International trade is nothing but a form of technology. The fact that there is a place called Japan, with people and factories, is quite irrelevant to Americans’ well-being. To analyze trade policies, we might as well assume that Japan is a giant machine with mysterious inner workings that convert wheat into cars.

Any policy designed to favor the first American technology over the second is a policy designed to favor American auto producers in Detroit over American auto producers in Iowa. A tax or a ban on “imported” automobiles is a tax or a ban on Iowa-grown automobiles. If you protect Detroit carmakers from competition, then you must damage Iowa farmers, because Iowa farmers are the competition.

The task of producing a given fleet of cars can be allocated between Detroit and Iowa in a variety of ways. A competitive price system selects that allocation that minimizes the total production cost. It would be unnecessarily expensive to manufacture all cars in Detroit, unnecessarily expensive to grow all cars in Iowa, and unnecessarily expensive to use the two production processes in anything other than the natural ratio that emerges as a result of competition.

That means that protection for Detroit does more than just transfer income from farmers to autoworkers. It also raises the total cost of providing Americans with a given number of automobiles. The efficiency loss comes with no offsetting gain; it impoverishes the nation as a whole.

There is much talk about improving the efficiency of American car manufacturing. When you have two ways to make a car, the

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* This assertion is true, but not obvious. Individual producers care about their individual profits, not about economywide costs. It is something of a miracle that individual selfish decisions must lead to a collectively efficient outcome. In my chapter “Why Prices Are Good,” I indicated how economists know that this miracle occurs. In the present chapter I will pursue its consequences.
road to efficiency is to use both in optimal proportions. The last thing you should want to do is to artificially hobble one of your production technologies. It is sheer superstition to think that an Iowa-grown Prius is any less “American” than a Detroit-built Volt. Policies rooted in superstition do not frequently bear efficient fruit.

In 1817 David Ricardo—the first economist to think with the precision, though not the language, of pure mathematics—laid the foundation for all future thought about international trade. In the intervening 150 years his theory has been much elaborated but its foundations remain as firmly established as anything in economics. Trade theory predicts, first, that if you protect American producers in one industry from foreign competition, then you must damage American producers in other industries. It predicts, second, that if you protect American producers in one industry from foreign competition, there must be a net loss in economic efficiency. Ordinarily textbooks establish these propositions through graphs, equations, and intricate reasoning. The little story that I learned from David Friedman makes the same propositions blindingly obvious with a single compelling metaphor. That is economics at its best.