Global Imbalances: Trade Tensions and Capital Flows
By Professor Wade Jacoby

Trade is a tricky subject, and it's made trickier by two dangerous myths: first, that free trade is automatically good or, second, that protectionism is the answer to the problems trade brings. Don't buy either myth. First, all coherent trade theories recognize that some people will be hurt from trade, but too often, we're not honest about the 'no pain, no gain' nature of trade. In the US, the least educated are the most hurt, but the pain can hit quite a few households and hit them quite hard. And as a country, we've done a generally terrible job of retraining or otherwise helping those most hurt.

But trade protectionism is an ineffective band-aid, and it's often applied to the wrong wound. To understand that, however, we have first to understand the implications of the sharp rise in inequality, we see all around us. As inequality grows in one country after another, something odd starts to happen: because the wealthy save a high portion of their income while the poor and middle save very little, more inequality means a lot more savings. In some places, this is the household savings of the well-off, but in other countries, it can be companies sitting on huge piles of cash, or even governments like Germany running a budget surplus. And if a country's savings go *up*, then their consumption has to *fall* because those are just two sides of the same coin. Think China, Korea, the Netherlands, Germany.

Here's where it gets really tricky: as a country's consumption falls, business has less incentive to invest, and that falls too. If that happens, then the only source of growth left is trade: making money through exports because either consumption or investment (or both) become weak sources of growth. Lots of countries are now doing this. Meanwhile, the US is left to soak up those extra savings, which flow to our deep and open (and mostly anonymous and legally-protected) capital markets. Some Americans benefit a lot from these flows, but many are harmed by the increase in private debt it causes and by the unemployment represented by the jobs lost to countries driving down their own consumption and getting fat on ours. Other Americans are hurt by soaring property prices driven up by foreign buyers. Thus, the inequality that launches the problem then produces even more inequality in its effects. Those with assets do well from this system. Those without often get creamed.

And here's where UVU comes in. Its dual mission can make a big difference, particularly in getting non-traditional students the education, training, and credentials to compete in a modern economy. This would help address the inequality problems at the root of our trouble. So let's drop the fantasy that a rising tide must lift all boats and recognize that sometimes the tide never moves that much, and some people just get thrown overboard. And let's drop the other fantasy that we can solve a capital flows problem with trade tools. That won't work, no matter how much the president wants it to. Let's invest in the next generation, making them smarter and more productive. Let's limit foreign capital inflows to our investment needs. Above all, let's do a lot of things to bring down inequality *everywhere* so that fewer states feel they have to repress labor income and lean on exports so heavily. Healthier domestic politics will fix the unhealthy international trade system we have now. It’s the only real fix there is.