I Z A
World of Labor
Evidence-based policy making

NEW REPORT: Regulating trade is not the best way to help lower-income workers who suffer from trade-induced losses.

As the EU has announced retaliatory trade measures against Trump's new tariffs, a timely IZA World of Labor report looks at the effects of trade regulation on firms and workers. It shows that reducing adjustment costs to trade liberalization would be a more effective policy to boost employment than trying to restrict trade.

For years, economists have been nearly unanimous in their support for free trade. Recently, however, support for trade liberalization has been falling, as nationalism has risen in both the US and Europe. Regulating international trade has emerged as a political response to public discontent: calls for raising tariffs and pulling out of trade agreements are becoming more common. And most recently the US imposed a 25% duty on European steel and a 10% duty on European aluminium. However, Raymond Robertson of Texas A&M University summarizes latest research showing that reducing adjustment costs would be a more effective policy to boost employment than trying to restrict trade.

While trade increases national welfare, its liberalization can impose significant and concentrated costs on workers. When production is highly localized, lower-cost imports of a particular good will benefit consumers of that good nationwide; however, areas with a high concentration of producers competing with these imports will experience a fall in employment. Workers are facing adjustment costs of searching for new jobs, learning about new technologies, loss of firm and industry-specific human capital, and mobility (e.g. if they have to change location). These costs are often born disproportionately by certain segments of society, which has created a groundswell of anti-globalization in many countries.

From a national welfare point of view, the main issue is how much adjustment costs diminish the welfare gains from free trade. According to Robertson studies suggest that adjustment costs can lower the welfare gains from trade by 2–3%. However, these estimates nevertheless suggest that trade can create sufficient gains to compensate those who have to change sectors.

According to Robertson it is important to note that the costs to workers in these models come from the adjustment itself. This means that using trade policy to "correct" for the losses incurred by workers would likely cause a second round of adjustment, which would impose additional costs on workers. Not only would the gains to consumers be lost if tariffs were imposed, but the resulting shift of workers from their current sectors to the now protected sectors would burden them with another round of adjustment costs. Robertson says: "*Policymakers who impose the tariffs might be surprised to see the lack of employment growth in the protected sectors if workers do not sense that wages in the protected sectors are high enough to cover the associated adjustment costs*."

Instead the economist suggests: "*Policies that reduce adjustment costs may increase aggregate welfare more than regulating trade flows does…direct policies, such as moving subsidies and providing information about opportunities throughout the country seem to hold the greatest potential for success.*"

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Notes for editors:

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The site offers relevant and succinct information on topics including diversity, migration, minimum wage, youth unemployment, employment protection, development, education, gender balance, labor mobility and flexibility among others.

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