The New Protectionists

BY MELVYN KRAUSS

Lew's shrill criticism of Germany suggests the U.S. Treasury has been thoroughly politicized.

The U.S. Treasury Department's recent accusation that Germany's export surplus is beggaring euro area partners such as Greece and France is as wrong in terms of economics as it is terrible politics.

Germany makes high-quality products at competitive prices. That's why it has a current account surplus that is forecast to reach 7 percent of GDP this year, a position that the United States and other developed nations can only envy. This success is not due to some neomercantilist policy of using export subsidies and unfair trade interventions, so in what way can it be described as unfair?

If the United States, or France, or Italy could pull off such an export success story, they would. So they should: Just because a country has an export surplus doesn't mean it is stealing from its neighbors.

Underlying the arguments of Germany's critics is the assumption that Europe's periphery countries gain nothing from the German surplus. Of course they do. When auto workers in Sindelfingen and Wolfsburg take vacations in Mykonos and Tuscany, the money they spend in effect contributes to Greek and Italian exports. Tourism accounts for more than 16 percent of Greece's GDP, and the biggest number of visitors come from—Germany.

Southern workers are also coming to Germany in record numbers to work in export industries, and commonly they remit a large part of their compensation home. This represents an import of labor services by Germany that aids the periphery. And

Melvyn Krauss is emeritus professor of economics at New York University and a senior fellow at the Hoover Institution at Stanford University.

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220 I Street, N.E.
Suite 200
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Fax: 202-861-0790
www.international-economy.com
editor@international-economy.com

don't forget that earnings from the manufacture of goods for export are often spent on imports, some of which are from the periphery.

The Treasury report's most startling charge is that the German export surplus is responsible for "a deflationary bias for the euro area as well as for the world economy." This is a bizarre way for the United States to treat an ally. First, the National Security Agency bugs Chancellor Angela Merkel's mobile phone, then the administration accuses Germany of causing global deflation. High-handed behavior of this kind weakens U.S. influence and leadership.

Treasury argues that by exporting too much, Germans must be spending too little, acting as a black hole that sucks in demand from countries that in many cases are already suffering a catastrophic demand shortage. The assumption behind this thesis is that only domestic demand can stimulate the periphery, but that is clearly mistaken.

As Germany's export sector grows, so does the economy and its demand for goods and services, including for Greek and Italian beaches and labor. Yes, increasing domestic demand at the euro area's German core also has stimulative effects for the periphery, but whether reallocating German savings from the export sector to domestic demand would benefit the likes of Spain, Italy, and Greece more than the current situation isn't at all clear.

If Germans are given more money, for example, will they spend it or save it, buy houses or imports? And if they do buy a lot more imports, will these be Greek or Chinese? None of us know, just as we can't predict what happens to the health of the euro area's strongest economy if its exports decline. A weak, overindebted German economy wouldn't help Greece or the global economy as a whole; it would hurt them.

What we do know is that Germany's exporting of savings is not responsible for falling global prices. Haven't the U.S. Treasury and its cheerleaders noticed that commodity prices have come down sharply in recent months? So far this year, gasoline on the New York Mercantile Exchange is down by 10 percent, copper by the same, and corn by 40 percent. The decline in commodity prices and its effect on euro area inflation has absolutely nothing to do with the German export surplus. Indeed, the more Germany exports, the more it supports commodity prices, by importing the raw materials it needs to make cars and industrial machinery.

That the U.S. Treasury secretary has descended to shrill Germany-bashing suggests he isn't listening to his own highly professional staff, and it's evidence of how politicized Treasury has become during Jack Lew's short tenure. If anything deserves the label "beggar-thy-neighbor" that critics use for German policies, it is the Treasury's attack on Germany's export surplus and its concomitant obsession with increasing German domestic demand.

How convenient for bankrupt Detroit—which sells cars in direct competition with Mercedes-Benz in Sindelfingen and Volkswagen in Wolfsburg—for the U.S. Treasury to point the finger of blame for the world's economic problems at German exports. Where I live in California's Silicon Valley, one sees more German cars on the roads than Cadillacs, Chevrolets, and Fords. German cars are no problem for us. If Lew wants to bail out Detroit, he should do so directly, instead of pursuing disguised protectionism.

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Let's just walk through what would need to happen if Germany's government were foolish enough to follow the advice coming from the United States. The government in Berlin would need to boost domestic demand, presumably by increasing public spending. This would have the effect of bidding away resources from Germany's export sectors, increasing labor and other costs of production. That would undermine the current competitive advantages of Germany's export sector. So yes, BMWs would become more expensive to buy in Silicon Valley, making its U.S. competitors more attractive.

German officials called the Treasury report incomprehensible, but I think not—it is the evil witch of U.S. protectionism dressed up as Snow White. Those who think the economic crisis would be fixed if only Germany would rack up more debt have leapt onboard the Treasury boat to support their own Keynesian campaigns to increase government spending. In the process, they have opened themselves up to the charge of supporting Treasury protectionism. ◆