

**THE TRADE BALANCE MATTERS:  
FOCUSING ON TRADE  
IMBALANCE TO  
CREATE / RESTORE  
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Government dialogue about job creation is typically accompanied by extensive government expenditures or stimulus intervention. That dialogue, while intended to bolster the economy and reduce unemployment (particularly in sectors like manufacturing), excludes a leading cause of the current recession: foreign trade deficit.

Trade deficit is defined as a negative balance of trade, or a trade gap. Simply put, it means there is more coming in than going out. In the 1950's and 1960's the United States had trade surpluses, with trade deficits starting in 1971 and occurring every year since 1970, except for 1973. Our GDP grew an average of 4.3 percent in the 1950's and 1960's. From 1970 to 2000, our GDP grew an average of 3.1 percent, but only 2.4 percent from 2001 to 2008. This has to be associated with the trade deficit and loss of manufacturing jobs. The trade deficit ran \$151.7 billion in 1987, climbed to \$379.8 billion in 2000, and has hovered around \$700 billion the last four years (2005-2008).

Typical economist estimates are that a \$100,000 to \$120,000 drop in trade deficit creates one job. Using this logic, eliminating the trade deficit could create approximately **six million new jobs**.

Experts have long identified trade deficit as a detriment to the United States economic growth:

Peter Morici, economics professor at the University of Maryland, writes,

“As a consequence of the cumulative effect of trade deficits over the last ten years, the United States economy in 2006 will be about \$1.7 trillion smaller than it otherwise would have been. The continued economic prosperity of the United States demands that the country reduce the trade deficit significantly. In reality, trade liberalization has consisted largely of the United States opening its market, while many other countries have avoided equivalent concessions. Until both trade and banks are fixed, sustained economic growth can not be accomplished...the trade deficit will drag the economy back down into a double dip recession.”

Economist Howard Richman writes on <http://www.tradeandtaxes.blogspot.com/> February 7, 2009:

“John Maynard Keynes was the greatest economist of the 20<sup>th</sup> century; American economists consider themselves to be following Keynes' recommendations when they try to stimulate an economy with stimulus packages, but they studiously ignore the fact that Keynes had different advice for trade surplus countries and trade deficit countries. Countries can improve their lot by practicing strategies that produce trade surpluses. When they do so, they destabilize the trade deficit countries. *Volume 25* of Keynes collected writings are full of his plans that would regulate the world economy--with the goal of keeping trade in balance.”

“Warren Buffett reinvented Keynes prescription for trade deficit economy when he put together his plan for Import Certificates.

Now we are in a great recession caused by trade imbalances. China, the main trade surplus country, should be stimulating her economy, appreciating her currency, taking down her tariffs, and reducing her export subsidies. Doing so would help the debt-laden economies of her trading partners and, thus, allow them to buy more of her products. Instead she is enacting a half-hearted stimulus and increasing her trade manipulations in attempt to steal even more market share during the recession.

The United States could get right out of the current recession through Warren Buffett's Import Certificates plan. Our trade deficit was an enormous 5 percent of our GDP in 2008. We should be following the strategy tailored by Keynes and Buffett for an economy that is running a huge trade deficit..."

Trade imbalances can result in economic instability. And, when the country with instability is the United States, that instability affects the whole world. Workers are being laid off from California to New York and from Sweden to Brazil. For example, unemployment rose as follows: In Brazil, from 5.6% in October 2008 to 7.8% in January 2009; Germany from 6.5% in October to 7.4% in December; Sweden from 5.7% in October to 7.3% in January; and Australia from 4.1% in October to 5.3% in January.

An approach to balancing trade is presented in U.S. Senator Byron Dorgan's book, *Take This Job and Ship It*. It expands upon Warren Buffett's idea to balance our trade through a plan of Import Certificates, and it works as follows:

Senator Dorgan writes:

"The plan that I believe we should employ to tackle these dangerous trade deficits and stop the wholesale export of American jobs is one offered by Warren Buffett. He is a wealthy man, but he is so much more than that. Warren Buffett is one of our nation's original and creative thinkers, and someone with the credibility to be taken seriously.

So, when he calls our growing trade deficit and, the demise of our manufacturing sector dangerous, it is important to take note. The proposal he has advanced is simple, fair, and, more important, would work. It is a proposal that would lead to balanced trade and would, more than anything that has been done previously, finally force open foreign markets.

Here is the Buffett proposal in summary. It would achieve balanced trade by issuing Import Certificates (IC's) to U.S. exporters in the amount equal to the dollar value of their exports. Each exporter would be able to sell the IC's to others in their country who want to import goods into our country, or they might sell the IC's to exporters from other countries who wish to ship into the U.S. market. Here is the way Warren Buffett describes his plan:"

Senator Dorgan quoting Warren Buffett:

"To import \$1 million of goods, for example, an importer would need IC's that were the by-product of \$1 million of exports. The inevitable result: trade balance.

Because our exports total about \$80 billion a month, IC's would be issued in huge, equivalent quantities--that is, \$80 billion certificates a month--and would surely trade in an exceptionally liquid market. Competition would then determine who among those parties wanting to sell to us would buy the certificates and how much they would pay. (I visualize that the certificates would be issued with a short life, possibly of six months, so that speculators would be discouraged from accumulating them.)

For illustrative purposes, let's postulate that each IC would sell for 10 cents--that is, 10 cents per dollar of exports behind them. Other things being equal, this amount would mean a U.S. producer could realize 10 percent more by selling goods in the export market than by selling them domestically, with the extra 10 percent coming from his sale of IC's.

In my opinion, many exporters would view this as a reduction in cost, one that would let them cut the prices of their products in international markets.

Commodity-type products would particularly encourage this kind of behavior. If aluminum, for example, was selling for 66 cents per pound domestically and IC's were worth 10%, domestic aluminum producers could sell for about 60 cents per pound plus transportation costs in foreign markets and earn normal margins. In this scenario, the output of the U.S. would become significantly more competitive and exports would expand. Along the way, the number of jobs would grow.

Foreigners selling to us, of course, would face tougher economics. But that's a problem they're up against no matter what trade "solution" is adopted--and make no mistake, a solution must come. (As Herb Stein said, "If something cannot go on forever, it will stop.") In one way the IC approach would give countries selling to us great flexibility, since the plan does not penalize any specific industry or product. In the end, the free market would determine what would be sold in the U.S. and who would sell it. The IC's would determine only the aggregate dollar volume of what was sold.

To see what would happen to imports, let's look at a car now entering the U.S. at a cost to the importer of \$20,000. Under the new plan and the assumption that the IC's sell for 10%, the importer's cost would rise to \$22,000. If demand for the car was exceptionally strong, the importer might manage to pass all of this on to the American consumer. In the usual case, however, competitive forces would take hold, requiring the foreign manufacturer to absorb some, if not all, of the \$2,000 IC cost.

I believe that IC's would produce, rather promptly, a U.S. trade equilibrium well above present export levels but below present import levels. The certificates would moderately aid all our industries in world competition, even as the free market determined which of them ultimately met the test of 'comparative advantage'.

Would this start another Smoot-Hawley tariff war? Hardly. At the time of Smoot-Hawley we ran an unreasonable trade surplus that we wished to maintain. We now run a damaging deficit that the whole world knows we must correct.

For decades the world has struggled with a shifting maze of punitive tariffs, export subsidies, quotas, dollar-locked currencies, and the like. Many of these import-inhibiting and export-encouraging devices have long been employed by major exporting countries trying to amass ever-larger surpluses--yet significant trade wars have not erupted. Surely one will not be precipitated by a proposal that simply aims at balancing the books of the world's largest trade debtor. Major exporting countries have behaved quite rationally in the past and they will continue to do so though, as always, it may be in their interest to attempt to convince us that they will behave otherwise.”

Senator Dorgan writing in his book again:

“I have quoted Warren Buffett extensively about his plan because it's his idea. It is new, fresh, and interesting. And I support it. His point is not that we must have a neutral trade balance with every country. Rather, it is in the aggregate that we must strive to have a balance in our trade when we measure it against all of the countries with whom we trade.

This type of plan would have to be phased in over a certain time, but it can be done and would put us back on track toward balanced trade.

The free traders who are the architects of our current policy will say it is a giant retreat toward protectionism. Nonsense. It is a giant step toward common sense.”

Economic experts assert that economic growth and continued overseas job outsourcing cannot coexist. Economist Peter Morici adds, “The continued economic prosperity of the United States demands that the country reduce the trade deficit significantly”--and also states, “Until both trade and banks are fixed, sustained economic growth can not be accomplished.”

In September 2006, Senators Byron Dorgan and Russ Feingold fleshed out the Buffett plan in Congressional bill form (Senate Bill 3899) which they named the Balance Trade Restoration Act of 2006. This bill died in committee.

The economy, however, is in a far different place than it was in late 2006—and now is the perfect time to reexamine Import Certificates as a solution for balanced trade.

Balancing the trade deficit (and accordingly, boosting America's GDP), has become even more crucial as our nation's financial obligations grow. America's high trade deficit is being further burdened by costly stimulus packages, a large national debt with lots of interest costs, and expanding programs in education, health care and alternative energy. Entitlement programs like health care and social security will grow disproportionately in the next few years.

As the stimulus package begins to assist American families and boosts consumer confidence, we have the opportunity to shore up America's manufacturing sector too: creating new manufacturing jobs by balancing trade.

Balancing the trade deficit and balancing our nation's fiscal budget will ensure that America again will be the beacon on the hill. **The Trade Balance Matters.**

### **Author**

**Dick Alexander** is the founder and chairman of Global Shop Solutions, a manufacturing enterprise resource planning software company located in The Woodlands, Texas. He is a graduate of the University of Missouri, served two years as a Naval officer, earned his CPA, and is a Masters graduate of the Harvard Business School.

Alexander's last 45 years associated with manufacturing include being the controller of a major tractor manufacturer, and a medical electronics firm. In 1976, he founded Global Shop Solutions and remains an active chairman today.

Regarding the American economy, Alexander is concerned about maintaining the country's leadership in science, technology, education, and manufacturing.

### **Major References**

**Peter Morici** is a Professor of International Business at the University of Maryland and has served as Director of Economics at the U.S. International Trade Commission. The Ford, Rockefeller, Sloan, Donner and several other foundations have supported his work. He is the author of 18 books and monographs. His views are frequently featured on CNN, Reuters Financial Network, Bloomberg News, CNBC, ABC, Fox, National Public Radio and Broadcasting, and the BBC, and in columns on the opinion pages of newspapers and portals in the U.S. and abroad.

Most of the quotes in this article are taken from his monograph, *The Doha Round: No Help for America's Trade Deficit*.

Howard Richman, [www.tradeandtaxes.blogspot.com](http://www.tradeandtaxes.blogspot.com)

U.S. Senator Byron Dorgan, *Take This Job and Ship It* (Quoting Warren Buffett).