# Explaining Gradualism in Trade Liberalization: A Political Economy Approach

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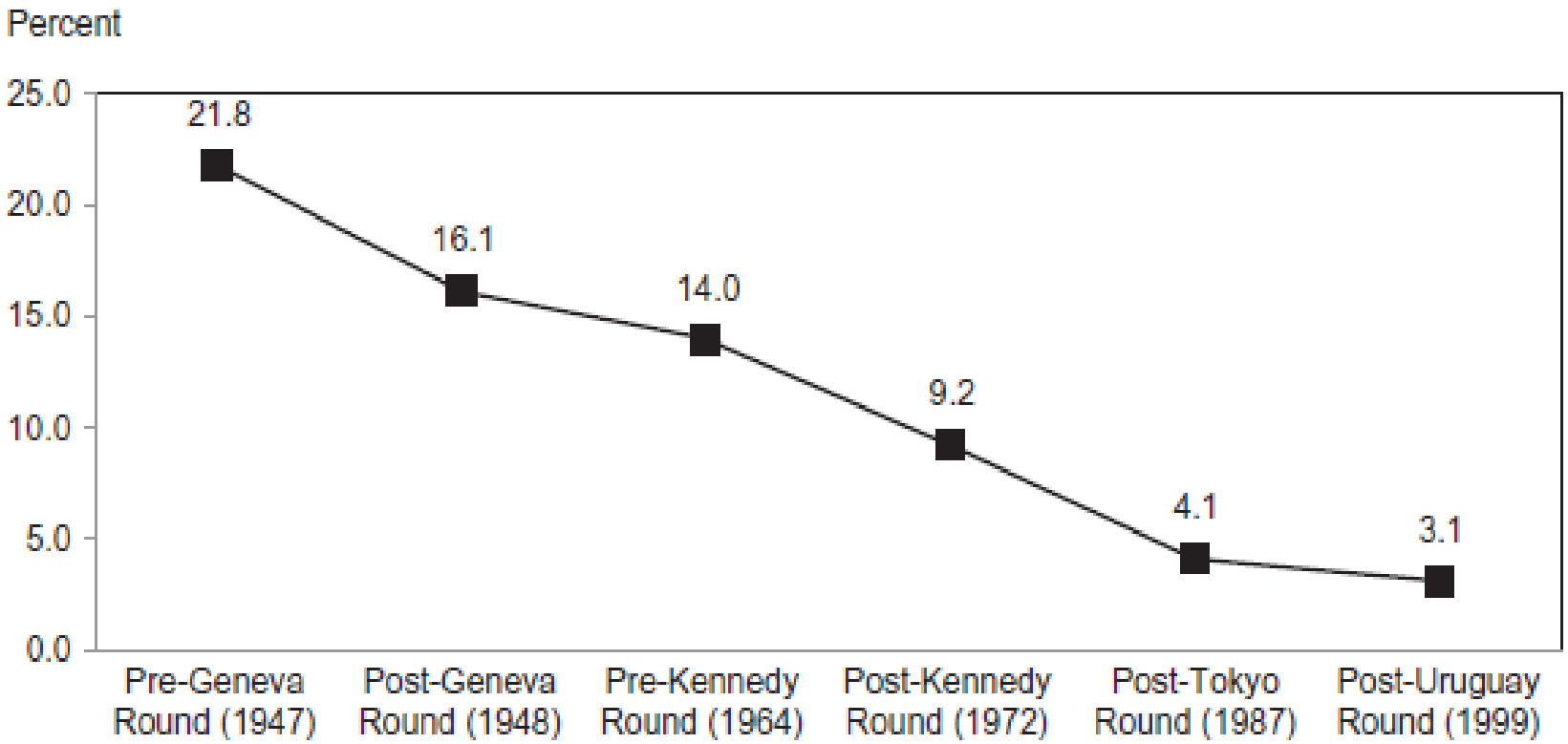
# Average tariffs for U.S., Western Europe, and Japan




Source: Bown, C.P., Irwin, D.A., (2017) "The GATT's Starting Point: Tariff Levels circa 1947," in Assessing the World Trade Organization: Fit for Purpose?, M. Elsig, B. Hoekman, and J. Pauwelyn eds., Cambridge University Press, forthcoming, fig. 1

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2. What are the frictions preventing free trade?

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- Convex adjustment costs as workers leave import-competing sector (Mussa 1986); Furusawa & Lai similar for repeated game
- Gradual reductions improve welfare when there's a minimum wage (Mehlum 1998)
- Workers lose specialized skills as they leave (Staiger 1995)
- Lobbying and capital mobility (MRC 2007)

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## Limitation of punishments to WEC (Zissimos 2007)

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- i.e. a story that doesn't hinge on specific nature of trade
- The hope: lessons could be applied to other issue areas

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- BUT ability to maintain protection reduced by shocks to political support
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- Immediate loss of protection / rents *can* $\Rightarrow$ erosion of future political power and accompanying protection
- Demonstrate with a dynamic model of political economy

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5. Tariff revenue is distributed and consumption takes place (not explicitly modeled)

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- $F_X(m_t, l_t) = A(m_t)F_t^{\alpha} l_t^{1-\alpha}$

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  - Represents import-competing sector, X

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**Assumption 1**

$\gamma(e_{t-1}, \theta_{t-1})$ is increasing and concave in $e_{t-1}$ for all $\theta_{t-1} \in \Theta$.

# Lobby

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$$\max_{e_t, m_t, l_t} \sum_{t=1}^{\infty} \left\{ A(m_t) \cdot F^{\alpha} \cdot l_t^{1-\alpha} \left[ P^W + \tau(\gamma(e_{t-1})) \right] - l_t - \mu_t - e_t \right\}$$

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- $\tau_t$: home tariff on good X

# Two-Period Model

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Given $\gamma_0$

$$\max_{l_1, e_1, \mu_1, l_2, \mu_2} \left\{ A(m_0 + \mu_1) \cdot F^{\alpha} \cdot l_1^{1-\alpha} \left[ P^W + \tau(\gamma_0) \right] - l_1 - \mu_1 - e_1 \right\}$$
$$\left\{ A(m_1 + \mu_1) \cdot F^{\alpha} \cdot l_2^{1-\alpha} \left[ P^W + \tau(\gamma(e_1)) \right] - l_2 - \mu_2 \right\}$$

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**This is gradualism!**

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- CRS production