REVIEW ESSAY

Washington's New Trade Consensus

And What It Gets Wrong

By Gordon H. Hanson January/February 2024

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In This Review

If the era of hyperglobalization started in 1995, with the creation of the World Trade Organization (WTO), its death throes began in early 2018, when U.S. President Donald Trump raised tariffs on U.S. imports of Chinese solar panels and washing machines. Those levies were followed by tit-for-tat increases in import duties between the two countries. By the end of 2019, the world's two largest economies were in open trade war. President Joe Biden has left Trump's tariffs largely intact, signaling that economic antagonism toward China enjoys bipartisan support and will remain the United States' position for the foreseeable future.

At peak globalization, around 2015, China and the United States were linked by extensive flows of trade, capital, and labor. Supply chains spanning dozens of countries produced powerful electronics. Cross-border listings on financial exchanges made it easy to build globally diversified stock portfolios. International competition for talent clustered the best and brightest minds in superstar cities to foster the creation of yet more technological wonders. Now, that world of largely unfettered exchange sits on shaky ground. Muscular government intervention is fashionable on both the left and the right in the United States, to the consternation of not just China but also U.S. partners. Leaders in Japan, South Korea, Taiwan, and Europe understandably worry, for instance, that U.S. subsidies to the electric vehicle and semiconductor industries will damage their economies.

The energetic official who led the United States down this protectionist path was Robert Lighthizer, the U.S. trade representative for Trump's entire presidential term. As the architect of the U.S.-Chinese trade war, Lighthizer sought to sideline the WTO and decouple the U.S. and Chinese economies. The lasting impact of his efforts, for better or worse, makes him the most consequential U.S. trade representative of the last 30 years.

Lighthizer and Trump imposing duties at the White House, Washington, D.C., January 2018
Jonathan Ernst / Reuters

Because of his association with Trump, some observers group Lighthizer with officials who would make isolationism a core GOP tenet. That would be a mistake. To be sure, Lighthizer is no establishment Republican. He fought, and won, policy battles with

Trump's treasury secretary, Steven Mnuchin, and other GOP traditionalists who favored free trade. Yet he also sidelined Trump's economic adviser, Peter Navarro, who represented the nihilistic burn-it-all-down policy of Steve Bannon, the president's former chief strategist. Lighthizer's stance on U.S. trade policy is at once aggressive, unilateral, and pragmatic—a vision laid out in his captivating, if at times exasperating, new book, *No Trade Is Free*.

Lighthizer provides insight especially into how future U.S. presidents may balance the tricky trade-policy trilemma of confronting China, improving the lot of American workers, and maintaining U.S. alliances. He gives a clear-eyed account of how China did not live up to its trade promises, offers practical lessons in how a steely-eyed realist negotiates trade deals, and suggests a plan for U.S. trade policy that may have a better chance of being implemented than those of most current U.S. presidential candidates. But the book also takes some jaw-dropping liberties in interpreting the history of U.S. trade policy, imbues manufacturing with near mystical economic properties, and sees trade deficits as the only metric that matters for evaluating trade agreements.

And yet Lighthizer has the political wind at his back. Many of his views, including some particularly incorrect ones, are increasingly popular across the board in the United States. His positions appeal to the right by embodying Trump's "America first" bravado and realist aggression, and to the left by embracing Biden's industrial policy and environmental protections. But Lighthizer's book is a reminder of the shaky assumptions that underlie the new trade consensus. In fact, the United States has lost its comparative advantage in manufacturing basic goods, and so recovering the twentieth-century heyday of American manufacturing will prove impossible. If Lighthizer's prescriptions do become canonical, the United States will still fail to resuscitate its factories but will do considerable damage to its international relationships in the process.

TRADE SCHOOL

Lighthizer grew up in the Rust Belt in Ohio, an origin story he invokes to explain his belief in the importance of factories, manufacturing, and blue-collar life—and his antipathy to the forces that devastated American manufacturing. After joining the white-collar world of law, he entered government in 1983 as deputy trade representative under President Ronald Reagan. In that role, Lighthizer threatened other countries, including Japan, with tariffs to reduce steel exports to the United States. He returned to practicing law and represented U.S. steel companies, filing lawsuits on their behalf that claimed they suffered from the unfair practices of foreign firms. By the 1990s, when much of the Republican Party began to embrace free trade, Lighthizer remained steadfast in his defense of domestic producers and would continue to support this cause through decades of work as an international trade lawyer, making him a natural candidate for Trump's trade representative. In that role, he sought to rebalance the United States' trade relationships by levying tariffs (notably on China) and hamstringing the WTO by blocking the appointment of the organization's appellate judges. In his stints under both Reagan and Trump, he sought to forge a trade policy that shrank the trade deficit and protected domestic manufacturing.

Lighthizer grounds his vision of trade policy in the *Report on the Subject of Manufactures*, a document that Alexander Hamilton, the first U.S. secretary of the treasury, presented to Congress in 1791. Hamilton believed that industrialization was essential for U.S. economic vitality and saw import tariffs as necessary to energize the U.S. manufacturing sector, which was still nascent at the time. The job of the U.S. government, Lighthizer maintains, is to leverage American power to make trade deals on the most favorable terms possible and to use trade policy to fortify U.S. manufacturing, on which national prosperity depends. Lighthizer notably embellishes Hamilton by defining favorable trade deals as ones that shrink the U.S. trade deficit. Hamilton would not have defined them that way. In his day, the United States tracked the flow of gold and silver in and out of the country but not the overall trade balance. Instead, the first U.S. treasury secretary focused on how trade policy would affect U.S. economic growth in the long run, a metric far superior to Lighthizer's.

Predictably, some of Lighthizer's analysis is rather partisan. He concludes that Reagan's trade deals were good, whereas President Bill Clinton's, such as the North American Free Trade Agreement (NAFTA), were bad. (Lighthizer worked for Bob Dole, Clinton's failed challenger in the 1996 presidential election.) Yet Lighthizer is also something of an iconoclast. He praises President Barack Obama for taking on China, recounts the long-lasting friendship he developed with stalwart Democrat and AFL-CIO head Richard Trumka, and advocates a softer stance on Japan than the one he held in the 1980s. He now recognizes that through decades of investment in the United States, Japanese companies have become major employers of American workers. As Trump's trade representative, he even sought (unsuccessfully) to win Japan's support in punishing China for its unfair trade practices.

In Lighthizer's telling, U.S. trade policy succeeds when it favors manufacturing and allows for unilateral action—such as imposing punitive tariffs on other countries without first going through the WTO or getting U.S. allies on board—and falters when it lets imports grow unabated. He sees the high points in U.S. economic history as the period from 1861 to 1932 when Republicans (mostly) kept tariffs elevated, to the benefit of the industrial North in the United States; the sky-high, bilateral Smoot-Hawley tariffs of 1930; the gradualist trade liberalization from 1947 to 1986 under the auspices of the General Agreement on Trade and Tariffs (GATT), the WTO's predecessor; and Reagan's efforts in the 1980s to limit imports of cars and steel. Low points, according to Lighthizer, include the period of 1830 to 1860, when Democrats, beholden to the agricultural South, reduced import tariffs; and the disastrous creation of the WTO and NAFTA in the 1990s. Lighthizer disingenuously blames Clinton for the WTO, writing that the Democratic president abandoned "prudent trade policies" and instead placed "trust in an international body," referring to the WTO. He bizarrely suggests that the United States came to reject a Hamiltonian orientation toward trade policy only in 1995. In truth, the process of creating the WTO began with the Uruguay Round of the GATT, which started in 1986 under Reagan, and NAFTA negotiations were initiated in 1990 by President George H. W. Bush. The era of hyperglobalization was a genuinely bipartisan creation.

MADE IN AMERICA?

Lighthizer confers special importance to manufacturing and the making of physical stuff.

As he sees it, "Prosperity comes from the agriculture, manufacturing, and mining (including oil production) industries." His reasoning is in part moral, because workers derive a sense of dignity from making tangible goods, and in part material, in that manufacturing offers a path to high wages for American workers.

Consider the moral reasoning first. Lighthizer traces his idealization of manufacturing to his childhood on the shores of Lake Erie, where ferry boats helped deliver ore from Minnesota's iron range to blast furnaces in Pennsylvania. (He spends less time on how his decades of representing U.S. steel companies may have contributed to his fondness for manufacturing.) He looks warmly at the early industrial supply chain that paid respectable incomes to miners, railroad workers, and iron smelters. On the dignity of work, Lighthizer cites Arthur Brooks and Oren Cass, thinkers on the American right. But he just as easily could have mentioned the political theorist Hannah Arendt or the sociologist William Julius Wilson, scholars associated with the left. The claim that honest work builds self-worth and strengthens community would draw nods from many quarters.

His reasoning about the material gains from manufacturing is also legitimate. Economists once thought that market wages, when measured properly, did not differ much between industries except to compensate for the risks of the job or other unpleasantness. Because the going wage reflects the price of skill, the more skill a worker has, the higher her wage, whichever line of work she takes up. Decades of research have overturned such a view. More granular data reveal that, accounting for individual characteristics, including age, education, gender, race, and ethnicity, some industries pay their workers more than others do, regardless of whether their workers are more skilled. Manufacturing offers many of the choicest jobs. The largest industrial firms frequently have a commanding presence in their respective markets, allowing them, often with a push from unions, to share some of their profits with workers in the form of higher compensation. Out of 20 major sectors, the pay in manufacturing ranks fourth, behind information technology and ahead of professional services, such as accounting and advertising. When manufacturing workers lose their jobs—whether the cause is imports, robots, or the energy transition—they tend to suffer a permanent decline in earnings relative to those who keep their positions. When manufacturing jobs disappear en masse, as when factories close, entire regions suffer. My own research shows how import competition has, in the long run, hurt U.S. factory workers and their communities.

A solar panel factory in Ningbo, China, February 2019
Zhejiang Daily / Reuters

According to Lighthizer, the United States should restrict imports to stem the loss of manufacturing jobs. He pursued this strategy under Reagan. When faced with surging imports of Japanese cars in the 1980s, the administration threatened trade restrictions. Under Trump, Lighthizer oversaw a 25 percent levy on most Chinese goods. Research indicates that both these measures failed. Japan voluntarily restrained itself from exporting cars to the United States for fear that Washington would impose duties or quotas. As a result, U.S. automakers temporarily enjoyed an increase in profits, but American consumers had to contend with higher car prices, causing real incomes to decline. And the U.S. government missed out on tariff revenues because Japan restrained its car exports merely at the threat of trade restrictions. Similarly, Trump's tariffs on China did not affect employment in U.S. manufacturing hubs. For some goods, U.S. importers have been able to find alternative sources of supply from countries such as Vietnam; for other goods, the comparative advantage of American manufacturers is so weak that even a 25 percent tariff still leaves China as the cheapest option. Tariffs did, however, raise prices for U.S. consumers.

Lighthizer's diagnosis of what ails American manufacturing is partially correct. Import competition has shuttered factories and eliminated jobs. But he misattributes job loss to shady trade deals rather than to the simple truth that the United States has little comparative advantage in most areas of manufacturing. As the U.S. labor force has become more educated and as U.S. technology companies, consulting firms, and other business service providers have established a commanding global presence in their industries, rising costs have priced American companies out of many manufacturing markets. The main solution he offers to counter job losses—import restrictions—does not work. Although the United States has done a poor job of helping workers and their communities recover from the decline of manufacturing, there is little reason to believe that import barriers would make their lives any better.

RUST BELT AND ROAD

At the heart of *No Trade Is Free* are misconceptions about the United States' industrial decline, which have led the author to rail against trade agreements. Lighthizer incorrectly asserts that "there is very little actual benefit to the United States in the form of real efficiency gains from trade agreements." He is resentful of the WTO in part because China has gotten away with flouting its trade commitments since joining the organization. Such a view is widely shared among economists. But another source of Lighthizer's pique lies in the WTO's governance. To him, the body's dispute settlement procedure, which was the primary innovation of the WTO over the GATT, is an abomination. It permits countries to file complaints about U.S. trade policy to a panel of experts, who then decide the case according to WTO rules. Appeals are heard by a separate panel of experts. According to

Lighthizer, the way the WTO settles disputes is unacceptable because it constrains unilateral action and therefore dilutes the United States' bargaining power. His preferred approach would replicate how Reagan handled Japan: threaten punishing unilateral action and then negotiate bilaterally to arrive at a solution. He ignores the proliferation of antidumping trade duties—taxes on imported goods that have been unfairly subsidized—which are decidedly unilateral and run afoul of WTO rules. From 1999 to 2019, the United States took more antidumping actions than any other country.

Lighthizer also takes issue with NAFTA because it exposed the United States to a Mexican industrial policy allegedly based on suppressing wages, and because after it passed, the U.S.-Mexican trade deficit widened. Another one of his gripes with the deal is, presumably, its association with Clinton. Lighthizer ignores how NAFTA helped U.S. companies build successful cross-border supply chains for automobiles, aerospace, and medical devices. With NAFTA, Mexico hoped not to be North America's sweatshop but to become the next South Korea. Lighthizer believes that the U.S.-Mexico-Canada Agreement, a deal that he negotiated to supplant NAFTA, helped the United States (and the U.S. auto industry specifically) by imposing more stringent rules on how the United States' neighbors pay their workers and source the inputs for traded goods. But such constraints restrict trade by operating like import tariffs. Whereas NAFTA aspired to be a free trade agreement, the USMCA does not. Here, at least, Lighthizer succeeded in implementing his vision.

Lighthizer seems uncomfortable with international specialization. Under the GATT, which he recalls fondly, the United States struck deals with countries whose average wages and industry structure were roughly similar to its own. The trade created by the GATT tended to be like for like, such as German chemicals for U.S. pharmaceuticals. But the WTO, with a large membership that includes many low-wage countries, has allowed global supply chains to be sliced ever more finely. The iPhone, for example, combines U.S. engineering; German, Japanese, South Korean, and Taiwanese components; and Chinese raw labor—a mixture of resources like those used in manufacturing furniture or household appliances. Although such specialization yields the gains in efficiency extolled by economics textbooks, it can profoundly disrupt local economies. Specializing more in some products, such as airplanes or software, means pulling resources out of others, such as sofas and auto parts.

The economist Adam Smith used the example of a pin factory to argue that when workers specialize, they produce more. Multilateral trade deals have allowed Smith's proverbial pin factory to go global, but they have caused job loss in U.S. manufacturing. Lighthizer holds it as an article of faith that factory jobs in the United States are worth saving.

BAD DEALS

Most likely to gall economists are the passages in which Lighthizer grades U.S. trade deals by their effect on the U.S. trade deficit. To win in a trade deal, in Lighthizer's eyes, the United States must export more and import less. He mistakenly asserts that the United States "could achieve balanced trade by imposing tariffs on imports." But this is true only in the extreme, when tariffs are raised so high that imports fall to zero. Consider the increases enacted during the U.S.-Chinese trade war, from 2018–19, when overall average U.S. tariffs on Chinese imports rose from four percent to 26 percent. Large jumps in tariffs do reduce imports. But they also tend to reduce exports, because factories then focus on making goods for domestic consumers, which necessarily requires pulling resources out of producing goods for foreign markets. Because tariff increases tend to reduce both imports and exports, they do not change the trade balance much. In fact, since Trump imposed tariffs, the U.S. trade deficit has expanded, not contracted.

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Lighthizer is also wrong to blame the creation of the WTO for the rise in the U.S. trade deficit in the 1990s and the following decade. The U.S. trade deficit did rise from 1998 to 2008, before dropping back to 1999 levels in the early 2010s. The cause was not the WTO, but the 1997 Asian financial crisis, after which Asian central banks substantially increased their holdings of foreign reserves, primarily by purchasing U.S. Treasury bills. That resulted in the United States having a bigger capital account surplus, meaning that more capital was flowing into the United States than was flowing out. The United States offset that account surplus by importing more than it exported. The U.S. trade balance was affected because U.S. Treasury bills remained the foreign asset of choice for central banks around the world, which pushed up the value of the dollar, making imports cheaper and U.S. exports more expensive, causing a large trade deficit. For better or worse, the U.S. dollar's status as the global reserve currency is largely what has kept the United States in a trade deficit.

Lighthizer also asserts, with little merit, that the only way for the United States to reduce its trade deficit is to export more manufactured goods, because trade in services is too small to matter. But that neglects the important fact that the United States runs a large surplus in its trade of services. In 2019, before the COVID-19 pandemic disrupted trade, U.S. exports of services were equal to 4.2 percent of GDP, compared with 7.7 percent for U.S. exports of goods. The U.S. trade surplus in services, at 1.4 percent of GDP, offset more than one-third of the U.S. trade deficit in goods, at 4.1 percent of GDP. Moreover, U.S. service exports are even larger than they appear because U.S. technology companies use tax havens to park much of their foreign income from patents, trademarks, and other intellectual property. This income counts as exports of services, though it does not show up in the U.S. balance of payments until the income is repatriated, often decades later. With manufacturing accounting for less than nine percent of U.S. employment, most future U.S. job and export growth will likely be in services, not industry.

DUTIES CALL

Lighthizer fetishizes manufacturing, is intent on driving the U.S. and Chinese economies apart, and desires balanced trade above all else. He wants the United States to use higher tariffs more aggressively. He wants to amend import laws to include border adjustments —taxes that compensate for the different regulations between countries—for labor rights, environmental protections, and health and safety concerns. He wants to subsidize favored industries. And he wants to use the full might of the United States to bend other countries' trade policies to its liking.

This trade agenda—call it pragmatic unilateralism—combines the assertiveness of Trump with the industrial policy of Biden. It includes measures that environmentalists and labor activists have long advocated and calls for a realist application of U.S. power that would please traditional conservatives. Ten years ago, such a proposal would have drawn scant support. Today, it could be the sort of compromise trade platform that Democrats and Republicans could accept, congressional gridlock notwithstanding. Because the two parties seem to be converging on economic policy, it is reasonable to think that Lighthizer's trade agenda may emerge organically from the alternation of power, with new presidents expanding on rather than overturning the trade and industrial policies of their predecessors. Because Biden has let Trump's tariffs on China stand, the trade policies of their administrations differ little. Biden seems to favor carrots, including subsidies for U.S. manufacturing through the Inflation Reduction Act and the CHIPS Act, whereas Trump prefers sticks—during his 2024 presidential campaign, he has floated a new ten percent levy on all U.S. imports. But both camps endorse policies that tilt the playing field in favor of U.S. industry. Hamilton would be pleased.

If Washington continues down the path of trade unilateralism, it will destabilize the global alliances and institutions that it spent seven decades building. That path, alluring as it may be to the antiglobalist right and the interventionist left, would almost certainly not restore U.S. manufacturing to its mid-twentieth-century greatness. Even if by the end of the decade, the United States could defy the odds and increase the share of workers employed in manufacturing by 50 percent, the sector would still count for just one in eight American jobs. However hard it may be for Lighthizer to accept, the future of American prosperity lies in the service sector, not in the furnaces and assembly lines of the past.

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