

Wonking Out: Economic Nationalism, Biden-Style

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If you're under 50, you probably don't remember when Japan was going to take over the world. But in the late 1980s and early 1990s, many people were obsessed with Japan's economic success and feared American decline. The supposedly nonfiction sections of airport bookstores were filled with volumes featuring samurai warriors on their covers, promising to teach you the secrets of Japanese management. Michael Crichton had a best-selling novel, "Rising Sun," about the looming threat of Japanese domination, before he moved on to dinosaurs.

Paul Krugman: Get a better understanding of the economy — and an even deeper look inside Paul's mind.

The policy side of Japanophilia/Japanophobia took the form of widespread calls for a national industrial policy: Government spending and maybe protectionism to foster industries of the future, notably semiconductor production.

Then Japan largely disappeared from America's conversation — cited, if at all, as a cautionary tale of economic stagnation and lost decades. And we entered an era of self-satisfied arrogance, buoyed by the dominance of U.S.-based technology companies.

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Now the truth is that Japan's failures have, in their own way, been overhyped as much as the country's previous successes. The island nation remains wealthy and technologically sophisticated; its slow economic growth mainly reflects low fertility and immigration, which have led to a shrinking working-age population. Adjusting for demography, the economies of Japan and the United States have grown at about the same rate over the past 30 years:

Image



Japan has done better than you think.Credit...FRED

In any case, however, we seem to be entering a new era of worries about the role of the United States in the world economy, this time driven by fears of China. And we're hearing new calls for industrial policy. I have to admit that I'm not entirely persuaded by these calls. But the rationales for government action are a lot smarter this time around than they were in the 1980s — and, of course, immensely smarter than the economic nationalism of the Trump era, which they superficially resemble.

Which brings me to the 250-page report on supply chains that the Biden-Harris administration released a few days ago. This was one of those reports that may turn out to be important, even though few people will read it. Why? Because it offers a sort of intellectual template for policymaking; when legislation and rules are being drafted, that report and its analysis will be lurking in the background, helping to shape details of spending and regulations.

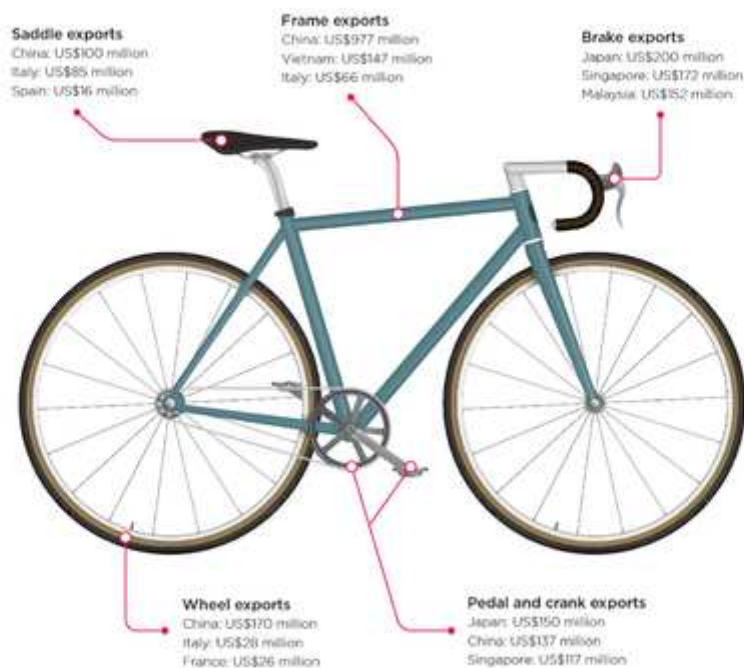
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Now, the world economy has changed a lot since the days when American executives were trying to reinvent themselves as samurai. Countries used to make things like cars and airplanes; nowadays they make parts of things, which are combined with other parts of things that are made in other countries and eventually assembled into something consumers want. The classic — and at this point somewhat tired — example is the iPhone, assembled in China from bits and pieces from all over. Last year's World Development Report from the World Bank, obviously written pre-pandemic, was devoted to global value chains and had a nice alternative example: bicycles.

Image

Figure 1.1 Where do bicycles come from?



Source: WDR 2020 team, using data from UN Comtrade database. See appendix A for a description of the databases used in this Report.

Spinning globalization.Credit...World Bank

I'm a bit surprised, by the way, to learn that Japan and Singapore have so much of the market for pedals and cranks. I thought America really led the world in cranks (charlatans, too).

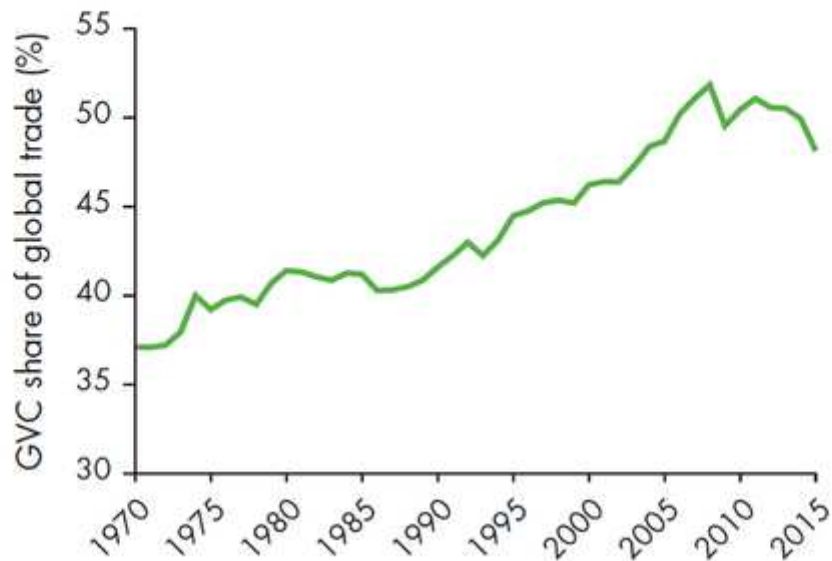
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Anyway, the World Bank offers a measure of the global value chaininess of world trade — the share of exports that cross at least two borders on the way to their final buyers:

Image

Figure 1.2 GVC trade grew rapidly in the 1990s but stagnated after the 2008 global financial crisis



Global value chaininess on the rise. Credit...World Bank

This measure shows that the big growth of globe-spanning supply chains isn't new; in fact, it took place mostly between 1988 and 2008. But the dangers associated with fragmented production have been highlighted by recent events.

The Biden-Harris report focuses on four sectors: semiconductor chips, batteries, pharmaceuticals and the rare earths that play a key role in much technology. It's not hard to see why.

The modern economy uses chips with practically everything — and the production of chips is very globalized. So we have a situation in which U.S. auto production is being crimped, thanks to drought in Taiwan and a factory fire in Japan disrupting the supply of these tiny but essential components. Moreover, much of the world's supply of rare earths comes from China, whose regime isn't noted for being shy about throwing its weight around.

And vaccine nationalism — countries limiting the export of vaccines and key components for making them — has become a real problem in the age of Covid.

As you might guess, then, a lot of the Biden-Harris report focuses on national security concerns. National security has always been recognized as a legitimate reason to deviate from free trade. It's even enshrined in international agreements. Donald Trump gave the national security argument a bad name by abusing it. (Seriously, is America threatened by Canadian aluminum?) But you don't have to be a Trumpist to worry about our dependence on Chinese rare earths.

That said, the supply-chain report goes well beyond the national security argument, making the case that we need to retain domestic manufacturing in a wide range of sectors to maintain our technological competence. That's not a foolish argument, but it's very open-ended. Where does it stop?

One thing is clear: If you thought the revival of economic nationalism was purely a Trumpist aberration, you're wrong. The Biden administration isn't going to go in for dumb stuff like Trump's obsession with bilateral trade imbalances, but it isn't going back to the uncritical embrace of globalization that has characterized much U.S. policy for decades. Will this lead to a new era of trade wars? Probably not — but don't expect a lot of big trade deals in the years ahead.

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