IS FREE TRADE THE ANSWER TO ENDING POVERTY WORLDWIDE? THE CASE OF HAITI

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Abstract

Free trade is indeed the answer to ending poverty not only nationally, but also worldwide. Our case study of Haiti is no exception whatsoever to this general rule. Why? This is due to the fact that each and every trade, without exception, necessarily improves the economic welfare of all parties to the commercial interaction, at least ex ante. And, there is no other economic activity that can make anything even approaching this claim.

Key words: free trade; economic welfare; Haitian economics

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The inequality between First World and the Third World countries is radical (Anand & Segal, 2015) and has, in recent years, become a global issue. Even though the public's interest in conquering global poverty has recently escalated (Banks & Hulme, 2012), these inequalities have been present both in ancient and modern times. However, the disparity between each of these two worlds is not only explained by wealth but also and even more importantly by that which creates wealth, such as skills, habits,

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technology and knowledge, all unevenly distributed among the world's population.

Ancient civilizations such as that of the Egyptians, Chinese and Greeks were far more advanced than other civilizations in their respective eras. This was mostly due to the fact that these populations were close to the Middle East where agriculture was developed and was a pillar for starting communities, cities and empires[1].

Without the knowledge of these ancient societies, western civilizations would not have been able to develop and grow. However, throughout history, the dynamics of this inequality have shifted. For example, in the nineteenth century the Britons were no longer behind. Rather, they lead the world into the industrial age. This drastic development of civilization was due, in large part, to trade.

Trade has taken place for several thousands of years, and has been a central aspect of development, efficiency, growth and innovation for all countries it has touched. This engine of growth increases economic opportunities, creates jobs and reduces poverty. History has taught us that, without trade of not only goods, but also of knowledge, skills, and technologies, the world would not be as advanced as it is today. There are, however, many aspects that contribute to a country's development such as its geography (is it landlocked or does it have coastal cities?) and resource availability. Research conducted by the World Bank (2018) has shown that the poorest countries in the world tend to

[1] However, historical evidence suggests that agriculture was developed independently in various parts of the world. It is known that Native Americans of the Southwest United States have implemented agricultural practices for at least 12,000 years (Steele, Reyes, Elias, Aney and Rango, 2018; Crepelle, and Block, 2017). It is also known that maize was domesticated in South America for at least 3500 years ago (Atkins, 1998). Another geographical explanation is supplied by Diamond, 1999, who pointed to the importance of latitude vis a vis longitude. See also Eichengreen, 1998; Landes, 1998; Easterly and Levine, 2003; Smith, 1776; Acemoglu and Robinson, 2012.

be the ones most closed to trade while nations that have reduced trade barriers tend to be among the fastest growing.[2]

While possessing technological advances and geographical advantages are surely important, a country's governance can seriously hinder its evolution and, in some cases, lead it to fall behind compared to competitive nations. Examples such as Japan, which in the 15th century was technologically and institutionally advanced compared to the western world, soon fell behind significantly after their government completely shut their doors off to the rest of the world (Sowell, 2016). China also faced the same setback in the 15th century when their government imposed strict restrictions concerning communications with the outside world. China was "ahead in technologies such as printing, navigation and rocketry" (Dyson, 2014, p. 6 quoted by Sowell, 2016, p. 71) but once these restrictions were put into place China also faltered. Centuries later, countries including China and Japan adopted policies that opened up doors to global markets, allowing their populations to take advantage of trade. These policies quickly increased their GDP's, wages rose, and poverty decreased (Kling & Schulz, 2009).

Free trade is the idea that products and goods should be purchased and sold between members of different countries with minimum to zero restrictions. The common perception, however, deems free trade as detrimental to a nation's economy. Thus, governments inflict thousands of tariffs, quotas, and other barriers to trade. These restrictions not only limit consumer choices, but also increase the price of goods. By fueling global competitions, free trade allows consumers to buy more, better quality goods at a lower cost.

For the past fifty years, international trade, in the framework of economic globalization, has benefited nations (Shin, 2009; Samimi & Jenatabadi, 2014). However, the 2008-2009 financial

[2] Gwartney, et al, 1996; 2008 demonstrate that economic freedom in general, not merely concerning international trade, boosts economic growth.

crisis motivated a global protectionist spiral, characterized by a combination of traditional and new (and more harmful) trade policy instruments (Kutlina-Dimitrova & Lakatos, 2017). "The period of crisis has seen a steady increase in the number of protectionist measures, amounting to an annual average of more than 800 new harmful interventions" (Kutlina-Dimitrova & Lakatos, 2017, p. 5). Among the protectionist policies most often established by contemporary economies, tariffs represent about the 25%; anti-dumping duties (15%)[3], financial grants (10%) and new measures as public procurement and state loan, each representing 5%. The protectionist trend started in 2009 in Russia, Argentina, Turkey and China (Kee, Neagu & Nicita, 2013) and during the last three years it has spread to all the G20 countries, which have also increased their trade restrictions.

Of the contemporary examples of protectionism, the most prominent is that of the United States. Since 2017, the Trump administration has adopted protectionist policies[4] that although they have not been the most radical in American history (for example, those of Reagan were larger in scale and scope),[5] they have generated great alarm in global markets. Under pretexts such as national security and the idea that Americans are losing in international trade, Trump administration has taken measures such as increasing tariffs on steel and aluminum, US industry basic inputs, (25 and 20 percent respectively), and has aroused fears of a trade war with China.

In the midst of Trump's high-profile attempt to undermine trade with this latter country the effect on the trade between the NAFTA nations, for the most part, goes almost unnoticed. The United States, Canada and Mexico are all part of the North American Free Trade Agreement (NAFTA). The agreement went into effect on January 1, 1994. Since then, trade between the three

[3] For the case in favor of "dumping," see McGee and Block, 1997; Yoon, McGee and Block, 1999; Gries and Block, 1998
[4] See Block, 2018
[5] Rodrik, 2018.

nations has grown exponentially. In 2016, NAFTA countries represented 28% of the world's gross domestic product (GDP) with just less than 7% of the world's population (Canada-United States-Mexico Agreement website). Since the implementation of NAFTA, the North American economy has expanded, with the combined GDP for Canada, the U.S. and Mexico reaching USD $21.1 trillion in 2016. (Canada-United States-Mexico Agreement website). This agreement has given the North American companies a chance to take advantage of significant cost savings and have allowed them to be more competitive. However, critics of this agreement have argued that NAFTA has cost thousands of Americans their jobs and has increased the United States' trade deficits. Under the Trump administration, there is another agreement currently undergoing negotiation, meant to replace NAFTA.

To wit: the United States-Mexico-Canada Agreement (USMCA) is an "amalgamation of the old NAFTA, the previously-rejected TPP, and some new protectionist measures" (Dorobat, 2017). Here are some of its most damaging measures: steel and aluminum tariffs are "likely to remain in place in the form of a quota plan" (Dorobat, 2017); the agreement between the US-Canada block with Mexico specifies new rules of origin for car industry that are extremely restrictive: for instance, two thirds of a car´s value must be manufactured in North America and only those manufacturers that meet new and more exigent labor conditions will be able to ship vehicles to Mexico (Dorobat, 2017; Lester & Manak, 2018). This will have a harmful effect regarding production costs. Other measures include more restrictive copyright policies and discouraging the NAFTA parties "from negotiating trade deals with non-market economies" (Lester & Manak, 2018).

In the long term, trade protectionism weakens industries. Without competition, companies have less of a need to innovate and produce. Quantity falls below the level that otherwise would have obtained and prices tend to rise. Eventually, domestic products will decline in quality as well and become more expensive than foreign goods. Many people believe job-outsourcing is the result of trade, it actually emanates from its very impediment, leading to declining US competitiveness. By increasing protectionism, the United States' economic growth will not increase as quickly; this might well cause layoffs among the 12 million U.S. workers in exports.

Free trade increases prosperity for the citizens of all participating nations. It initiates economic growth, enhances efficiency, and increases innovation. These benefits rise as exports and imports are enhanced, due to increased specialization and division of labor. With free trade, companies are faced with competition, not only domestic, but also from abroad. Thus, companies have more incentives to increase efficiency, create and produce a better product while cutting costs (Lamaj, 2015).

Critics, however, believe that free trade creates unemployment especially in America where cheap labor is not an option (O´Leary, Eberts & Pittelko, 2012). Free trade may reduce jobs in inefficient industries, but it frees up resources to create jobs in efficient industries, boosting overall wages and improving living standards (Boudreaux, 2015). It helps a nation develop and keep up with the changing industries, including new technology, "such as apps on mobile devices, which have displaced a variety of products, including radios, cameras, alarm clocks, calculators, compact discs, DVDs, tape recorders, flashlights, file cabinets and even blood-pressure monitors" (Boudreaux, 2015, p. 3). But over time, this system works in tandem with other market processes to shift workers and resources to more productive uses, allowing more efficient industries to thrive. The results are higher wages, investments in efforts such as addressing infrastructure, and developing a more dynamic economy that continues to create new jobs and opportunities. The Peterson Institute for International Economics (2007) estimated that ending all trade barriers would increase U.S. income by $500 billion per year.

People who advocate free trade generally point to comparative advantage. This is the principle which holds that when a country produces goods, it does so not based on its objective productivity level, but, rather on the basis of how it compares with that of other nations. Each country can specialize in the products they are best suited to make.

Consider the following example. Assume the U.S. can produce 10 tons of steel with a given effort, or 6 tons of fish, and that these two products are equally valued; thus, it has a GDP of 16 units. Posit that Haiti's numbers are steel 7, fish, 8; GDP, 15; total for the two countries together: 31. This is case of absolute advantage. Now introduce trade. Each nation specializes in what it does best and leaves off its weakest product. The U.S. spends all of its effort on steel and comes away with 20 units. In like manner, Haiti does so for fish, 16 units. The "world" product, consisting of these two countries thus rises from 31 (16+15) to 36 (20+16). Not too shabby.

Now for comparative advantage. Let us leave U.S. statistics as they were before: 10 steel + 6 fish = 16. But Haiti is now less productive: 2 steel + 5 fish = 7. The total for both is now 23 (16+7). Now let us introduce comparative advantage. Haiti is only 20% as efficient as is the US in steel: 2/10. But, relatively speaking, Haiti does far better compared to the US in fish: 5/6. So, each country specializes in what it does relatively best. The US sticks to steel and comes up with 20 units (10x2), but no fish. Haiti concentrates on fish and produces 10 units (5x2). The total rises from a pre-trade 23 (16+7) to a post-trade 30 (20+10). If this is not the "magic of the market," then nothing is.

Another benefit of free trade is the reduction of monopolies. The market power of monopolies decreases with free trade because firms are now competing, also, on a global scale. Free trade also leads to higher economic output as an increase in demand for local goods results in higher exports. This in turn creates more jobs for the local economy and the country enjoys higher economic growth. Consumers also enjoy a wider variety of goods, a well as increased consumption outside of their previous production possibility curve. Apart from economic growth and low prices, free trade promotes innovation. Trading knowledge and technologies accelerates improvements in these domains.

Free trade is an important part of economic development (Rahman, 2014: Riley, 2010, Froning, 2000). However, some myths persist with respect to their nature and benefits. As a result, free trade is viewed with suspicion. Let us explore those myths.

MYTH 1: TRADE IMBALANCE IS ECONOMICALLY HARMFUL

Generally, a so-called "negative" trade imbalance is seen as deleterious in international trade. The idea that a country is "forced" to import more and export less is terrifying to the economically illiterate. However, the reality is that trade deficits can be quite beneficial for the economy. If an economy like Haiti had a "negative" trade balance with a country like the United States, that simply means the latter imported more from the former and exported less[6]. A massive arrival of imports will diversify and expand the local Haitian market. Furthermore, for Haiti importing goods can be much cheaper than trying to produce them within its borders. Think for example of a capital good like a state-of-the-art tractor. What would be more convenient? Bringing it from an advanced market like the US or trying to produce it autarkically using a very limited capital supply? On the other hand, once the money spent on imports is received by foreign exporters, it "returns to the domestic economy as demand for domestically produced goods and services". (Boudreaux, 2018, p. 44). Therefore, a deficit in current account is compensated by a surplus in capital account.

Another fear with respect to trade deficits is that it depreciates the local currency. Neither theoretically nor empirically has this causality been demonstrated. On the theory side, balances

[6] In the early days of the United States, this country had a "negative" trade balance with European countries, mainly due to investments from the latter to the former. No great harm was imposed on the new nation; exactly the opposite occurred.

of payments between countries do not cause changes in the purchasing power of the respective currencies, which, in turn, does not affect the determination of exchange rates. On the evidence side, sometimes the reduction of the current account deficit is associated with the appreciation of the currency of one of the trade partners; while other times the opposite occurs (Shostak, 2017).

The authors of the present article have a very serious negative balance of trade with WalMart and McDonalds. We purchase goods from both; neither of them has yet reciprocated in the slightest. So far, it has all been a completely one-way street. According to this myth, we ought to be harmed by these two large corporations. The obvious retort is that both parties gained, at least ex ante and almost always ex post also, from every single commercial transaction which led to his supposedly “negative” balance.

MYTH 2: WE NEED TO PROTECT INFANT INDUSTRIES

This is the idea according to which a country needs to immediately be-competitive on global markets. In turn, this would only be achieved if the government protects certain industries in their consolidation phase (*infant phase*) against competition from well-established foreign industries (who are in an *adult phase*).

One problem with this argument is that such protection, which in theory would be temporary, typically becomes permanent, so that "infant industries" never reach maturity. The empirical evidence shows that once the protected industries reach a certain degree of development, protectionism increases, arguing that now they are strategic industries that impart great benefits to national development, so they must be taken care of (Panagariya, 2019). In a country like Haiti, applying an infant industry protection policy would be doubly disastrous: on the one hand, it would violate the very logic of free trade, to the detriment of the consumer, and on the other, it would plunge the potentially protected industries into a particularly corrupt institutional environment.

A more serious fallacy committed here is that *every* new firm, without exception, is an "infant" when it begins. This theory, then, implies that government should subsidize *all* new companies. But that would be out and out socialism, the death knell for economic development (Mises, 1922). On the normative side of the equation, if the infant succeeds, its investors shall gain, thereby. There is thus no ethical case in forcing others, who will not take part in the profits, the general taxpayer, to finance the start up. Let the stockholders bear the costs as well as the benefits.

MYTH 3: ONLY BIG PARTNERS GAIN WITH FREE TRADE

Trade works optimally regardless of the trade partners size. Every country gains from free trade even if it suffers "from low productivity in all economic sectors relative to their trading partners" (Panagariya, 2019, p. 32). This is explained by the Ricardian idea of comparative advantage, according to which a certain country would benefit if it exports the product in which it uses its relatively abundant factor – in the case of Haiti and the underdeveloped countries, in general, it is labor – and imports the product that uses its relatively scarce factor more intensively – in the same case, it is capital – (Panagariya, 2019). This fact seems to be confirmed for Haiti, since 85% of exports from Haiti correspond to a labor-intensive textile sector (OEC, 2017). However. On the other side, the product that Haiti mostly imports is rice (it represents 7.6% of total imports and the highest percentage if accounting is done for individual products). However, the interesting thing is that this import is motivated by a political consideration.

The rice industry in Haiti experienced a boom "from the early 1960s to the mid-1980s" (Cochrane, Childs & Rosen, 2016, p. 4). By 1985 the country produced approximately 100,000 tons, the highest result in the period from 1960 to 2015 (Cochrane, Childs

& Rosen, 2016) (Wilcock & Jean-Pierre, 2012). The soil and climate are ideal for doing so. Consumed by every country in the world and-a staple food in more than half the world's population, this essential commodity is critical to the Haitian diet. The people depend on it to provide energy, while keeping them satisfied and cheaply so. American producers were unable to produce enough rice inexpensively to sell globally. The "solution" was to export their rice to other countries. Under the Clinton administration, the government subsidized rice farmers. This policy, which is still in place today, costs Americans approximately "434 million dollars a year" (Fang, 2015).[7]

One of the measures of this new policy was to force Haiti to drop tariffs on imported subsidized U.S rice (from 50 % to 3%) (Lundahl, 2014, p. 48). This policy wiped out Haitian rice farming, seriously damaging Haiti economy as American rice was selling for much cheaper than Haitian rice and subsequently forced Haitian rice farmers into unemployment. The rice economy of Haiti was destroyed, still affecting Haiti's economy to this day (Lundahl, 2014) (Cochrane, Childs & Rosen, 2016) (Blumberg & Cohn, 2015).

Bill Clinton (2010) issued an apology for his policy failing,

Since 1981, the United States has followed a policy, until the last year or so when we started rethinking it, that we rich countries that produce a lot of food should sell it to poor countries and relieve them of the burden of producing their own food, so, thank goodness, they can leap directly into the industrial era. It has not worked. It may have been good for some of my farmers in Arkansas, but it has not worked. It was a mistake. [...] I have to live every day with the consequences of the lost capacity to produce a rice crop in Haiti to feed those people, because of what I did. Nobody else.

In this case, the impoverishment of the Haitian economy was not the outcome of free trade, but rather the result of a desire,

[7] See Fang, 2015: http://yris.yira.org/essays/1534.

politically motivated, to get rid of a product that the local market did not want, moving it towards a foreign market.[8] Clinton's apology was entirely justified.

Politically managed trade also occurs in the Dominican Republic (DR). Currently, this country exports approximately 853 million dollars worth of products to Haiti (CSIS, 2019). Meanwhile, due to trade barriers–such as tariffs and restrictions, Haiti only exports less than 42 million dollars' worth of goods and services to the Dominican Republic, most of which is conducted illegally (CSIS, 2019). Strategically, the DR imposes quality standards that Haitians are unable to meet, this constitutes a non-tariff barrier. Thus, the DR is able to sell their best products to wealthier countries, while still profiting on the products that "did not make the cut" by exporting the lesser quality products to Haiti.

If there were genuine free trade, Haiti could take full advantage of its comparative advantage, instead of resigning itself to receiving unwanted products (as in the case of the United States) or low-quality remnants (as with the Dominican Republic).

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[8] This is just the tip of the iceberg of blaming markets for political shenanigans. Similarly, laissez faire capitalism is widely held responsible the recession of 2008, as if there were no federal reserve system in existence at the time.

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