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Essays on Free Trade

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Introduction

“Free trade” means freedom to trade. Freedom is a concept and principle that everyone holds dearly, except dictators and bullies. Trade and voluntary exchange is being practiced by everyone in this planet except perhaps by hermits and absolute loners who live by their lonesome in very secluded places. But even loners who live alone in the farthest mountains and caves “trade” with their pets: hermits give their pets some food, while pets give hermits company and some warning and protection from dangers posed by some wild animals.

Which means that those 2 concepts, “freedom” and “trade” are loved and practiced by almost everyone in this planet. And yet “free trade” is among the most misunderstood, if not the most hated, concepts in the world today by many people. Very ironic indeed, in spite of the fact that everybody in this planet is a consumer and consumers by nature love plenty of choices, plenty of options, plenty of bargains.

The four essays below attempt to explain further the importance and beauty of free trade. In fact, it can be safely argued that free trade is “fair trade” and any restriction to voluntary exchange is an “unfair trade” practice.

The first paper was my essay that was a runner up to Tech Central Station's essay writing contest in 2006, "Do free trade agreements help Asia become globally competitive?". The second, "Commodity price equalization" is a portion of a paper on free trade I presented in a conference in Kuala Lumpur, also in 2006. The third and fourth papers are my most recent essays on the subject, published this month in the online magazine, www.thelobbyist.biz.

Here we go.

I. Actions Louder than Words

15 May 2006

<http://www.tcsdaily.com/article.aspx?id=051506B>

Free trade agreements and their variants (economic cooperation agreements, regional and sub-regional trade agreements) are agreements among Presidents and Trade Ministers, agreements among governments; they are not agreements among people of those countries.

Funnily enough, countries or governments do not trade with each other; people do. And when people trade with each other, they normally do not set conditions, they do not make paper agreements. For instance, a Filipino software engineer does not require that a Thai garments producer should first buy his software program before he will buy the Thai's new lines of long sleeve shirts. People simply buy certain goods or services from everywhere because they want something of value for their money.

People are happy when they find bargains -- cheap clothes, shoes, computers, food, drinks, cell phones, -- whether or not those are available in their traditional, often local, shops. People are happy when they have plenty of choices of products, and sources to find various goods and services to fill their needs. In this sense most people advocate free trade whether they know it or not.

Some groups, however, have a double standard. They want all their consumption needs and production inputs to be liberalized and to be available at bargains, but want their own products and services to be protected from competition. It doesn't work that way. Still, governments the world over so often give in to protectionist aspirations. Such is done often in the name of "nationalism" and "helping the poor", but this view is myopic.

Enabling the poor to have access to high quality but affordable food, clothing, medicines and housing or construction materials (made available by markets and competition among producers and sellers) is, itself, "helping the poor".

Expanding job creation and employment opportunities as companies expand or the number of small- and medium-sized entrepreneurs grows due to lower production inputs and costs, is also "helping the poor".

If people want protectionism, then everything should be protected, no exemptions. If local farmers want their rice or bananas or pineapples to be protected from foreign competition, then they should not expect to buy cheaper, free-trade-price fertilizers, chemicals, seeds, tractors and their spare parts, and other production inputs. They should not expect to buy cheaper clothes, toys, shoes and other consumer items for their families.

Why we don't have free trade

There are a number of reasons why government trade negotiators are prone to leaving trade restrictions that sabotage free trade.

One -- protectionist lobbyists, from local farmers or manufacturers, to plain anti-globalization NGOs and ideologues, are more organized than consumers. And government officials tend to listen to noisier, more organized groups, despite the fact that everyone on this planet is a consumer.

Two -- governments want to retain high tariffs to raise revenues that finance bloated bureaucracies in their countries. Corrupt leaders benefit from high tariffs, bureaucratic paper work and other non-tariff barriers. So often, of course, importers and traders will be forced to bribe them in exchange for letting in the restricted commodities.

Three -- the "net gains in trade" is still not realized and appreciated by majority of government officials and their trade negotiators. Take rice trade liberalization. When poor households including non-rice farmers (banana farmers, aquaculture farmers, and so on) save from buying cheaper imported rice than locally-produced rice, they do not burn their savings. They will use the money saved to increase their consumption of bananas and other fruits, vegetables and fish, poultry and livestock products, or have haircut more often. This price signal will alert some rice farmers to shift to other livelihood like vegetable farming, aquaculture, poultry and livestock farming, and so on. The job displacement is temporary but the economic efficiency of labor and resource re-allocation is more long-lasting.

What to do?

Since government trade negotiators have such limitations, the WTO should not be headed and negotiated by them, but by leaders and representatives of federations of traders (exporters and importers) in each country. Now, this is easier said than done since the WTO was formed by governments, not by private traders and consumers.

If full free trade among many people in Asia and the rest of the world is not possible, there are other alternatives. One is for countries whose political leadership and trade negotiators understand the benefit of full free trade, to undertake unilateral trade liberalization.

Two, allow "dumping" of surplus products and services by other countries. Dumping is good, especially if the "dumped" products are still of good quality. As discussed above, economic and job dislocation of the adversely affected sectors is short-term, but millions of consumers who realized great savings from buying "dumped" clothes from abroad will have extra money to buy other goods and services which they would not buy otherwise if said dumped products are not available.

Three, allow export subsidies by rich country governments and do not make it a hindrance to more trade liberalization. If those governments will over-tax their citizens so that their exports can be sold at a lower price to poorer countries, so what? Buy their heavily-subsidized farm products, let the citizens of recipient countries enjoy cheaper imported food and dairy products.

While free trade agreements among Asian countries can help them be more globally competitive, very often such agreements are couched in various conditionalities. That actual free trade between and among partner countries are 10 or 20 years from their signing date. Hence, what will really help Asian countries be more economically dynamic and globally competitive, is actual free trade, preferably with no more paper free trade agreements.

II. Commodity price equalization

11 September 2006

<http://www.minimalgovernment.net/events/paper20060911.pdf>

In international trade theory, globalization and free trade results over the long-term in "commodity price equalization" across countries; or if capital, labor and technology are highly mobile, free trade and globalization results in "factor price equalization". Only transportation cost between and among countries would spell the price difference. Of course, such equalization can be temporary as innovation and competition among enterprises is unceasing.

This means that countries that have surplus output (say, surplus rice in Thailand and Vietnam) will experience declining rice prices domestically if

trade is restricted, while rice prices in countries that have low rice output relative to their population's needs (like the Philippines) will be high. Globalization and free trade reallocates resources and products from countries and places where they are abundant, to places and countries where they are scarce and needed. Such resource reallocation is reflected in commodity price (in this example, rice price) that is generally the same across many countries, adjusted for cost of living in those countries.

Consider three countries:

Country **A** has rice surplus production every year (wide and flat riceland, good irrigation, few typhoons, good technology, small population).

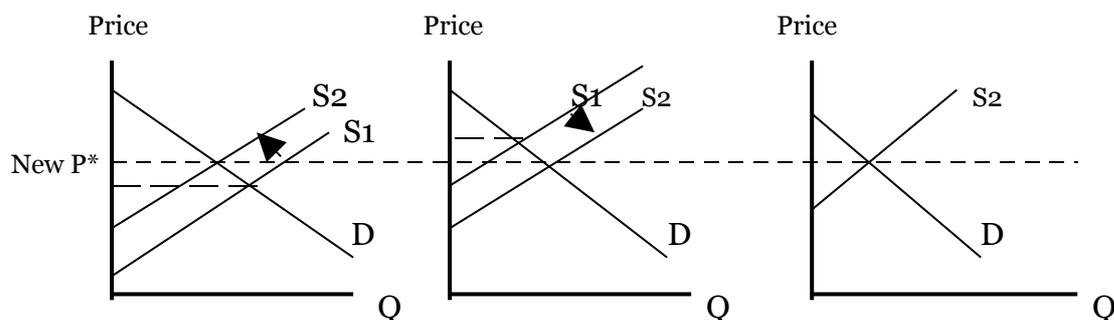
Country **B** has rice deficit every year (mountainous and degraded land, poor irrigation, lots of typhoons, poor technology, big population).

And country **C** produces no rice (industrialized and urbanized, imports many of its food requirement).

No trade or restricted trade among them, country A will have very low rice price because of over-supply. Country B will have expensive rice because of under-supply. And country C will have very expensive rice. With free trade, there should be rice price equalization among the 3 of them as whatever surplus in A will be bought and imported by B and C. If A suffers a bad harvest, then all three of them will have expensive rice price.

Graph 1: Commodity price equalization under free trade

Country: A (surplus, exports) B (deficit, imports) C (non-producer, imports)
Examples: Thailand, Vietnam Phils., Japan Singapore, Hong Kong



The global supply curve tends to move more flat in a regime of free trade and unhampered globalization. A flatter supply curve means a flatter price range (ie, small difference from the most expensive to the cheapest price of a commodity) across a wider and bigger supply of that commodity around the world.

Thus, even in years and periods of robust global economic growth, globalization and free trade should result in modest price rise and stable single-digit inflation rate on average across the world. This is because for

countries and places to further expand output, they will have to hire more workers and technology from other countries, import more production inputs (from agricultural raw materials to high-tech farm machineries) from other countries. The fast movement of inputs, intermediate goods and services, and final products around the globe will provide the momentum for such robust global growth to be sustained for several years. This is on the assumption of course that there are no adverse external interruptions like wars, terrorist attacks, and natural disasters.

III. The case for unilateral trade liberalization

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http://www.thelobbyist.biz/column_detail.php?id_article=842&id_category=25

Representatives of member-states of the World Trade Organization (WTO) will hold another “crucial talks” in Geneva starting July 21 this year. The negotiations will focus on agricultural issues (tariffs, domestic support, and other subsidies) and non-agriculture market access (NAMA). These are among the “unfinished agenda” from the Doha Development Round in 2001, and they contain among the most contentious issues.

Some facts here on the two basic documents: the “Revised Draft Modalities for Agriculture” (July 10 draft) is 116 pages long, single spaced, including tables. The “Draft Modalities for Non-Agricultural Market Access” (July 10 draft) is 112 pages, single spaced, including tables. Both documents are not so easy to understand for someone busy producing or trading various goods and services, or for ordinary consumers who only want as many choices as possible. But those documents can be convenient and easy to understand for someone whose job is to put up various regulations and restrictions, then meet and talk how on to slightly reduce those restrictions and schedule endless rounds of global meetings and negotiations.

From time to time, we get to read news stories and opinion articles on how this and that country’s trade representatives and negotiators are blaming someone else, or group or bloc of country representatives, why the trade talks collapse. The tone of the blame-game is something like this: “We can’t bring down our tariffs and agricultural subsidies because the other parties and countries are not bringing down their tariffs and non-tariff barriers on other sectors.” So the current trade protectionism is justified because the other parties are equally protectionist, if not retaining and instituting even more trade restrictions.

One wonders how much money have been paid by taxpayers from the countries concerned, first to pay for the salaries, travels, and perks of their country trade negotiators, including their pool of consultants and secretariat support, in all those years. And second, how much taxes they have been paying for continued subsidies to their local producers so that the latter can sell them products and services at a cheaper price when similar products and services can be sourced and imported elsewhere at a low price and they don't have to pay a single cent of tax money for these.

Consider Hong Kong. The people in this economy are busy producing various goods and services, and facilitating international trade. Why? Because it has a unilateral trade liberalization policy. They don't pay for a huge army of trade negotiators and consultants; they don't blame other parties and countries why they continue to be rigid and restrictive in allowing the exports of other countries when their own citizens demand for it. Hong Kong did not ask, and is not asking, that other countries should reduce their tariffs and other non-tariff barriers first, before they will go to the negotiating table. Almost any country that has good quality products and have buyers there can bring in their commodities and pay zero tariff.

In this situation, millions of people from many parts of the world are swooping into this small but very dynamic economy to tour, dine, meet, shop, and do more shopping. Why? Because those people know that Hong Kong offers plenty of choices for them, from the most expensive global brands to the cheapest products sold in huge volume. Choices that are not easily available in their country because their governments, trade negotiators, and many local producers are busy persuading other countries that they start liberalizing first before they do, busy blaming other governments if they fail to do so, or busy concocting various reasons and alibi why they should retain their trade restrictions even after other countries have started liberalizing their importation policies.

In a situation like this, the Hong Kong government and economy is creating lots of jobs for its people and emigrants, and when people have jobs, they don't demand various state welfare and subsidies because they can provide for themselves and their families. And if there is less demand and clamor for various state subsidies, there is less demand and rationale for high and multiple taxes and fees. This mainly explains why Hong Kong remains the freest or among the freest economies in the world.

Singapore is another country that has unilateral trade liberalization policy. And very often it is neck-and-neck with Hong Kong in the annual ranking of the world's freest economy studies by various big international think tanks. It is also attracting millions of foreign visitors. Every year, the number of tourists is about twice or thrice the size of its nationals.

Dubai too, and Georgia. The latter, a small European economy, has enacted a zero-import tariff policy just a few years ago, and it is among the fastest growing economies in the European continent. Brunei, Estonia, and Chile are close to being unilateral free traders too.

Trade negotiations are being done by thousands of country trade representatives and bureaucrats, along with WTO officials and staff. Unfortunately, neither countries nor governments trade with each other. People do. And when people trade with each other, from other countries or continents, they do not set conditions. A Korean telecommunications engineer does not demand that a French fashion designer should first buy his Korean company's services or cellular phone products, before he buys the Frenchman's line of clothing. No such thing. People buy a product or service because he thinks he gets value for his money. And this forces many producers and suppliers from many parts of the world to produce good quality commodities at competitive prices, if they want to attract as many buyers and clients as possible. And people engaged in this kind of trade are better off.

For the Philippines and other developing countries, a unilateral free trade policy will serve their economies better. Among the immediate positive results are the following:

First, their people will have lots of choices for their consumer goods and production inputs, whether they are manufacturers that need good quality raw materials, or farmers that need good quality but cheap hand tractors.

Second, the economy will boost its tourism potentials as many people from other countries having high commodity prices due to high taxes and trade protectionism will come in not only to enjoy the tropical climate and white sand beaches, but also to shop, shop, and shop.

Third, the economy will generate plenty of new jobs, from manufacturers who can produce more efficiently and cheaply with more options for their production technologies and raw materials, to farmers who can produce more with cheaper farm machineries and modern post-harvest machines. This also includes tourism-related industries like airlines, hotels, malls, shops, restaurants, and beach and mountain resorts.

Fourth, the economy will worry less about so-called "external aggression". Take Hongkong again. Any potential aggressor country, assuming there is any, will think not only twice or thrice, but a hundred times, before it will ever attempt to invade and colonize that economy. This is true even if it has a very small air force, navy, and army, or even if we assume that China will not give it protective cover. Why? Because among the biggest American and Canadian companies, among the biggest British, French, German, Italian, other European companies, among the biggest Japanese, Korean and Australian

companies, have branches, offices, and shops in Hongkong. So any potential aggressor country will face the most ruthless fighter planes, the most modern battle ships, and the most battle-tested soldiers of these big and rich countries who will protect their respective business interests and nationals that are based in that territory. So it is safe to assume and assert that if you are a unilateral free trader and a unilateral low tax economy, you will attract some of the biggest companies in the world, and you will attract no external enemy.

This list of the benefits of unilateral free trade is not exhaustive and complete; it only outlines some of the most basic arguments. To summarize: If we want more economic growth, more job creation, let us minimize if not stop trade negotiations, go straight to a unilateral trade liberalization. If we want peace, let us have free trade and free market.

IV. Asserting consumer choice through free trade

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http://www.thelobbyist.biz/column_detail.php?id_article=851&id_category=25

High unemployment and underemployment rates are among the scourge of modern economies today, both in rich and poor countries. People would want to be productive, to be economically useful to their family and community. It's just that there are a number of man-made restrictions that prevent them from being hired by other people, or from employing themselves through entrepreneurship. In a number of countries though, there are plenty of subsidies and allowances given to jobless people, single parents, etc. So there are some "incentives" to become irresponsible because they are "entitled" to certain social and economic benefits anyway. But that is not the subject of this paper. It is those who were rendered economically unproductive due to man-made restrictions like high taxes, bureaucratic business regulations, and trade protectionism.

Trade protectionism comes in two forms: high tariffs and high non-tariff barriers (NTBs) like plentiful trade requirements and regulations. Any or both of these happening can cause damage to the economy, the entrepreneurs, their employees and the jobless people in particular.

Take the case of Hong Kong. There are no tariffs or import taxes, so imported goods – except those explicitly prohibited like hazardous wastes and ozone-depleting substances – come in duty free. Aside from zero tariff policy, international trade is facilitated and very much encouraged through the following additional policies: (a) no laws for valuing goods for customs purposes (since there are no tariffs). (b) no rules of origin or certificate of origin required, (c) no rules on anti-dumping and countervailing measures or any "safeguard" actions. These policies amount to zero NTBs. In addition, there are no State-owned trading enterprises that can cause unfair competition to private sector traders. For the exporters, there are no export-related duties and taxes, no "local content" requirements for exports, no subsidy to exporters.

What all these mean is that the government will hire very few customs personnel and inspectors, and importers too will not need to hire additional lawyers, accountants, other "negotiators" with government customs officials since there are very few requirements to comply with. Since there is very little demand for such kinds of jobs and services, young people will see it and they would rather become traders and entrepreneurs when they grow up.

When there is zero tariff, zero NTBs (zero tax for countervailing, anti-dumping or other safeguard measures, zero fees for other trade regulations like rules of origin certificates, and so on), landed price of imported goods is low and cheap. So when you add up those two important factors, (i) plenty of entrepreneurs + (ii) cheap imported commodities (whether for household consumption or production inputs and intermediate goods), the result is more economic growth, more job creation, possibly a full-employment economy.

Full employment does not mean zero unemployment rate. It could mean 2 or 3 percent unemployment rate because some people are “jobless” at the time of a labor force survey because they have a high “reservation wage”. Meaning a job is awaiting for them anytime but they refuse to take it because they are waiting for another job offer with higher pay or better package (say car and housing, travels, commissions, etc.).

Resistance to free trade through very small or zero tariff and very small or zero NTBs, comes from three groups of people. These are the protected sectors and businessmen, the left-leaning NGOs and lobby groups, and the government bureaucracy and politicians. Let us tackle them one by one.

The protectionist businessmen and sectors can be understandable because they feel threatened that their products might be spurned by local consumers who might find imported substitutes not only cheaper but better in quality. But the same protectionist businessmen and sectors also want free trade in other products and commodities that they do not produce. A rice farmer is biased only against imported rice but he wants free trade and more choices when it comes to fertilizers and hand tractors, shoes and clothes for his children, tv and other appliances for his house, etc. When they realize that they actually benefit from free trade for their household needs and farm inputs, plus the possibility that they can export their surplus rice at a higher price when their productivity improves due to more modern farming tools and practices, their opposition to free trade can weaken.

The second group, the left-leaning NGOs, trade unions, media and other professionals are harder to please because of very often, plain envy and ideological hatred of free markets. They hate to see some people becoming very rich and prosperous because of the big economic opportunities opened up by free trade. They hate to see inequality and temporary economic dislocation as a result of resource reallocation in society. And some of them are on the payroll of big businesses who benefit from trade protectionism and absence of foreign competition. But being consumers, deep inside they want free trade, they want more choices, they want bargains, for their various personal and professional needs, from shoes and jeans to food and drinks, to cell phones, laptops and cars.

The last group, the government trade bureaucracy and politicians, are the hardest to please, the hardest to convince of the evils of trade protectionism. Mainly because they live off on taxes, and high tariff means high tax revenues. Or high tariff and NTBs mean difficulty for entrepreneurs and hence, higher incentives for the latter to pay them bribes or other favor in exchange for facilitating trade. When a country is protectionist, the trade bureaucrats and some politicians enjoy vast arbitrary powers: who can trade and who cannot trade; where they can export and import and where they cannot; by how much quantity they can trade; how much fees to pay and many papers and documents to submit; and ultimately, how quick or late they can allow trade. Arbitrary powers mean arbitrary mean and opportunity to amass wealth at the expense of consumers, especially the poor and the jobless.

Unlike businessmen, farmers, labor unions, media people and other professional groups, consumers are not organized. The power of the consumers is in their purchasing capacity, in the expression of their preferences and priorities as reflected in the goods and services they buy. Their power is therefore, not fully articulated in media and Congress, but in various market places like malls, shops and public markets. The absence or non-articulation of power by consumers is also reflected in the level of poverty and joblessness in society.

It is important therefore, to continue explaining the importance of free trade if society is to attain full employment and assert consumer choice and freedom. And it is equally important to explain and expose the reasons and vested interests of some groups of people who are opposing free trade.

Meanwhile, the WTO has just released its “World Trade Report 2008: Trade in a Globalizing World” (http://www.wto.org/english/news_e/pres08_e/pr534_e.htm). The main message of that report is simple: Trade and globalization have brought greater prosperity to hundreds of millions as well as greater stability among nations.

And late this week, the International Policy Network (www.policynetwork.net) will publish a report entitled “While Doha Sleeps: Securing Economic Growth Through Trade Facilitation”, and our institute, Minimal Government Thinkers, Inc. (www.minimalgovernment.net) will be one of the sponsoring think tanks of this paper. Watch for it next week.