practice.

A starting point must be a brief survey of the salient findings from the individual studies. Thereafter, I address the key questions they raise for policy formulation and execution.

9.1 Findings from Individual Studies

9.1.1 Automobiles

From a policy perspective, perhaps the key findings arising from the auto study center on the effects of protection on the industry. It seems clear that voluntary export restraints (VERs) on Japanese automobiles did not achieve the results the automakers apparently hoped for: on one hand, the VER was largely offset initially by a decline in demand (as a result of the recession), thus making the VER ineffective, and later it resulted in higher profits for Japanese companies (thus strengthening their competitive position) as well as increased imports from other countries. Nelson's analysis convincingly demonstrates that the turnaround for U.S. automakers was a result of competition, and not of protection per se.

It should also be noted that VERs were adopted when administration officials began to be concerned that congressional pressures would otherwise result in an even more protectionist outcome: there were bills pending in Congress that would have mandated even more restrictive measures governing auto imports than the VERs on Japanese automobiles. Thus the fact that VERs were employed does not at all prove that the administration was in the forefront of those seeking more protection: the administration moved to forestall congressional action.

9.1.2 Steel

Like automobiles, steel appears to have been experiencing economic difficulties in large part because the earlier high degree of industry concentration and world preeminence had left it very comfortable, unaccustomed to responding to competitive challenges from other sources of supply.

There are several other aspects of the experience with steel that are of interest. First, it is not evident whether the various protectionist measures imposed on steel imports did in fact help the domestic industry. Second, a new technology—the emergence of minimills—resulted in greatly reduced cohesion within the industry in seeking protection. Moreover, some steel users became active opponents of steel protection. This is a clearcut case where the “indirect”

effects of protection are important, and the only instance in the seven studies where using industries became at all significant as opponents of protection. Third, when the steel industry was still cohesive in seeking protection, it used the administered trade processes, antidumping and countervailing duties, as an instrument to induce the executive branch to take action. Finally, the effectiveness of a well-organized and cohesive industry effort (for or in the case of steel users, against) in lobbying for a desired outcome was certainly important in the steel industry.

9.1.3 Semiconductors

The semiconductor industry represents another instance where administered trade processes were used to induce the American and Japanese governments to agree upon a VER rather than permit the administered protection process to reach its conclusion. It also represents another instance in which a number of questions may be raised as to whether the protection that resulted helped the U.S. industry: profits were increased for existing Japanese firms, thus enabling them to invest in the next generation of chips that much sooner; third-party effects were important as Korean firms were attracted into the industry by the higher world prices; and Japanese firms located plants within the United States to avoid U.S. protection.

Although the opposition of downstream users of semiconductors proved important in limiting the extent of protection, the semiconductor negotiations raise significant questions as to the extent to which U.S. trade policy can be driven by the interests of one or a few firms. As Douglas Irwin notes, at one point, the position of the U.S. Trade Representative (USTR) was that of one firm (Micron), and the industry held virtual veto power over negotiated agreements.

9.1.4 Textiles and Apparel

The very fact that the textiles and apparel industry has been protected since the mid-1950s raises questions about the efficacy of protection as an instrument to achieve the goals desired by the industry. Employment was declining before the industry received protection; when it did receive protection, new plants opened in the South but plants in New England closed. One analysis suggests that protection accelerated the rate at which the industry relocated to the South (Isard 1973).

The evolution of the protection of the industry also attests to the extent to which an instrument, once in place, tends to become more complex over time as more and more groups attempt to seize it for their own purposes. Finally, J. Michael Finger and Ann Harrison point to the coherence of the industry's organization and lobbying activities: they attribute some of the restrictiveness of the Multi-Fibre Arrangement (MFA), as well as its perpetuation, to that effectiveness.

9.1.5 Lumber

As Joseph Kalt demonstrates, Canadian policy toward lumber results in in-tramarginal transfers, but economic analysis demonstrates fairly clearly that it does not affect exports to the United States. Despite that, the U.S. industry has been able to appeal to the administered protection process to achieve protection which, in that instance, Kalt judges to be of substantial benefit to the industry by raising the United States' price of lumber.

In evaluating the arguments that are effective in achieving a ruling favorable to the industry seeking protection, Kalt finds that the political influence of the participants is a significant factor in determining the outcome: that is, when the potential gains from winning are significant and the group seeking protection is politically influential, protection is more likely to follow from the process.

9.1.6 Wheat

The wheat Export Enhancement Program (EEP) subsidizes wheat exports. The economic benefits to wheat growers are small relative to the cost of the subsidies, and the question is why, in the absence of a strong rationale, these subsidies have persisted since their initial introduction.

Bruce Gardner points to the unity between the farmers and agribusiness as a key factor in achieving continuing support for the EEP. Notably, also, domestic wheat users have not opposed the program. The fact that EEP supporters are well organized and effective in their political representation has been important. It is also significant that the program was found to be budget-neutral (because of the existence of large government stocks), which enabled Congress to support the program without budgetary consequences.

9.1.7 Agriculture in NAFTA

Whereas the EEP affects only one group of farmers, negotiations over NAFTA potentially affected many groups. Analysis of the positions of various farm groups and the determinants of the degree to which groups received benefits under NAFTA is therefore informative as to the relative strength of different groups.

Perhaps the most significant result to emerge from an analysis of the factors influencing the outcome for different agricultural commodities under NAFTA is the starting point for David Orden's analysis: it was predetermined that, at the end of a (fairly long) transition period, all agricultural protection between the United States and Mexico would be removed. That decision, in an important way, set the agenda and determined the context in which various agricultural groups could attempt to influence the outcome: they could slow down the process but not stop it.

A second significant result of the analysis of the determinants of NAFTA is the extent to which those who remained "moderate" until the final moments

before the NAFTA accord reached Congress were able to extract relatively large gains (in terms of their narrowly defined self-interest) in return for their support. Sugar producers, for example, did well because of their willingness to compromise.

9.2 Questions for Policymakers

From the perspective of policy analysis, these findings raise several key issues. First is the extent to which protection achieves the results its supporters hope for, even within their own industries. Second is the extent to which current U.S. trade law and implementation appropriately reflect U.S. interests and, related to that, the questions that arise regarding the frequent failure of user groups to be represented when policy is formulated. Third, the importance of industry unanimity and the absence of opposition from user groups as an important determinant of protection raises a number of questions. While “political strength” matters greatly to an industry’s ability to receive protection, that strength can rest on factors other than industry size or even the importance to the industry of receiving protection. Political strength can result from being strategically positioned in the middle of an issue—those in such a position may not be the ones with the most to gain or lose. Fourth, direct winners and losers from protection are not all equal in their attempts to influence the process. In that sense, good lobbying, effective organization, and the means of seeking political representation all matter. Finally, from several of the studies it emerges that once the battle for protection is initially won, the barrier to continued protection is greatly reduced.

9.2.1 Does Protection Help the Protected Industry?

There has been protection for textiles and apparel since the mid-1950s. The first such measure was termed the “Short-Term.” Despite that, the industry has chronically complained that protection is “inadequate” and does not “help enough.” Despite increasing restrictiveness, especially in the late 1980s, protests from the industry have not diminished.

Protection for automobiles (also in the form of voluntary export restraints) does not appear to have reversed the fortunes of the U.S. automobile industry: Douglas Nelson concludes that competition was the important stimulant.² The same questions can be raised about the semiconductor agreement (although industry representatives appear to believe that they were assisted by the semiconductor agreement). For steel, a technological change—the emergence of the minimills—seems to have been important in affecting the industry: it is questionable how much the old integrated mills benefited from VERs on steel

2. See Scherer (1992). Scherer notes that firms in general react more “passively” to foreign competition when trade barriers are in place and, because of that, have less satisfactory performance.

imports. Even in the case of wheat, Gardner believes that the Export Enhancement Program arguably did little for wheat growers, and certainly did less than their enthusiastic support for the program suggests they believed it would.

Among the protected industries studied in the NBER project, then, there is only one instance in which the author believes that U.S. producers unequivocally benefited: lumber. In all the others, it cannot be persuasively argued that the protection accorded an industry was important in turning its fortunes around.³ This does raise important questions about the efficacy of protectionist trade policies, even in assisting the industries that seek protection. To the extent that trade barriers give producers false assurances, they may indeed be counterproductive from the industry's perspective in the long run.

9.2.2 Does Current Trade Law Reflect U.S. Interests?

There are powerful grounds for arguing that the United States is so important in the international economy that its actions significantly affect the actions undertaken by its trading partners. Certainly other countries have recently been adopting "unfair trading" laws covering countervailing duties and antidumping that are patterned after U.S. law.⁴

The United States clearly has a systemic interest in an open international trading system that by far outweighs the benefits (if any) that can be achieved from individual affirmative findings in administered protection cases, the imposition of VERs, and other protective measures. Even if protection through any of these channels could be shown unequivocally to benefit the American economy, questions could still be raised about the total effect when repercussions on foreign countries are taken into account.

Quite aside from that overarching concern, however, there are grounds for concern about the impact of protection that are not recognized in political debates about trade policy and in the criteria used in U.S. trade law for determining whether protection is warranted. A first and obvious omission, long noted by economists, is that the interests of final consumers are not represented. In political debates, this is no doubt a reflection of the organization costs among large numbers of individuals, each of whom has a small amount to gain if a particular product's price is lower.

However, even more surprising is the fact that under U.S. trade law, the ITC is not empowered to take consumer interests into account in its findings with respect to administered protection. Moreover, the ITC is not even permitted to

3. NAFTA is only now going into effect, and therefore the question of the benefits to different agricultural groups cannot be addressed.

4. There are a number of criticisms that can be made of U.S. trade laws, in addition to those made here. Chief among them are: (1) the law is administered in ways which provide protection even during the period when litigation is proceeding—the Staiger-Wolak finding; (2) the procedures for construction of costs, and other aspects of administrative procedures, can result in findings of "selling below cost" even when the foreign firm is not doing so; and (3) there are circumstances in which foreign firms can be found guilty of practices which, if adopted by an American firm, would be legal. See the essays in Boltuck and Litan (1991).

consider the impact of protection on *other American industries*, including users of the product.⁵ Thus, even if economists could convincingly show that the effect of protection on other American industries was quantitatively more harmful (because, for example, of a loss of competitiveness vis-à-vis imports) than the benefits⁶ to the prospectively protected industry, that would not constitute sufficient evidence to reject protection.

It should be noted that the failure to consider the “general equilibrium” consequences of protection is a characteristic of political debates on protection as well. Debates over protection for steel and machine tools come to mind as particularly telling examples where the products are purchased primarily by other producers and increased prices inevitably raise their cost structure. But the experience with semiconductors—where producers of personal computers discovered that they would be at a significant disadvantage vis-à-vis their foreign competitors—also vividly illustrates the point.

Even when users are not concentrated in a few industries, the effects on other industries of raising costs can be significant. Yet in all these instances, the political process treats protection to the industry seeking it as something that can be accomplished without harming other sectors of the American economy. Not only is protection itself an economic act of discriminating against the many in favor of the few, but the political and administrative criteria used for awarding protection are biased in that direction. While it might be the case that, for example, society deems that the benefits of protection to apparel exceed the costs, a procedure (or rules of political discourse) which at least permitted these costs to be taken into account would be far preferable to present practices.

9.2.3 There Will Be Protection when the Industry Is Unanimous

Perhaps the most intriguing finding arising from the studies and from discussions with policymakers is the reluctance of using industries to oppose protection, and the general belief that protection will be granted when the industry is unanimous in supporting it.⁷

The most effective defense against protection would appear to be a division within the industry. The most vivid example of this among the NBER cases is steel, where prospects for protection diminished substantially after the owners of minimills opposed it. For semiconductors as well, industry unanimity was not achieved prior to the mid-1980s: until that time, the industry's efforts to

5. There is the question, of course, as to why users do not oppose the imposition of protection on their inputs. As seen in Moore's analysis of steel, they can so oppose (if the protection sought is through VERs, but not if it is through the ITC), but it seems to require a fairly major stake in the outcome to induce the necessary organization.

6. It is assumed here that the benefits of protection to the protected industry are positive. As indicated above, however, even this assumption may be suspect.

7. This regularity was noted by several of the “witnesses” when participants in the projects met with policymakers in Washington, D.C., in July 1993. The same point has been made by Milner (1988).

obtain protection had failed. Evidence from other sources and all analysts' accounts point to the same conclusion.

This raises a number of interesting, and unanswered, questions. Why, for example, did the auto industry—a major steel user and itself in difficulty—not oppose steel VERs in the early 1980s? Why did it take until the late 1980s for producers of agricultural machinery to finally oppose continued protection for steel? And, to cite another example, why do apparel makers side *with* textile manufacturers in seeking protection when, as using industries, their interests in textile protection would appear to diverge?⁸

When policymakers were queried in this regard at the project meeting in Washington, responses generally focused upon a “gentleman’s agreement,” or understanding, that each industry would not protest others’ protection, but rather seek its own (implicitly, unopposed). If such is the case, questions arise as to how such tacit understandings came about. If there are not such implicit understandings, the puzzle remains as to why opposition is not more frequently voiced.

9.2.4 Good Lobbying and Organization Do Matter

Short-term economic interests generally determine the side on which various interest groups fall in pressuring for or against protection. However, some groups are better organized, or more readily organized, than others. The correlation between the magnitude of economic interests and the effectiveness of organized lobbying efforts does not appear strong. Some groups that might benefit from protection (or its removal) do not appear well organized, while others are extremely effective.

J. Michael Finger and Ann Harrison point to the well-organized efforts of the textile and apparel groups as a key factor in their achieving as much protection as they in fact receive. Michael Moore’s discussion shows the importance of effective organization and lobbying in seeking and maintaining protection.⁹

Protection for the semiconductor industry appears to have been another instance in which a well-organized industry group was crucial to the achievement of protection. Once there was opposition from users (the personal computer assemblers, who had to compete with foreign assemblers), the degree to which the industry could seek to achieve protection diminished.

In this regard, however, perhaps the most interesting and telling cases among the studies are those concerning agriculture: maneuvering regarding the timetable for reduced protection to agriculture under Mexican entry into NAFTA

8. Here, of course, a possible answer might be that the two industries together form a more effective lobby that can achieve more than either could separately, and that the joint gains exceed the potential if each goes it alone.

9. The needed degree of effectiveness is clearly greater for achieving initial protection than for perpetuating it. Even when protection is perpetuated, however, it can be restrictive to varying degrees. A more effective lobby will, presumably, achieve greater restrictiveness than a less effective one.

was heavily influenced by the pressures that different producer groups were able to bring to bear. Likewise, the wheat growers were able to organize to achieve the Export Enhancement Program in ways that other farm groups apparently were not.

9.2.5 Past Protection Matters

The evidence from these studies and elsewhere strongly suggests that the existence of a protectionist instrument—VER, EEP, sugar quota, or whatever—in the past strongly increases the ease with which protection may be obtained today. Stated otherwise, the expected level of protection in the future is higher, for the same industry characteristics, (1) if the industry received protection in the past and (2) the higher the level of protection was in the past.

Clearly, each round of MFA negotiations started with the preceeding level as a base: much of the industry's lobbying efforts were directed to achieving heightened protection. Likewise, Gardner points to the ease with which the wheat growers were enabled to achieve a renewal of the EEP, contrasted with the initial barrier to obtaining it. A semiconductor agreement with Japan in 1991 was far easier to obtain because there had been one in 1986. The history of protection for steel in the 1970s made it easier for the industry to persuade the U.S. administration to negotiate again.

9.3 Interrelationships

Each of these key findings, which are spelled out in considerably greater detail in the conference volume, has implications for policymakers. They are, however, interrelated and when taken in the aggregate suggest that current practices regarding protection may be widely at variance with considerations of the public good or economic efficiency.

Questions concerning the efficacy of protection in directly improving an industry's fortunes become even more pressing when it is recognized that the indirect negative effects are not adequately taken into account. Conversely, the economic costs of failing to examine indirect effects of protection loom larger if questions arise concerning the sign and magnitude of direct effects.

When consideration is further given to the proposition that using industries that may be harmed by protection are reluctant to protest, economic efficiency may be further diminished when a unanimous industry seeks protection as a perceived means of alleviating its problems. When effective organization and political clout are then important in determining outcomes, there is a further delinking of economic efficiency from the granting of protection.

Add to these considerations concerns as to the "fairness" of the administered protection laws, and it seems clear that questions must be asked about the degree to which current U.S. trade policy achieves objectives that are in the interest of the American people and economic efficiency.

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