Supporting Question 1	
Featured Source	**Source A:** Henry George, argument against trade barriers, *Protection or Free Trade, An Examination of the Tariff Question, with Especial Regard to the Interests of Free Trade* (excerpt), 1905

Trade is not invasion. It does not involve aggression on one side and resistance on the other, but mutual consent and gratification. There cannot be a trade unless the parties to it agree, any more than there can be a quarrel unless the parties to it differ. England, we say, forced trade with the outside world upon China, and the United States upon Japan. But, in both cases, what was done was not to force the people to trade, but to force their governments to let them. If the people had not wanted to trade, the opening of the ports would have been useless.

Civilized nations, however, do not use their armies and fleets to open one another's ports to trade. What they use their armies and fleets for, is, when they quarrel, to close one another's ports. And their effort then is to prevent the carrying in of things even more than the bringing out of things—importing rather than exporting. For a people can be more quickly injured by preventing them from getting things than by preventing them from sending things away. Trade does not require force. Free trade consists simply in letting people buy and sell as they want to buy and sell. It is protection that requires force, for it consists in preventing people from doing what they want to do. Protective tariffs are as much applications of force as are blockading squadrons, and their object is the same—to prevent trade. The difference between the two is that blockading squadrons are a means whereby nations seek to prevent their enemies from trading; protective tariffs are a means whereby nations attempt to prevent their own people from trading. What protection teaches us, is to do to ourselves in time of peace what enemies seek to do to us in time of war.

Can there be any greater misuse of language than to apply to commerce terms suggesting strife, and to talk of one nation invading, deluging, overwhelming or inundating another with goods? Goods! What are they but good things—things we are all glad to get? Is it not preposterous to talk of one nation forcing its good things upon another nation? Who individually would wish to be preserved from such invasion? Who would object to being inundated with all the dress goods his wife and daughters could want; deluged with a horse and buggy; overwhelmed with clothing, with groceries, with good cigars, fine pictures, or anything else that has value? And who would take it kindly if any one should assume to protect him by driving off those who wanted to bring him such things?

Public domain. Henry George, *Protection or Free Trade, An Examination of the Tariff Question, with Especial Regard to the Interests of Free Trade*. New York: Doubleday, Page, and Co., 1905.

Supporting Question 1	
Featured Source	**Source B:** Federal Reserve Bank of Dallas (W. Michael Cox and Richard Alm), annual report advocating free trade, *The Fruits of Free Trade* (excerpts), 2002

NOTE: The text below includes the introduction of the report, which is then followed by key tables from within the report.

The Fruits of Free Trade

Attacks on free trade don't make economic sense. In fact, the critics often get it backwards.

We hear that trade makes us poorer. It's just not so. Trade is the great generator of economic well-being. It enriches nations because it allows companies and workers to specialize in doing what they do best. Competition forces them to become more productive. In the end, consumers reap the bounty of cheaper and better goods and services.

We hear that trade costs jobs and depresses wages. Again, it's just not so. By spurring economic activity and reducing costs, trade helps create jobs. By enhancing productivity, it keeps U.S. companies vibrant, leading to fatter pay-checks and added benefits. Workers protected by trade barriers might keep their jobs a while longer, but the costs in inefficiency and higher prices make it economic folly. Whenever we erect barriers to trade, we negate the gains from free exchange and competition. Trade protection degenerates into a negative-sum game in which special interests jostle for advantage at the expense of the common good.

We hear that exports are good because they support U.S. industry but imports are bad because they steal business from domestic producers. Actually, imports are the real fruits of trade because the end goal of economic activity is consumption. Exports represent resources we don't consume at home. They are how we pay for what we buy abroad, and we're better off when we pay as little as possible. Mercantilism, with its mania for exporting, lost favor for good reason.

We hear that free trade isn't fair trade. Cheap imports can hurt higher-cost U.S. suppliers, but consumers certainly will gain. Why penalize them with tit-for-tat retaliation that only raises prices in the United States? Other countries' trade transgressions don't warrant missteps of our own. A nation will consume more whenever it opens its markets, even if other nations don't reciprocate.

We hear that trade makes us dependent on foreign suppliers, but America doesn't have the climate and resources to make everything it needs. Other nations can produce many goods and services at lower cost. The price of independence is too steep.

Americans can't afford to buy into these trade fallacies. As a society, we often have to choose between protecting domestic industries and opening markets. In a weakened economy, steelmakers, catfish farmers and other producers are lining up to declare war on imports, creating a potential hit on Americans' wallets. At the same time, U.S. negotiators are seeking to expand the world trading system with new free trade agreements.

We need to understand what's at stake. Being wrongheaded on trade increases the risk of making bad choices that will sap our economy and sour our relations with other nations. Getting it right will promote prosperity and peace.

EXHIBIT 2. **The Alchemy of Exchange**

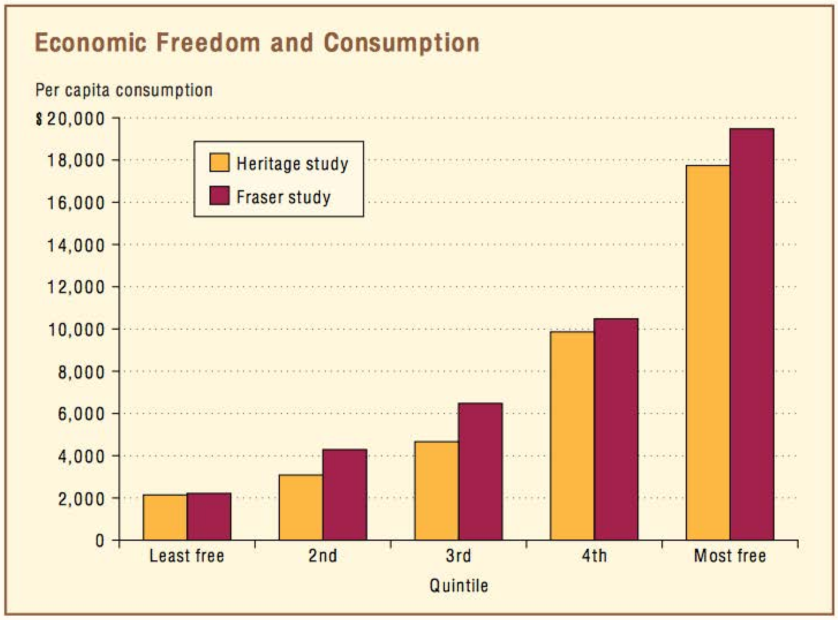
Five hundred Chinese workers can each produce four pairs of shoes or eight bushels of soybeans. One hundred U.S. workers can each produce five pairs or 100 bushels—more productive in both jobs but comparatively more so in farming. Under an autarkic regime—isolated from foreign trade—Chinese workers can afford one pair of shoes each and six bushels of soybeans; Americans, three and 40. Trading freely, China will specialize in shoes and America in soybeans, raising world production of shoes from 800 to 2,000 pairs and soybeans from 7,000 to 10,000 bushels. Chinese workers can then afford three pairs of shoes and 10 bushels of soybeans; American workers, five and 50.

	Autarky		Free Trade	
	China	U.S.	China	U.S.
Labor Force	500	100	500	100
Output per worker				
Shoes	4	5	4	5
Soybeans	8	100	8	100
Employment				
Shoes	125	60	500	0
Soybeans	375	40	0	100
Production				
Shoes	500	300	2,000	0
Soybeans	3,000	4,000	0	10,000
Consumption				
Shoes	500	300	1,500	500
Soybeans	3,000	4,000	5,000	5,000
Consumption per person				
Shoes	1	3	3	5
Soybeans	6	40	10	50

ANNUAL REPORT 2002 Federal Reserve Bank of Dallas 7

EXHIBIT 7. Free to Consume

People who live in free countries enjoy substantially higher living standards than those living in repressive countries. The World Bank collects data on per capita consumption by country. Two independent research groups—the Heritage Foundation in Washington, D.C., and the Fraser Institute in Canada—measure economic freedom across the world using a broad variety of criteria based on key components of free enterprise, including trade policies and openness to foreign investment. Relating the consumption and freedom data sets, one finds that per capita consumption in the economically freest fifth of countries is eight to nine times that of the least free fifth.



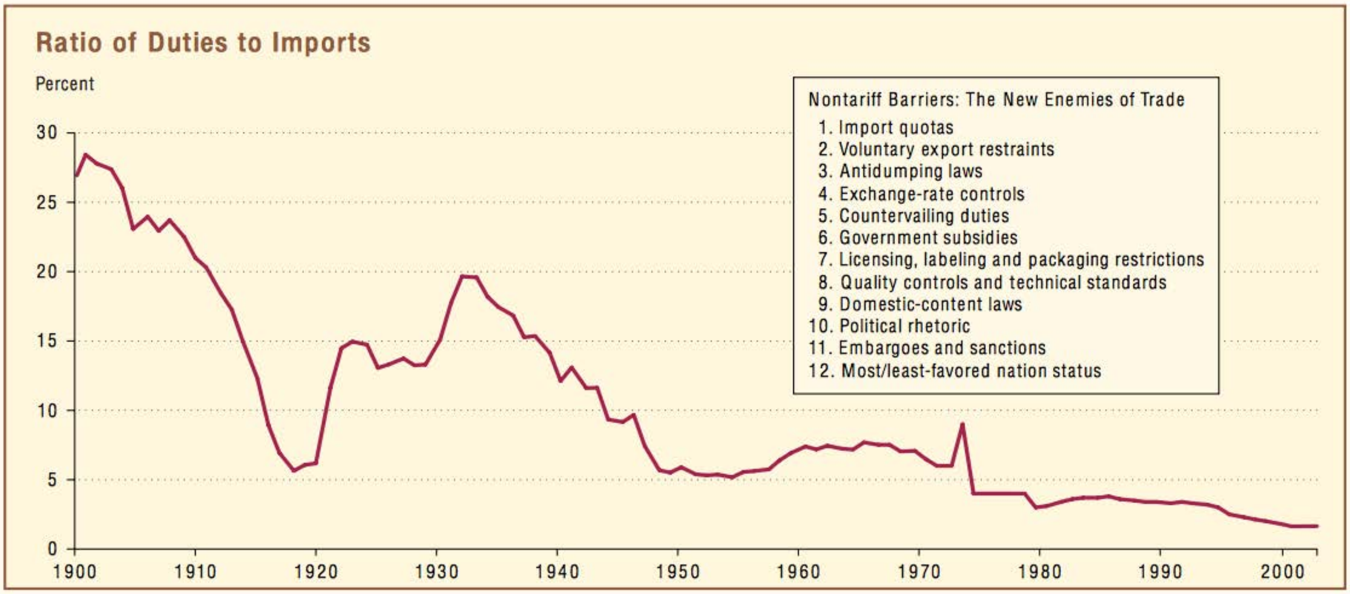
A Tale of Two Countries

In North Korea, which ranks lowest in economic freedom, consumers must wrangle for the most basic items, even food. Per capita income averages just $ 950 annually.

South Koreans enjoy the bounty of a capitalist-oriented, economically free society. Per capita income is $ 11,428—12 times that of North Korea.

EXHIBIT 8. **The Tax on Trade**

Reduced tariff rates lowered trade barriers and helped stimulate economic growth in recent decades. A growing number of nontariff barriers, however, threaten to undo the good. Voluntary export restraints; antidumping laws; government subsidies; licensing, labeling and packaging restrictions; domestic-content laws and others have emerged as the new enemies of free trade.



14 Federal Reserve Bank of Dallas ANNUAL REPORT 2002

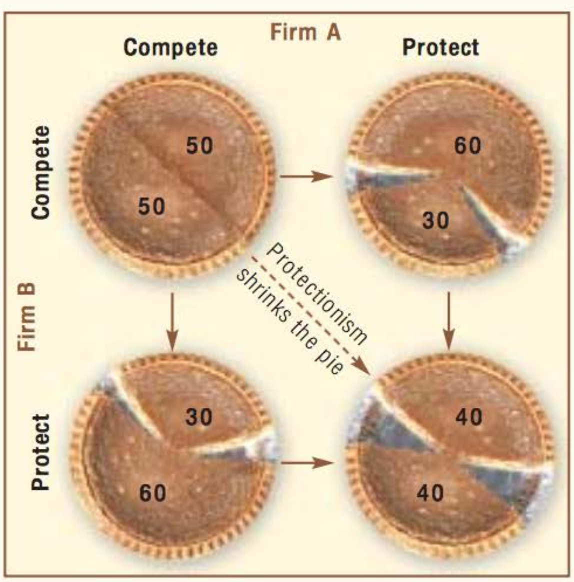


EXHIBIT 9. **The Politics of Protectionism: A Negative-Sum Game**

By offering trade protection, lawmakers create a dilemma for producers: Compete or seek protection. The economic pie is never greater than when firms compete because then they focus every resource on production. But suppose firm A can increase its piece of the pie (say, from 50 to 60 out of 100) by promising votes or campaign contributions in return for political favors. Then its incentive is to do so even though the total pie will shrink (say, to 90) as resources shift from production to protection. Its competitor, firm B, will do likewise, with similar results. The politics of protectionism lead ultimately to the worst possible outcome: a negative-sum game in which less is produced than under free trade. The only way out of this mess: *Nobody* gets protection.

EXHIBIT 13. **Protect and Destroy: The Lesson of Smoot–Hawley**

The stock market hates protectionism. That lesson—perhaps the clearest history has ever taught—comes from the Smoot–Hawley Tariff Act of 1930. In the late 1920s farmers, whose economic fortunes had not kept pace with industrialists', lobbied Congress for tariffs on agricultural products. The proposed act had few political sponsors at first (two of the three major political parties opposed it), and the stock market ignored it.

But as word of the bill spread, more and more U.S. producers joined the bandwagon, arguing for tariffs to assist domestic industry or protect them from foreign competition. Smoot–Hawley eventually expanded to cover more than 20,000 items across the gamut of U.S. production, with rates practically prohibitive to trade. With so many political constituents now on board, the Progressive and Democratic parties jumped the fence and on October 28, 1929, joined the Old Guard Republicans in supporting the legislation. That day the stock market crashed, falling 12 percent.

In the months that followed, foreign governments filed 34 formal protests, and 1,028 economists petitioned President Hoover not to sign the bill. But he did, on June 17, 1930, and the Great Depression engulfed the nation. The Dow Jones Industrial Average fell from a daily high of 381 in September 1929 to a low of 41 in 1932 as world trade contracted from $5.7 billion to just $1.9 billion three and a half years later.

It was the most expensive lesson markets have ever taught: Protect and destroy.

Dow Jones Falls as World Trade Contracts

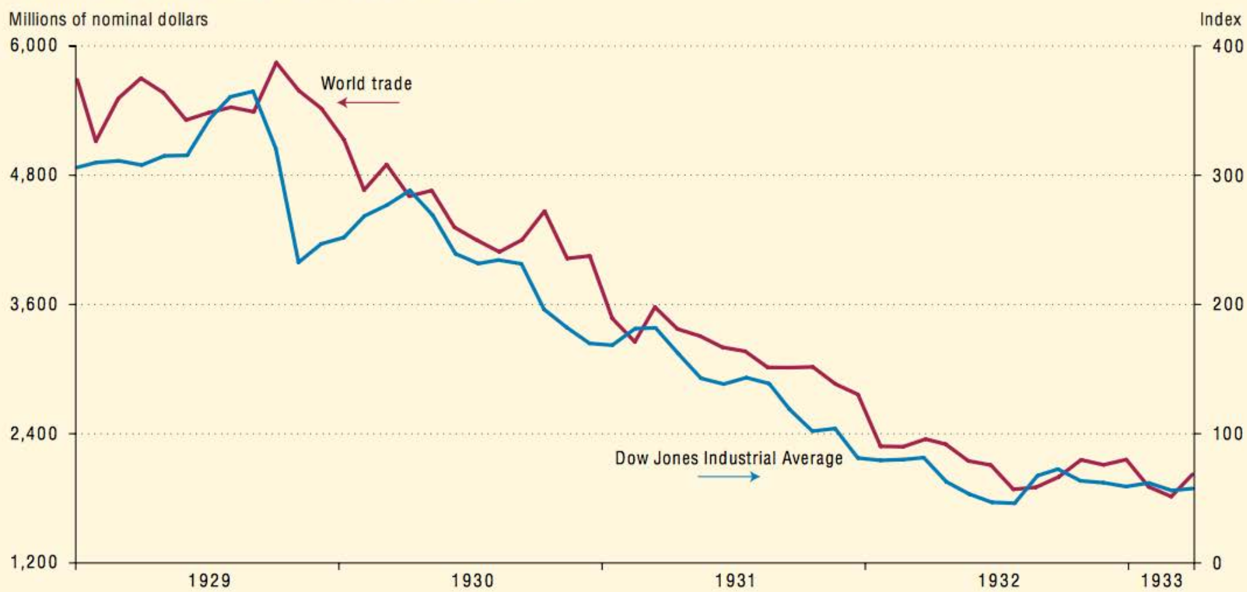
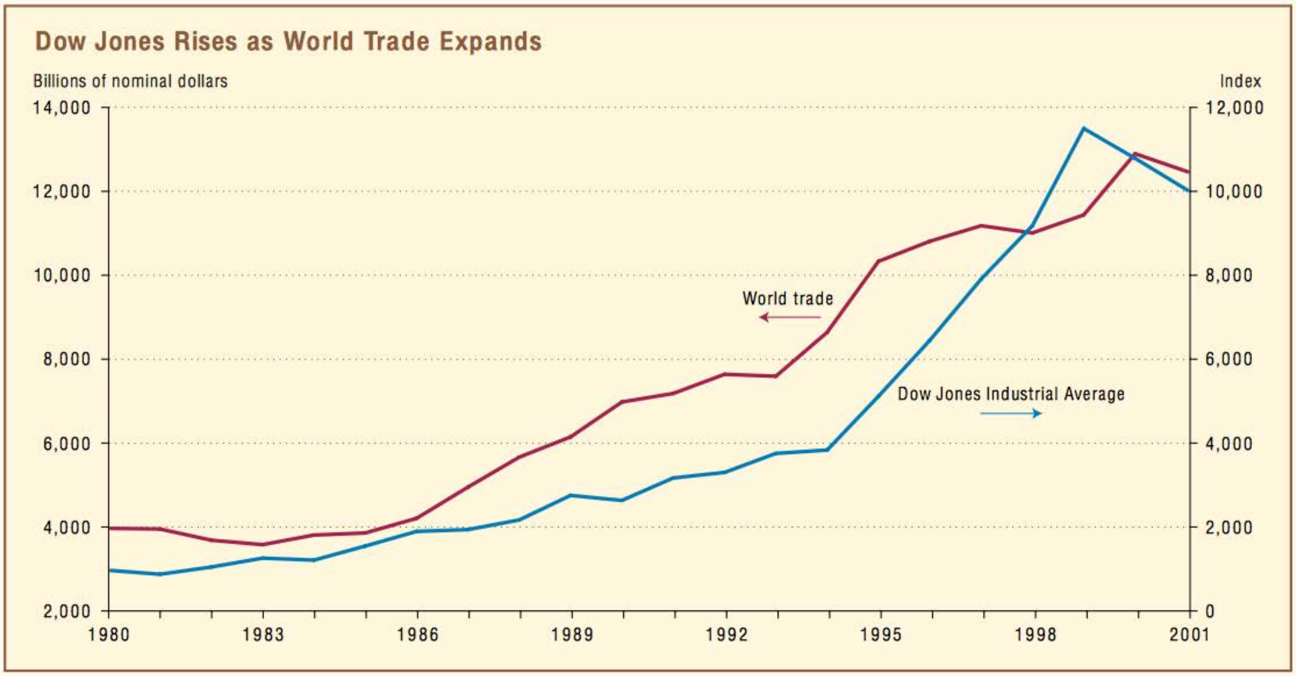


EXHIBIT 14. **Compete and Prosper: The Lesson of NAFTA and GATT**

The passage of the General Agreement on Tariffs and Trade, the North American Free Trade Agreement and GATT's successor, the World Trade Organization, ushered in an era of freer trade that's been applauded by stock markets worldwide. Smoot–Hawley taught us trade's lesson the hard way—protect and destroy. Today, we're relearning it the right way—compete and prosper.



The entire report can be found online at http://www.dallasfed.org/assets/documents/fed/annual/2002/ar02.pdf.

Federal Reserve Bank of Dallas, *The Fruits of Free Trade*. 2002 Annual Report. Used with permission.

Supporting Question 1	
Featured Source	**Source C:** Milton Friedman, videotaped Kansas State University lecture advocating free trade (transcribed excerpt), *Free Trade Versus Protectionism,* 1978

Transcribed Excerpt from the Lecture:

In the international trade area, the language is almost always about how we must export, and what's really good is an industry that produces exports. And if we buy from abroad and import, that's bad. But surely that's upside-down. What we send abroad we can't eat, we can't wear, we can't use for our houses. The goods and services we send abroad are goods and services not available to us. On the other hand, the goods and services we import, they provide us with TV sets we can watch, automobiles we can drive, with all sorts of nice things for us to use. The gain from foreign trade is what we import. What we export is the cost of getting those imports. And the proper objective for a nation as Adam Smith put it, is to arrange things so we get as large a volume of imports as possible, for as small a volume of exports as possible.

This carries over to the terminology we use. When people talk about a favorable balance of trade, what is that term taken to mean? It's taken to mean that we export more than we import. But from the point of view of our well-being, that's an unfavorable balance. That means we're sending out more goods and getting fewer in. Each of you in your private household would know better than that. You don't regard it as a favorable balance when you have to send out more goods to get less coming in. It's favorable when you can get more by sending out less.

The entire lecture can be found online at https://www.youtube.com/watch?v=urSe86zpLI4.