

# Economic Threats and Non-Threats

**What should we worry about?**

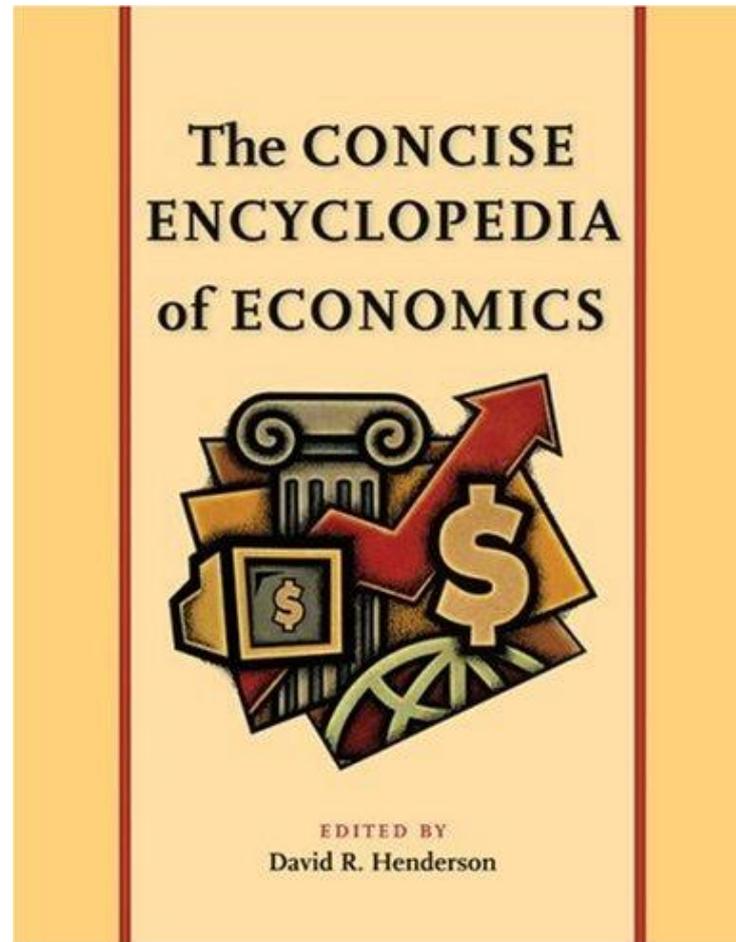
**and**

**What shouldn't we worry about?**

# My Jobs

- David R. Henderson
- Associate Professor of Economics
- Naval Postgraduate School
- Monterey, California
  
- and
  
- Research Fellow
- Hoover Institution on War, Revolution, and Peace
- Stanford University

# What I am most likely to be remembered for



# My Earlier Job

- Senior Economist, President Reagan's Council of Economic Advisers

January 1993



# Main Threat to Our Freedom

- Not the Chinese government.
- Not having our oil supply cut off.
- Not running out of arable land.
- Not Islamic terrorists.
- The main threat is what Ronald Reagan said it was on Thanksgiving 1981 during the Cold War, in his interview with Barbara Walters

- The main threat to our freedom is our own governments.

# Recent Losses of Our Freedoms

- Freedom to travel (TSA)
- Government Surveillance of our Phone Calls and E-Mail



# Loss of Our Economic Freedom

- Obamacare
- Permission required to start many businesses
- Proliferation of laws and regulations: “Three Felonies a Day”
- Federal Reserve: But not for the reason you might think
- Cronyism
- The Government Debt in Our Future

# Some Non, or Tiny, Threats

- China's Growing Economic Power
- The "Oil Weapon"
- Running out of arable land
- Terrorism

# Why is China Not a Threat?

- Globalization: A Boon to Mankind

- Globalization is the process by which regional economies are integrated through communication, transportation, and trade.

- Both sides gain from exchange.

# Should You Type for Yourself?

- Lawyer who's a great typist
- Lawyer has a so-so typist.
- Lawyer does 80 words a minute.
- Typist does 40 words a minute.
- So lawyer is twice as productive at typing as typist is.
- Question: should the lawyer do lawyering or should the lawyer type?

- Assuming lawyer is more than twice as effective at lawyering as typist is at lawyering, the lawyer should lawyer and the typist should type.
- Each should do what he/she has a comparative advantage in doing. That is Ricardo's insight.

# Protectionism

- Really should be called BARRIERISM
- Reverses gains from exchange
- Bastiat: Negative railroad
- Why Retaliation Hurts the Retaliator: Ronald Reagan's analogy

# Cost of Saving Jobs with Trade Restrictions

(Annual Cost to Consumers in Millions of Dollars)

<u>Industry</u>	<u>Total</u>	<u>Cost per Job Saved</u>
• Specialty steel	• 520	1.00
• Carbon steel	• 6,800	.750
• Bolts, nuts, screws	• 110	.550
• Textiles & apparel	• 27,000	.042
• Mushrooms	• 35	.117
• Automobiles	• 5,800	.105
• Motorcycles	• 104	.150

# Cost of Restricting Chinese Tires

# Don't Brag, Mr. President

- Obama, 2012 State of the Union:
- “Over a thousand Americans are working today because we stopped a surge in Chinese tires.”

# Annual Cost of Restricting Chinese Tires

- Cost increase on non-Chinese imports: \$817,000,000
- Cost increase on U.S.-made tires: \$295,000,000
- Total cost to U.S. consumers: \$1,112,000,000
- Cost per tire job saved: \$926,500

# What about Manufacturing?

- Loss in manufacturing doesn't indicate decline in manufacturing: it indicates increase in productivity
- China?
- “Manufacturing employment declined from the mid-1990s to 2002 in a number of countries whose economies are rapidly developing, including China, Brazil, and South Korea. In fact, China, Brazil, South Korea, and Japan had steeper percentage declines in manufacturing employment over that period than the United States.” Economic Report of the President, 2004, p. 76.

# Trade promotes Peace.

. “Peace is the natural effect of trade.”

--Montesquieu, 1750

- “When goods don’t cross borders, soldiers will.”

-- Otto T. Mallery, 1881-1956

# How much does trade promote peace?

The higher the gains from trade between two trading partners, the lower the level of conflict between them. A doubling of trade leads to a 20 percent decrease in belligerence. In short, trading nations cooperate more and fight less.

My (Henderson) summary of:

“An Analysis of Dyadic Dispute,” by Solomon W. Polachek, SUNY Binghamton and Carlos Seiglie, Rutgers University.

# Chinese “Sea Turtles”

Sea Turtles: People in China who have studied abroad.

Where do they go? North Korea?

About 37 percent come to the USA

Number of sea turtles on the Communist Party’s Central Committee:

2002: 6 percent

2007: 10.7 percent

# But What About China's Great Navy?

- How many aircraft carriers does China have?
- Hint: One eleventh of what the U.S. has.

# Used Carrier for Sale



# The Myth of the Oil Weapon

Either:

(1) It's a dud,

Or

(2) It will explode in its user's face.

# No lines; Dud; Explode

- First, no other oil-producing country, no matter what it does to its oil supply, can cause us to line up for gasoline.
- Second, an oil-producing country cannot impose a selective embargo on a target country because oil is sold in a world market. (Dud)
- Third, the only way a country's government can hurt another country using the "oil weapon" is by cutting output; doing so will hurt all oil consumers, not just the target country, will help all oil producers, friend and foe alike, and will hurt the country that cuts its output. (Explodes in user's face.)

# Oil “Dependence”



# Adam Smith

- “It is not from the benevolence of the butcher, the brewer, or the baker that we expect our dinner but from their regard for their own self-interest.”
- --Adam Smith, *The Wealth of Nations*, 1776.

# Henderson Channels Smith

- “It is not due to the benevolence of the world’s oil suppliers that we get our oil but from their regard for their own interests. Our oil supply is secure, not because our government threatens to use force against those who would make it insecure but because the world’s oil suppliers want to make money.”
- --David R. Henderson, “The Myth of the Oil Weapon,” 2007

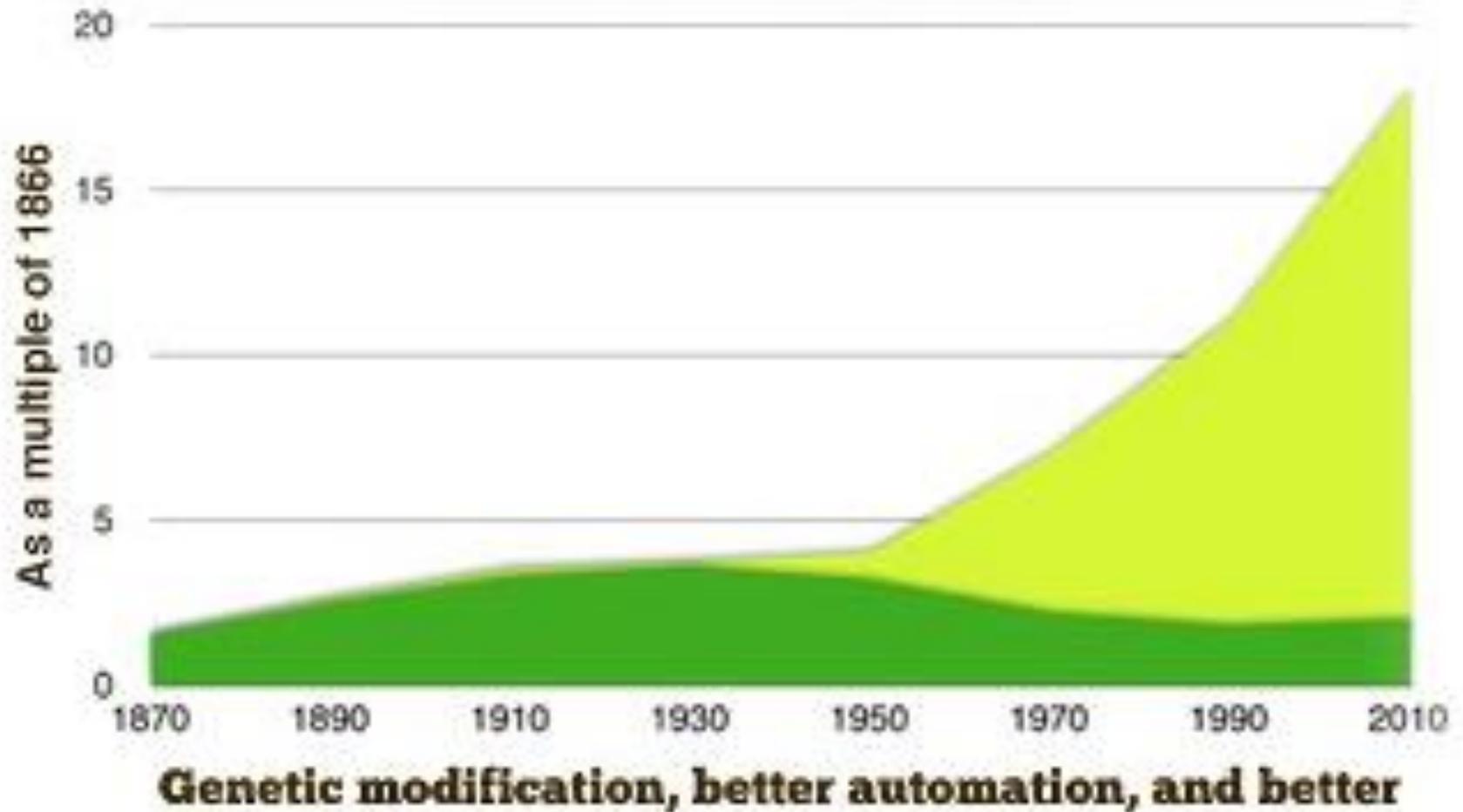
# Feeding the World

- “Whoever could make two ears of corn, or two blades of grass, to grow upon a spot of ground where only one grew before, would deserve better of mankind, and do more essential service to his country, than the whole race of politicians put together.”
- --Jonathan Swift, *Gulliver’s Travels*

# What If We Had Had No Progress Since 1961?

- People farm 38 percent of the earth's land area.
- If yields from land were at their 1961 levels, 82 percent of the earth's land would need to be farmed to feed today's population.
- Were we to replace all the industrial nitrogen fertilizer with manure, as many believers in organic farming advocate, we would need an extra seven billion cattle on an extra 47 million square miles of land to produce that manure. That's just 5 million square miles less than the total land area of the six habitable continents.

# Less Land, More Corn



# Why the Progress?

- Genetic Modification

# Let's Hear from an African



- “You people in the developed world are certainly free to debate the merits of GM foods, but can *we* eat first?”
- --Florence Wambugu, Kenyan ecologist

# The Terrorist Threat

“As the new millennium approaches, the United States faces a heightened prospect that regional aggressors, third-rate armies, terrorist cells, and even religious cults will wield disproportionate power by using--or even threatening to use--nuclear, biological, or chemical weapons against our troops in the field and our people at home.”

Defense Science Board, November 1997

# Whence Comes the Threat?

“As part of its global superpower position, the United States is called upon frequently to respond to international causes and deploy forces around the world. America's position in the world invites attack simply because of its presence. **Historical data show a strong correlation between U.S. involvement in international situations and an increase in terrorist attacks against the United States.**” (emphasis added)

Defense Science Board, 1997

If a foreign government did use terrorist methods in U.S. cities, we would face a choice. One option would be to change our foreign policy by refraining from meddling in other countries' affairs. Why do people fear a bomb exploding in Washington, D.C., but not, say, in Ottawa? To ask the question is almost to answer it. Few nations in the world have much of a grudge against Canada's government because it rarely meddles in other nations' business. Not so with the U.S. government, which meddles constantly around the world and has yet to see a country that it does not consider a "vital U.S. interest." (cont.)

The other choice would be to change the open nature of U.S. society completely. This would include increased restrictions on internal travel -- building on the precedent set by the Clinton administration for passengers on commercial airlines (who must show picture identification) -- and other restrictions on our freedoms that various bureaucracies in Washington probably have added to their wish list already.

If the second option were chosen, that would end the boom -- and a good deal more.

--David R. Henderson, "How Booming Cannons Hurt Booming Economies," November 1999.

# Terrorists' Goals

“Instead of religion, almost all suicide terrorist attacks around the world have in common a specific political goal: to compel a democratic state to withdraw combat forces from territory that the terrorists consider to be their homeland or prize greatly. This has been the central goal of every campaign of suicide terrorism since 1980, from Lebanon, Sri Lanka, and Chechnya to Kashmir, the West Bank, and Iraq. It also holds true for al-Qaeda, the organization of greatest concern to most Americans.”

Robert Pape, “Suicide Terrorism and Democracy,”  
November 1, 2006

# Now He Tells Us

“We can now remove almost all of our forces from Saudi Arabia. Their presence there over the last 12 years has been a source of enormous difficulty for a friendly government. It's been a huge recruiting device for al Qaeda. In fact if you look at bin Laden, one of his principle grievances was the presence of so-called crusader forces on the holy land, Mecca and Medina.”

Paul Wolfowitz, Deputy Secretary of Defense, May 9, 2003

# How Lethal is Terrorism?

“ Even with the September 11 attacks included in the count, the number of Americans killed by international terrorism since the late 1960s (which is when the State Department began counting) is about the same as the number of Americans killed over the same period by lightning, accident-causing deer, or severe allergic reaction to peanuts.”

- --John Mueller, “A False Sense of Insecurity”

# Driving vs. Flying

For the risk of flying to equal the risk of driving:  
There would have to be one set of September 11  
crashes per *month*.

--Michael Sivak and Michael Flannagan,  
*American Scientist*

# Panetta Impersonates Dick Cheney



# The Unlearned Lesson from 9/11

- United Flight #93
- Richard Reid, The Shoe Bomber
- The Underpants Bomber

# The Big Threat: Government

- TSA
- Obamacare
- Proliferation of laws and regulations: “Three Felonies a Day” (Harvey Silverglate)
- The Government Debt in Our Future
- Federal Reserve: But not for the reason you might think

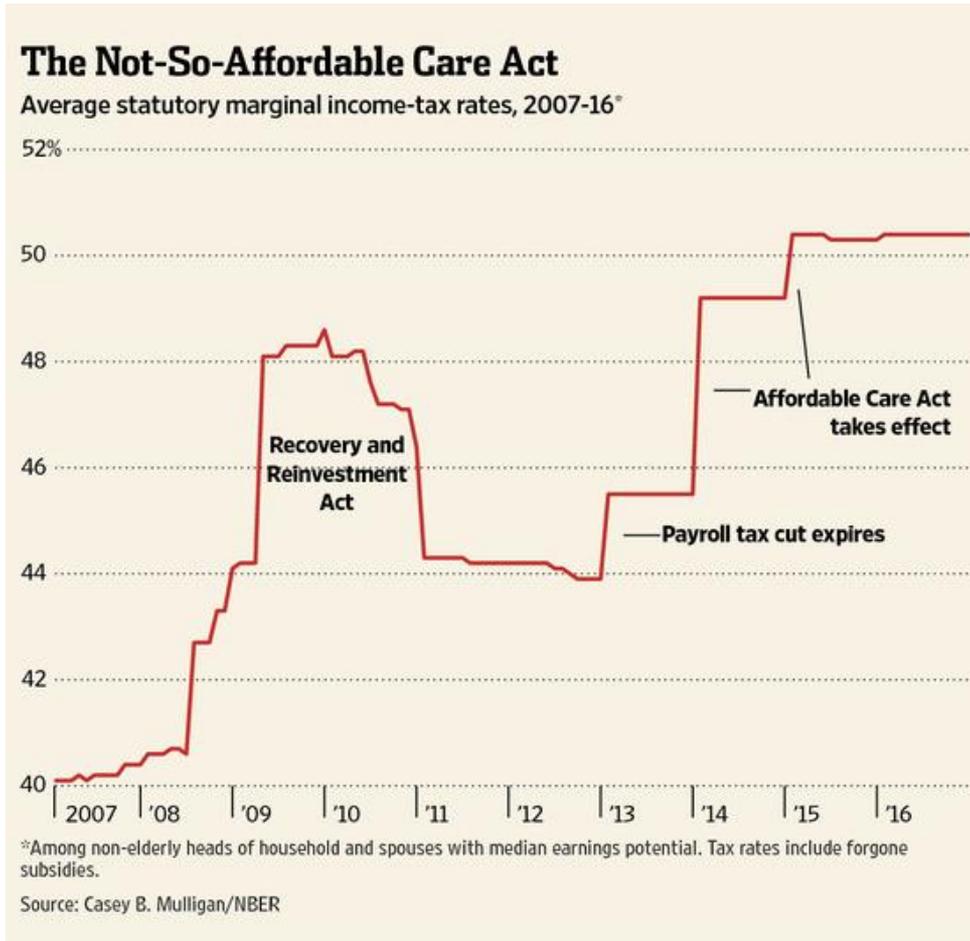
# Obamacare

- “If I (Obama) like your health insurance, you can keep it.”
- Undercuts the principles of insurance.
  - Can't price for risk
  - Requires coverages that people don't want

# High Implicit Tax Rates

- As you earn more, your subsidy falls.
- This increases your implicit tax rate.

# How ObamaCare Wrecks the Work Ethic



# Regulation Hurts Growth

“Federal regulations added over the past fifty years have reduced real output growth by about two percentage points on average over the period 1949-2005. That reduction in the growth rate has led to an accumulated reduction in GDP of about \$38.8 trillion as of the end of 2011. That is, GDP at the end of 2011 would have been **\$53.9 trillion** instead of **\$15.1 trillion** if regulation had remained at its 1949 level.” [Bold added]

Dawson and Seater, “Federal Regulation and Aggregate Economic Growth,” *Journal of Economic Growth*, Vol. 18, 2013.

# Regulation

FDA Says No to 23Andme selling genetic tests

CFTC Bans InTrade from Having U.S. Customers

European Union cuts Iran off from SWIFT

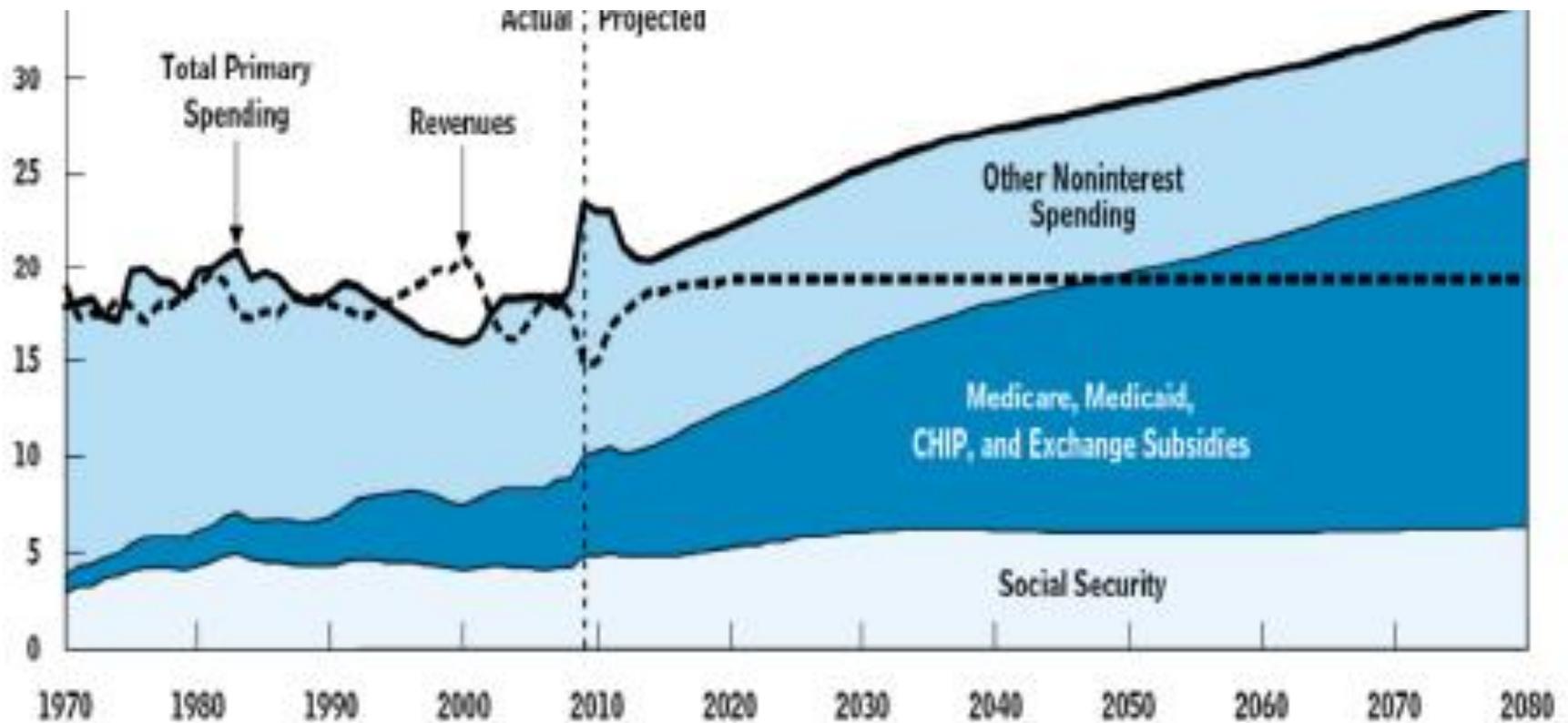
FCC Regulates Internet—the most dynamic sector in the history of America—as a public utility

Legal Workforce Act of 2015 (voted 20-13 out of committee): Phase in over 2 years of E-Verify

Operation Choke Point

(These are just a few of the new regulations and proposed regulations in the last 3 years.)

# The Federal Spending in our Future: % of GDP



Source: Congressional Budget Office.

# Three Options to Deal With Debt

- Cut Spending
- Inflate
- Default

# Inflation? Won't Help

- The average seigniorage of industrial countries between 1973 and 1978, a period of high inflation, was only 1.1 percent of Gross National Product.

Stanley Fischer, Governor of Bank of Israel, 2005-2013

Inflation's implicit tax on real cash balances will not be much more able to resolve the escalating budgetary problems of the U.S. government than would an excise tax on chewing gum.

# Default

“Countries do not go bankrupt.”

--Walter Wriston, former head of Citibank

“There is a myth that floated around the banking community not many years ago that governments do not go bankrupt. I cannot imagine who dreamed that one up.”

--Gordon Tullock, 1990

# Default: A Balanced Budget Amendment with Teeth

# The Real FED Threat: Central Planning

Rather than following the prescription of Milton Friedman to merely control the total money supply and permit the market to allocate credit, Bernanke favors credit allocation by the central bank. The evidence for this expanded role is sprinkled throughout his book. It is reflected in Bernanke's obsessive focus on interest rates as the sole indicator of monetary policy, his targeted but sterilized bailouts, his paying of interest on reserves, his expanding Fed assets to include mortgage-backed securities, and his efforts to manipulate the yield curve on Treasuries.

--Jeff Hummel

# Me on Stossel

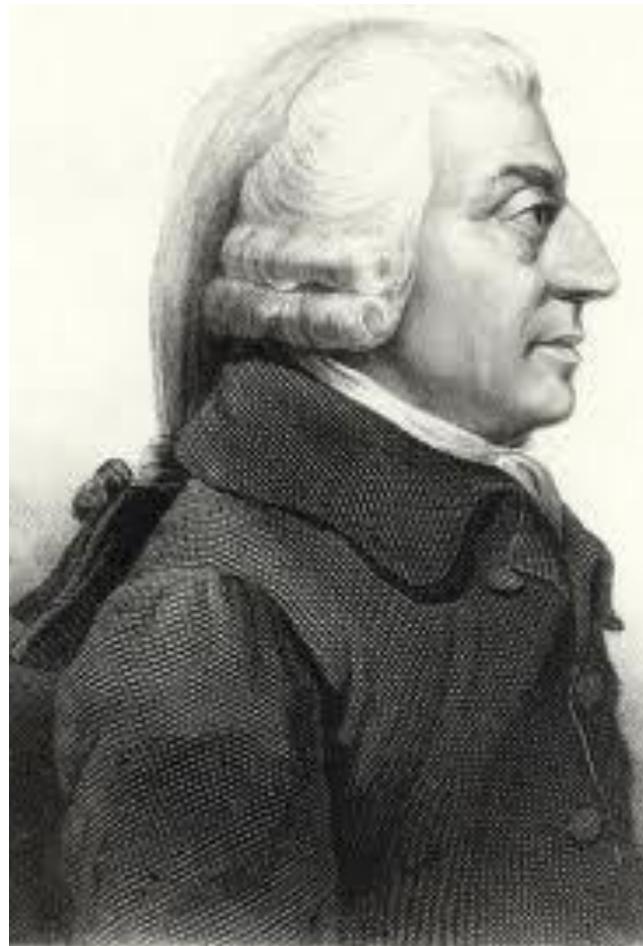


# The Bad

“That’s positively French!”

--Henderson to Stossel on Unemployment  
Benefits up to 99 weeks

# Adam Smith



# The Good

Adam Smith:

“There is a great deal of ruin in a nation.”