

## *The Economy in Perspective*

*Beyond Baghdad*...As this is being written, coalition forces have just entered Baghdad, and with surprising ease. Many unknowns remain regarding this war, including its duration, intensity, and conventionality. Many unknowns also remain concerning the political evolution of Iraq and the entire region surrounding it in the war's aftermath. The specifics of this evolution will change people's lives in a multitude of ways, not only for everyone in the region, but for millions more around the world. Yet, vital as these unfolding developments are today, they probably will contribute only fractionally to the economic future of the United States.

Our nation has become rich by using its resources productively. Some eras have certainly been more productive than others, but over the long haul, living standards have risen dramatically. Many factors have combined to yield this result, but the decisive one has been respect for democratic capitalism and all that it entails. Capitalism has its downside, but it has demonstrated its ability to "deliver the goods," literally and metaphorically. People who live within democratic political structures and capitalist economic systems have considerable freedom to save, invest, and trade. In particular, effective systems of property rights give people confidence that their future wealth will be tied to their current efforts.

Capitalism has proven its ability generate wealth so convincingly that many formerly noncapitalist economies have converted to capitalism or are in the process of doing so. Democratic capitalist societies achieve peak performance when transactions take place in competitive markets. The larger, more numerous, and more competitive the markets are, the greater the mutual gains from exchange should be.

Expansion of world capital and trade flows signifies a global pattern of resource reallocation that enhances the welfare of the trading nations. (Yes, there are still too many protective barriers to trade, especially in the agricultural sector, but their existence does not diminish trade's value.) In search of profit, companies throughout the world have been globally rearranging their supply, production, distribution, and support structures. The collective result of these machinations ultimately is to give customers the best values at the lowest possible prices.

The United States has a natural competitive advantage in this global trading order. Despite all of the upheaval that accompanies capitalism, our cultural and political history supports the individual freedom, creativity, and flexibility that nurture the creation of knowledge, innovation, and productivity. If capital inflows to a country are other nations' way of voting for its enterprises and ideas, then the United States remains very highly regarded indeed.

Long after the transformation of the Baghdad regime, the evolution of the world's trading regime will play a major role in the evolution of the U.S. economy. Global trade and capital flows ballooned during the last few decades and had a considerable impact on the U.S. Global trade increased from 20% of world GDP in 1970 to 40% in 2000. Total U.S. exports and imports comprised 10% of the nation's GDP in 1970 and 30% in 2000. Its exports expanded roughly 10% per year in real terms during that period, and the U.S. now accounts for nearly one-third of all global trade.

Given the magnitudes involved, it is easy to see that trade activity supports significant amounts of employment and investment within the United States itself. It is also apparent that many developing nations, often those with large populations and abundant natural resources, have the potential to increase their own living standards through international trade.

Progress in international trade does not come easily, principally because present concessions must be weighed against hazy future gains. Yet considering how poverty and hopelessness can breed resentment and militancy, the world's wealthiest nations surely have strong incentives to foster more open and vigorous global trading than has been achieved to date. In the second volume of his famous *Democracy in America*, published in 1840, the social philosopher Alexis de Tocqueville wrote:

Trade is the natural enemy of all violent passions. Trade loves moderation, delights in compromise, and is most careful to avoid anger. It is patient, supple, and insinuating, only resorting to extreme measures in cases of absolute necessity. Trade makes men independent of one another and gives them a high idea of their personal importance: it leads them to want to manage their own affairs and teaches them to succeed therein. Hence it makes them inclined to liberty but disinclined to revolution.