

# Hoover's Last Legacy

## *Time to Fix America's Tariff System*

By Edward Gresser

Inauguration season is, among other things, a chance to look again at old policies and discard those that either no longer serve their purpose, or were bad ideas to begin with. A policy perfect for such an examination is the last living legacy of the Hoover administration: the American tariff system. Long after its Jazz Age contemporaries have faded into history—Prohibition, the Sacco & Vanzetti case, the great stock market crash—America's 70-year-old tariff system survives. One wonders why.

At home, Progressive Policy Institute research<sup>1</sup> finds that while American tariffs seem ineffective at protecting U.S. jobs, they are very good at complicating the lives of single mothers. This is because tariffs are low on industrial inputs for factories, luxury goods, and other products bought mainly by businesses and wealthy consumers, but high on cheap clothes, shoes, food, and other products important to poor families. An extreme, but not unrepresentative, case is that of cheap sneakers, which carry the highest tariff rate in the system (48 percent). This tariff then travels through the system to end as a large, hidden sales tax. Bought only by the poor, these shoes have not been made in the United States since at least the 1970s.

Internationally, the tariff system's effects are similar. Tariffs are barely speed bumps for big economies like Japan, Germany, China, and the United Kingdom, whose exporters encounter few high rates. They present greater obstacles to smaller and poorer economies like Cambodia, Bangladesh, Pakistan, and, perhaps soon, Afghanistan.

An appropriate opportunity to scrap the system exists in the World Trade Organization (WTO)'s Doha Round of trade policy negotiations as part of a general reform of world trade regimes. But that will take time. An immediate priority should be to eliminate tariffs for the countries hit hardest—the least-developed Asian countries and states in the Muslim world supporting the U.S. fight against terrorism. A bill proposed in the 108th Congress by Sens. Max Baucus (D-Mont.) and John McCain (R-Ariz.), along with Reps. Adam Smith (D-Wash.) and Cal Dooley (D-Calif.), would eliminate tariffs for the Muslim world. It is the right foundation, in the next Congress, if slightly augmented, to include the least-developed Asian states. The cost to the United States would be low or nil. To the extent that such a policy would change import patterns, the likely result would be to shift purchasing away from China and some other large, diversified states rather than to increase competition in the United States. Yet the ethical and strategic benefits would be high.

## The Tariff System in Action

The table on pages 4-5 illustrates the unintentional results of the U.S. tariff system. It divides the roughly 11,000 products covered by American tariffs into four groups, as follows:

1. **Duty-free products**—those with no tariffs at all—are grouped in the far left column. Examples include sectors of high-tech industry, such as computers, pharmaceuticals, semiconductor chips, and airplanes; some light industry products, notably toys and furniture; and natural resources and tropical goods such as diamonds, aluminum, coffee, teakwood, and tea.
2. **Low-tariff goods** (with tariffs under 5 percent) come next, in the second column from the left. These are most often sophisticated manufactured goods of various types, such as lamps, boats, cars, eyeglasses, and luxury silverware.
3. **Medium-tariff goods** are listed third from the left—those with tariffs from 5 percent to 14.9 percent. Examples of these goods include fabrics, expensive shoes, bicycles, and some types of clothes.
4. Finally, on the right, are **high-tariff goods** with rates of 15 percent or higher. Most of these are clothes (especially cotton and artificial-fiber clothing) and moderately-priced to cheap shoes, together with household goods, such as cheap spoons, plates, and drinking glasses, foods such as butter and orange juice.

The table then arranges the top 100 imports from each country in a row, with the zero-tariff products on the left, the high-tariff products on the right, and the others in between. (In all but a few cases, the top 100 goods cover the vast majority of trade.) The countries with the most high- and medium-tariff goods—that is, the largest number of products on the right side of the table—appear at the top. The countries with the fewest high-

tariff goods are at the bottom of the table. Goods imported under duty-free programs, finally, are counted as having no tariffs.

The results are startling. Cambodia appears at the very top of the list, with 52 high-tariff and 42 medium-tariff products. (All 94 of these goods are varieties of clothing.) Bangladesh, Pakistan, Nepal, Mongolia, and Egypt follow closely behind, demonstrating that the system is effectively strongest on very poor Asian countries and large majority-Muslim states.

Middle-income countries such as Brazil, Thailand, China, and India appear in the center of the table, illustrating their relatively diverse set of exports.

At the bottom, and thus least affected by tariffs, are a mix of rich countries, African states, and oil exporters. For example, 69 of the top 100 imports from the United Kingdom had no tariffs and only one (Shetland wool sweaters) rose above 15 percent. Norway had 77 duty-free goods, and no high-tariff products at all. Likewise, only nine Saudi products, and three Ghanaian goods appear on the medium- and high-tariff side of the table. Norway had 77 duty-free goods and no high-tariff products.

## An Explanation

Why the disparities? Why the harsh treatment of low-income Asian and Muslim states, and the mild treatment of rich countries? Perhaps equally interesting, why do Africa's least-developed countries fare so much better than Asia's? Two facts answer these questions: the structure of the tariff system and the success of regional trade initiatives, like the African Growth and Opportunity Act (AGOA), Caribbean Basin Initiative (CBI), and Andean Trade Preference Act (ATPA).

### 1. Structure of Tariff System

First, the tariff system is not a uniform tax on imports. It treats different products in radically different ways.

The Hoover administration, designing the system in the 1920s, hoped to keep input costs

low for American factories while restricting foreign competition in finished goods. It was especially vigilant in Industrial Revolution-era industries, notably clothing, that had begun to encounter sharp foreign competition. The structure of the system reflected these considerations, and despite many changes, still reflects them today. Natural resource products like oil, gems, and minerals never had many tariffs in any case, reflecting the Hoover administration's determination to allow American factories to buy them without extra costs. Tariffs on heavy-industry products and technologies were higher than they are now, but still relatively low because international competition was weak. Tariffs on light-industry goods like clothes, fabric, and shoes were exceptionally high, reflecting the fact that international markets were already competitive in the early 20th century.

Since then, the United States has taken part in six decades of trade negotiations, beginning in Franklin D. Roosevelt's administration. These included eight rounds of General Agreement on Tariffs and Trade (GATT) talks, plus one WTO agreement. The agreements eliminated Depression-era tariffs on many types of high-tech and heavy-industry goods, whose makers have been interested in export opportunities. Tariffs have likewise fallen to quite low levels on cars, boats, and other heavy-industry products. In practical terms, computers, desks, toy robots, and airplanes have no tariffs. Cars get a 2.5-percent tariff and barrels of oil usually get fees of \$0.10 to \$0.50.

The older industries, however, often opposed these negotiations and won exemptions for their products. Thus, the agreements frequently excluded or gave only minimal attention to tariffs on clothes, shoes, a small range of foods, and other light manufactured products. The 48-percent tariff on cheap sneakers, for example, remains in effect because of Eisenhower-era lobbying by the shoe industry. The tariff remains, long after the industry itself has gone. Cheap cotton T-shirts, likewise, retain a 19.5-percent tariff, and acrylic sweaters have a 32-percent rate.

The outcome of such a system is easy to predict. At home, people who buy lots of cheap clothes will feel its effects in their budgets, and

companies that buy lots of semiconductor chips will not. Overseas, countries that make cars and computers, or pump oil, will encounter few tariffs. This is why Japan, Norway, and Saudi Arabia are at the low end of the table. But countries where sweater sewing and bed-sheet weaving are the main industries will get hit hard. This is why Cambodia and Pakistan, whose principal industries are textiles, are at the top.

## **2. Success of Regional Trade Agreements**

Second, the United States has made special efforts to help poor countries in some parts of the world—on valid grounds ranging from national security, to drug eradication, to humanitarian concern—but not in others.

Three regional programs are especially important. One is the AGOA of 2000, which exempts 37 sub-Saharan countries from tariffs in order to spark some investment and growth in the continent. The CBI and the ATPA, designed respectively to ease social conditions in Central America during the wars of the 1980s and provide alternatives to cocaine production, do the same for 28 countries in Latin America and the Caribbean. These programs have limitations, but all attempt to eliminate tariffs on clothes and some farm products. This is why, as the table shows, the treatment of countries like Ghana, Haiti, Colombia, and Honduras can be comparable to the treatment of wealthier states.

No such effort has been made for Asia or the Muslim world. It is true that countries in these regions can participate in the Generalized System of Preferences (GSP). Established in 1974, this excuses about 140 beneficiary countries from tariffs on about 3,000 types of products, and allow 40 "least-developed" countries to take advantage of almost 2,000 more. But unlike the three regional programs, the GSP excludes clothes, leather products such as belts and wallets, shoes, and other simple, labor-intensive products.

Despite these limitations, the GSP can be quite helpful for middle-income countries that produce relatively sophisticated products. Russia, for example, is exempt from 15-percent tariffs on caviar and titanium, Thailand from 4-percent tariffs

**U.S. Tariffs on Top 100 Goods<sup>2</sup> Imported  
From World and Selected Trading Partners, 2003**

	<b>Top 100 Products as % of Total Imports</b>	<b>Duty-Free Products</b>	<b>Low-Tariff Goods (&lt; 4.9%)</b>	<b>Medium- Tariff Goods (5% - 15%)</b>	<b>High-Tariff Goods (&gt; 15%)</b>
Cambodia <sup>3</sup>	98.5%	5	1	42	52
Bangladesh <sup>4</sup>	96%	6	5	48	41
Mongolia <sup>5</sup>	99.5%	9	9	43	39
Pakistan <sup>6</sup>	87%	11	6	66	17
Vietnam	89%	21	7	29	43
Sri Lanka <sup>7</sup>	88%	21	9	31	39
Uzbekistan <sup>8</sup>	99.9%	25	5	40	30
Oman <sup>9</sup>	99.8%	30	8	31	31
Nepal <sup>10</sup>	98.5%	30	10	36	24
Syria	99%	35	17	22	26
Egypt <sup>11</sup>	94%	37	17	31	15
Bulgaria <sup>12</sup>	85%	44	12	22	22
Turkey <sup>13</sup>	76%	49	9	27	15
Morocco <sup>14</sup>	98%	53	11	17	19
Indonesia <sup>15</sup>	70%	54	11	14	19
India <sup>16</sup>	70%	48	15	25	12
Philippines <sup>17</sup>	82%	52	10	15	23
Fiji <sup>18</sup>	99.7%	57	5	16	22
Pacific Islands <sup>19</sup>	97.5%	58	7	19	16
Mali <sup>20</sup>	99.9%	51	10	32	7
Armenia <sup>21</sup>	99%	56	9	24	11
Thailand <sup>22</sup>	69%	64	8	16	12
Latvia <sup>23</sup>	96%	63	10	17	10
Afghanistan	100%	30	16	13	0
Albania <sup>24</sup>	100%	35	6	8	3
Italy	53%	40	34	19	7
Korea	77%	52	23	21	4
China	52%	56	20	20	4
Honduras <sup>25</sup>	97%	58	18	20	4
Colombia <sup>26</sup>	93%	66	12	13	9

Haiti <sup>27</sup>	99%	72	7	13	8
Brazil <sup>28</sup>	76%	64	18	15	3
Jamaica <sup>29</sup>	99%	75	8	8	9
Madagascar <sup>30</sup>	99.7%	77	6	8	9
Taiwan	63%	56	29	9	6
Argentina <sup>31</sup>	85%	64	23	5	8
<b>World<sup>32</sup></b>	<b>51%</b>	<b>63</b>	<b>24</b>	<b>8</b>	<b>5</b>
Russia <sup>33</sup>	93%	78	9	5	8
Costa Rica <sup>34</sup>	92%	76	9	13	2
New Zealand	86%	50	34	12	4
Ethiopia <sup>35</sup>	100%	76	8	6	3
Malaysia	87%	75	14	4	7
France	69%	60	27	12	1
Australia	81%	63	28	4	5
Ireland	97%	68	15	17	0
Netherlands	70%	58	26	15	1
Singapore	93%	71	15	10	4
EU Total <sup>36</sup>	56%	65	24	11	0
Caribbean Islands <sup>37</sup>	97%	85	6	5	4
South Africa <sup>38</sup>	87%	83	7	9	1
U.K.	69%	69	23	7	1
Lesotho <sup>39</sup>	100%	64	7	3	2
Papua New Guinea <sup>40</sup>	100%	24	3	2	0
Japan	69%	57	37	6	0
Saudi Arabia	99%	69	22	9	0
Czech Republic <sup>41</sup>	68%	75	25	5	0
Barbados <sup>42</sup>	99.9%	78	19	1	2
Uganda <sup>43</sup>	100%	71	1	2	1
Norway	91%	77	17	6	0
Germany	62%	60	38	2	0
Ghana <sup>44</sup>	99%	93	4	2	1

SOURCE: Tariff and Import Data for 2003, International Trade Commission.

on felt-tipped pens, and Bulgaria from 5-percent tariffs on chandeliers. But countries like Cambodia and Nepal make few such goods. So in practice, the GSP system covers only two of the top 100 imports from Cambodia and Bangladesh, four of the top 100 from Mongolia, and five from Pakistan. These limited exceptions are usually minor products—Pakistan’s GSP privileges, for example, are not on leading exports like high-quality household linen, but on curiosities such as swords and toenail clippers.

## Conclusion

In light of this summary, the conclusions seem obvious: At age 75, the tariff system is unfair, and barely relevant to U.S. employment or international competition. In policy terms, three other points are worth noting.

First, tariffs on places like Cambodia and Nepal are permanent and normal policies. In sharp contrast to more transient debates, such as the recent one about steel policy, they will remain in place permanently, unless a deliberate decision is made to change them through an international trade agreement or a domestic bill.

Second, tariffs can be easily changed. The countries most affected, roughly speaking, are five low-income Asian states and approximately 10 Muslim countries. They are relatively minor trading partners, supplying at most 2 percent of America’s \$1.5 trillion in imports. Dropping the tariffs on their goods would thus make little difference for U.S. government revenues, and would be unlikely to affect production or employment in the United States in any noticeable way. The main effect would be to divert a fraction of garment exports from China and India to Cambodia, Nepal, Mongolia, and the Muslim world.

## Endnotes

<sup>1</sup> See Gresser, Ed, “Toughest on the Poor: Tariffs, Taxes and the Single Mom,” Progressive Policy Institute, September 2002, <http://www.ppionline.org>.

<sup>2</sup> HTS classification, 8-digit level, full-year 2003.

<sup>3</sup> Cambodia: includes GSP duty-free privileges on two jewelry items with tariffs of 5.5% each.

<sup>4</sup> Bangladesh: includes GSP duty-free privileges on two items with low tariffs (golf equipment and plastic packing.)

Third, reform can have rapid effects. The case of Jordan—the beneficiary of a unilateral tariff exemption since 1998 and a free trade agreement since 2001 is illustrative. Jordan’s exports to the United States have jumped from \$16 million in 1998 to nearly \$1 billion in 2004, helping to create approximately 40,000 jobs and sustain the national economy during a period in which the Palestinian intifada and the Iraq crisis drove tourism and other traditional sectors to near-collapse.

The WTO’s Doha Round is ultimately the best forum for addressing these problems, and the United States’ existing proposal for a global elimination of manufacturing tariffs—by not only wealthy countries, but also by large and advanced developing countries—is the right approach. But that initiative’s prospects are complicated, since tariff reform through the Doha Round is inextricably tied to agricultural subsidy cuts, services trade policy, and other difficult issues. And even if the Doha Round succeeds in 2005 or 2006, it will not be fully implemented for another decade.

There is a very strong case for a more limited step now. Sens. Baucus and McCain proposed precisely such a step in 2003, through their “Greater Middle East Engagement Act,” which would have eliminated tariffs on reforming Muslim-world nations. Sen. Dianne Feinstein (D-Calif.) proposed something similar for Nepal, and the Cambodian trade ministry has developed a legislative proposal that would serve the general need of the least-developed Asian and Pacific Island states.

One thing is necessary to finish the job, and place Herbert Hoover’s last legacy in the history books with Prohibition, the stock market crash, and the other colorful events of the Roaring 20s—that is an administration willing to lend a hand and reform the U.S. tariff system.

- <sup>5</sup> Mongolia: includes GSP duty-free privileges on two items with low tariffs (plastic packing and tungsten).
- <sup>6</sup> Pakistan: includes GSP duty-free privileges on four low-tariff items and one medium-tariff item (flags).
- <sup>7</sup> Sri Lanka: includes GSP duty-free privileges on three low-tariff goods and two medium-tariff goods.
- <sup>8</sup> Uzbekistan: includes GSP duty-free privileges on four low-tariff goods and one medium-tariff good.
- <sup>9</sup> Oman: includes GSP duty-free privileges on four low-tariff and five medium-tariff items.
- <sup>10</sup> Nepal: includes GSP duty-free privileges on two low-tariff and five medium-tariff items.
- <sup>11</sup> Egypt: includes: GSP duty-free privileges on seven low-tariff goods.
- <sup>12</sup> Bulgaria: includes GSP duty-free privileges on six low-tariff, three medium-tariff and one high-tariff good (caviar).
- <sup>13</sup> Turkey: includes GSP duty-free privileges on 12 low-tariff and six medium-tariff goods.
- <sup>14</sup> Morocco: includes GSP duty-free privileges on eight low-tariff and five medium-tariff goods.
- <sup>15</sup> Indonesia: includes GSP duty-free privileges on eight low-tariff and four medium-tariff goods.
- <sup>16</sup> India: includes GSP duty-free privileges on 7 low-tariff and 8 medium-tariff products.
- <sup>17</sup> The Philippines: include GSP duty-free privileges on 7 low-tariff and one medium-tariff good.
- <sup>18</sup> Fiji: includes GSP privileges on 11 low-tariff, 5 medium-tariff and one high-tariff good (fruit juice.)
- <sup>19</sup> The Pacific islands include Papua New Guinea, Fiji, Tonga, Samoa, Tuvalu, East Timor, Kiribati, Vanuatu, Micronesia, Palau and the Marshall Islands. As a group they receive GSP duty-free privileges on five low-tariff goods and two medium-tariff goods.
- <sup>20</sup> Mali: includes GSP/AGOA duty-free privileges on 7 low-tariff and 7 medium-tariff goods.
- <sup>21</sup> Armenia: includes GSP duty-free privileges on 13 low-tariff, 13 medium-tariff and one high-tariff good.
- <sup>22</sup> Thailand: includes GSP duty-free privileges on 8 low-tariff and 4 medium-tariff goods.
- <sup>23</sup> Latvia: includes GSP duty-free privileges on 14 low-tariff, 4 medium-tariff and one high-tariff good (titanium).
- <sup>24</sup> Albania: includes GSP duty-free privileges on 5 low-tariff and one medium-tariff good.
- <sup>25</sup> Honduras: includes partial CBI tariff elimination on 11 high-tariff and 7 medium-tariff goods, plus full CBI and GSP duty-free privileges on 11 low-tariff, 10 medium-tariff and 13 high-tariff goods.
- <sup>26</sup> Colombia: includes GSP and ATPA duty-free privileges on five low-tariff, 13 medium-tariff and 5 high-tariff goods, plus partial duty-free on one medium-tariff and six high-tariff goods
- <sup>27</sup> Haiti: includes GSP and CBI duty-free privileges on 8 low-tariff, 7 medium-tariff and 31 high-tariff goods, plus partial privileges on five high-tariff and two medium-tariff goods.
- <sup>28</sup> Brazil: includes GSP duty-free privileges on 13 low-tariff goods and 3 medium-tariff goods.
- <sup>29</sup> Jamaica: includes CBI duty-free privileges on 11 low-tariff, 17 medium-tariff and 13 high-tariff goods.
- <sup>30</sup> Madagascar: includes GSP/AGOA duty-free privileges on 2 low-tariff, 23 medium-tariff and 30 high-tariff goods.
- <sup>31</sup> Argentina: includes GSP duty-free privileges on 11 low-tariff and five medium-tariff goods, and partial privileges on one high-tariff good (cheese.)
- <sup>32</sup> NAFTA eliminates 25% tariffs on two varieties of trucks, imported largely from Canada.
- <sup>33</sup> Russia: includes GSP duty-free privileges on 8 low-tariff, 2 medium-tariff and one high-tariff good (titanium.)
- <sup>34</sup> Costa Rica: includes CBI and GSP duty-free privileges on 23 low-tariff, 8 medium-tariff and 11 high-tariff goods, plus reduction on three high-tariff and two medium-tariff goods.
- <sup>35</sup> Ethiopia: includes GSP & AGOA duty-free privileges on 22 low-tariff, 6 medium-tariff and 11 high-tariff goods.
- <sup>36</sup> The EU reference in this context refers to the total imports from the 15 European Union members in 2003. These include Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, the Netherlands, Portugal, Spain, Sweden, and the United Kingdom.
- <sup>37</sup> Caribbean includes Antigua, Anguilla, Bahamas, Barbados, Belize, British Virgin Islands, Cayman Islands, Dominica, Grenada, Guyana, Haiti, Jamaica, Montserrat, St. Kitts, St. Lucia, St. Vincent, Suriname, Trinidad & Tobago, and Turks & Caicos. The Caribbean islands taken together receive duty-free privileges on 14 low-tariff goods, 11 medium-tariff goods and 16 high-tariff goods through the Caribbean Basin Initiative.
- <sup>38</sup> South Africa: includes GSP and AGO duty-free privileges on 22 low-tariff, 6 medium-tariff and one high-tariff good, plus reduction on five high-tariff goods.
- <sup>39</sup> Lesotho: includes GSP & AGOA duty-free privileges on 1 low-tariff, 23 medium-tariff and 37 high-tariff goods.
- <sup>40</sup> Papua New Guinea: includes GSP duty-free privileges on 4 low-tariff goods.
- <sup>41</sup> Czech Republic: includes GSP duty-free privileges on six medium-tariff and 12 low-tariff goods.
- <sup>42</sup> Barbados: includes GSP & CBI duty-free privileges on 10 low-tariff, 5 medium-tariff and one high-tariff goods.
- <sup>43</sup> Uganda: includes GSP & AGOA duty-free privileges on 7 low-tariff, 6 medium-tariff and 13 high-tariff goods.
- <sup>44</sup> Ghana: includes GSP & AGOA duty-free privileges on 11 low-tariff, 21 medium-tariff and one high-tariff good.