

The Dynamics of International Intervention: Entrepreneurial Discovery & the Market Process

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Abstract

While optimal tariff calculations can show the possibility for large nations to increase national income via protectionist policies, they do not tell the whole story. In this paper, I extend the dynamics of intervention to analyze the impact of tariffs on the entrepreneurial market process. I propose that the unintended consequences of using trade policy to bolster a nation's economy will inevitably prevent an economy from allocating its resources to their highest-valued use. Even if a government manages to improve the terms of trade or protect an infant or favored industry, the disruption of the market process will prevent an efficient allocation of resources. First, government intervention inhibits and alters the course of entrepreneurial discovery distorting the market's allocation of scarce resources to their highest-valued use. Second, the incentives of market participants are changed, discoordinating market and government systems and producing unintended negative consequences such as rising input costs, increasing substitution for the protected good, and proliferation of lobbying. Derailed discovery and unintended negative consequences force decision-makers to either expand the interventionist policy or repeal the intervention and move toward freer trade. I illustrate the theory with two historical trade wars: The Chicken War, 1963, and the US-Canada softwood lumber disputes, 1982-Present.

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“Thus the direct use of the theory (optimal tariff) is likely to be small. But it is to be feared that its abuse will be considerable. It affords to unscrupulous advocates of vulgar Protection a peculiarly specious pretext for introducing the thin edge of a fiscal wedge.” (Edgeworth 1908: 555)

“The point is that the free-market economy forms a kind of natural *order*, so that any interventionary disruption creates not only disorder but the necessity for repeal or for cumulative disorder in attempting to combat it.” (Rothbard [1970] 2006: 322)

1 Introduction

Twenty-first-century populist rhetoric strongly opposes globalization. In the 2010s, populist leaders instigated a proliferation of trade barriers. For example, President Trump imposed steel and aluminum tariffs in March 2018. The 25 percent steel tariffs led to successive rounds of exemptions, retaliation, and increased lobbying. Yet, these barriers continually fail to achieve the objective of rebuilding the steel industry. As recently as January 24, 2020, President Trump imposed tariffs on an additional \$450 million of steel and aluminum imports (Proclamation 2020). As trade barriers proliferate worldwide, it is essential to understand their impact on the market process. Contrary to the commercial policy of these populist leaders, classical economists argued that unilateral free trade is efficient² regardless of the policy of foreign nations (Bhagwati 1988).

No matter the purpose of a trade barrier, it will disrupt the market process and distort price signals. Entrepreneurs, the driving force of the market (Mises [1949] 1998; Kirzner 1973), use tacit knowledge and price signals to seek profit opportunities. They innovate and adjust prices to compete with other entrepreneurs within that market. Limiting the geographic confines of the market will restrict competitive pressure and distort the entrepreneur’s primary tool for calculation: prices. If foreign steel companies must pay an entry fee (tariff) to participate in the

² Efficiency refers to production at the lowest opportunity cost and consumption at the highest possible indifference curve where exchange allocates resources to their most valued use.

American market, their prices no longer accurately communicate their opportunity costs. There is a buffer that enables American companies to be less efficient than their foreign competition and profit. Likewise, the altered prices and diminished competition reduce the urgency to innovate. It follows that a protected market will be more inefficient and less diverse than a barrier-free market. This paper develops and illustrates a theory of the dynamics of international intervention and rent seeking to explore how trade barriers lead to a breakdown of the market process, a misallocation of resources, and the failure of the initial policy.

My analysis of trade wars and protection draws out the intersection of the trade policy, the dynamics of intervention (DOI), and rent-seeking literature. The trade policy literature is vast, beginning with Adam Smith's ([1776] 1981) *Wealth of Nations* and extending to present-day work by Krugman (1980), Feenstra (1994), Bhagwati (2007), Irwin (2017), and Panagariya (2019). Going back as far as Torrens and Mill, economists have argued that manipulating a country's terms of trade through trade policy could improve a nation's well-being (Irwin 1996: 101-115). Harry Johnson's (1950-51, 1953-54) seminal work in trade policy derived a formula for an optimal tariff and showed it was possible to emerge better off from retaliation. Subsequently, a vast terms-of-trade (optimal tariff) literature built on Johnson's foundation.

Hamilton and Whalley (1983) calculate the optimal tariff with and without retaliation to show tariff levels of the early 1980s were far from optimal, leaving room to retaliate. Markusen and Wagle (1989) determined the calculations of Hamilton and Whalley (1983) were too high and show empirically that smaller countries have lower optimal tariffs. Following Bagwell and Staiger's (1999) use of a terms-of-trade model to evaluate the foundational principles of the General Agreement on Tariffs and Trade (GATT), literature developed exploring the impact of trade agreements on the terms-of-trade externality (e.g., Broda, Limão, Weinstein 2008; Ludema

and Mayda 2013). Similarly, Ossa (2014) presents estimates of optimal, Nash, and cooperative tariffs. He shows that retaliation is costly, and efficient trade negotiations produce significant gains. Finally, through comparative advantage analysis, Costinot, Donaldson, Vogel, and Wening (2015) conclude that an optimal tariff policy would increase US gains 20 percent in agriculture and 33 percent in manufacturing over a laissez-faire policy.

Here, I do not contest this *possibility* of improving the terms of trade but assert that the optimal trade policy literature makes assumptions about government actors that render its real-world use impossible. Namely, it assumes that bureaucrats are benevolent, intending to maximize the *nation's* wealth, and have the knowledge required to achieve this end.

The DOI maintains the assumption of benevolence but argues that government actors lack the requisite knowledge to intervene in the economy effectively. It began with Mises's (1929) insight that interventionism leads to inconsistencies in an economy that will, at minimum, preclude the achievement of the intervention's goal, and in the limit lead to a series of crises that push an economy to central planning. Rothbard ([1970] 2006) developed a typology of intervention and extended Mises' primary thesis. Lavoie (1982, 1985) addressed the so-called "Misesian Gap."³ Kirzner (1985) elucidated intervention's impact on entrepreneurial discovery, and Ikeda (1997) developed the dynamic process thoroughly. Finally, in an essay honoring Don Lavoie, Bradley (2006) consolidated a typology of the dynamics of intervention.⁴

Building upon the work of Kirzner and Ikeda, I argue that trade barriers distort entrepreneurial action, lead to undesirable outcomes, and force the government to intervene

³The Misesian Gap refers to the non-existence of a middle way. Mises showed that price controls could not "fix" an economy, but this does not prove there is no middle way. See Lavoie (1982, 1985) for elucidation of this debate.

⁴ Bradley's typology addresses the step-by-step process of intervention. In contrast, Rothbard's classification describes three relationships between the government and market participants.

further to salvage the economy and achieve its goal. Due to the entrepreneur's pursuit of profit, government attempts to improve a nation's economy with trade policy will lead to new and diverse unanticipated profit opportunities, which may or may not align with the intervention's goal. A lack of knowledge prevents successful policy, which creates a bureaucratic demand for information. This demand creates political profit opportunities (rent-seeking) that are an entrepreneurial distortion not directly addressed by the DOI due to the assumption of benevolence.⁵ "Suppose that, instead of discovering a new commodity or service or production process, an innovating entrepreneur discovers a way to convince the government that he "deserves" to be granted a monopoly right" (Buchanan 1980: 7). When this is possible, entrepreneurs will capitalize on it and compromise the government actor's benevolence. Thus, I include an analysis of rent-seeking motivated by trade policy.⁶

In the next section, I build a theory of international intervention to explore the impact of trade policy on the market process. After presenting my approach, in section three, I illustrate it with two trade wars: The Chicken War of 1963 and the US-Canada softwood lumber disputes from 1982-Present. I chose these cases due to their diverse contexts and to illustrate, not prove the theory. First, The Chicken War was a brief skirmish between allies resolved by a General Agreement on Tariffs and Trade (GATT) panel. The resolution approved US retaliation and the EEC did not repeal its tariff. This outcome has shaped global markets for the last 58 years and illustrates the power of trade policy to shape markets. Second, the ongoing 39-year Softwood

⁵ I follow Benson (2002), Ikeda (2005), Boettke, Leeson, and Coyne (2007), and Candela and Geloso (2020) in the evolving Austrian Political Economy (APE) that recognizes that relaxing the benevolence assumption does not destroy methodological integrity (Ikeda 2005). The critical assumption of APE is structural ignorance (Boettke, Leeson, and Coyne 2007).

⁶ The influence of special interest groups on the formation of trade policy has been addressed by Tullock (1967), Krueger (1974), Pincus (1975), Lagadec (2014), Kaempfer et al. (2004), and Grossman and Helpman (1992). In a comprehensive review of the antidumping literature, Blonigen and Prusa (2001) detail the political origin and market ramifications of antidumping policy but do not address entrepreneurial discovery.

Lumber Dispute between Canada and the United States illustrates primarily the proliferation of rent seeking necessary to maintain protection. It also demonstrates trade policy's inability to provide a viable, long-run solution to Canadian subsidies. I conclude with an evaluation of the theory considering the empirical cases.

2 Toward A Theory of The Dynamics of International Intervention

2.1 The Unhampered Market and Dynamics of Intervention

We make four assumptions to establish the unhampered market (Mises [1949] 1998). First, there is a division of labor and private property necessitating market exchange. Second, no exogenous force attempts to manipulate prices. Third, the government prevents intrusions in the market process. Fourth, one takes action to improve one's life. Transactions only occur when actors believe the benefits outweigh the cost. The sale of a car from X to Y for \$2000 indicates that Y values the vehicle more than \$2000, and X less than \$2000. The exchange moves the car to a more highly valued use.

If X and Y are unaware of each other, no exchange occurs, both are worse off, and efficient allocation does not obtain. Improving resource allocation requires an alert profit-seeking entrepreneur, E (Kirzner 1973). E , aware of society's diverse valuations, earns profits by reallocating resources to higher-valued uses (from X to Y). E 's profits will dissipate as others enter the used car market, increasing supply and lowering prices. Also, if E fails to judge market valuations correctly, a loss will result. This feedback prevents entrepreneurs from continually allocating resources to lower valued uses. Government intervention (violating assumption 3) disrupts this process, alters incentives, and hinders efficient allocation.

The initial government intervention disrupts discovery and alters actors' incentives, preventing the coordination of market and government systems (Ikeda 1997; 2015). The interaction of these effects produces unintended negative consequences that prevent the intervention from achieving its goal. The government is now at a “nodal point” (Ikeda 1997: 118). It must either intervene further or repeal the intervention (Ikeda 1997). The former causes the cycle to repeat and moves society toward a centrally planned economy, while repeal ends the process and moves society toward laissez-faire capitalism.

Kirzner (1985) details four types of discovery disruption. First, one may intervene to fix a so-called market failure. The government's intervention assumes there is a coordination failure that entrepreneurs will not attempt to profit from. Intervention to correct failure precludes market discovery, and profit opportunities go *undiscovered*. The intervention shifts resource allocation from the economic to the political sphere. Unlike entrepreneurs, bureaucrats and government officials are not residual claimants; thus, they are not profit-motivated. A lack of residual claimants prevents profits and losses, which indicates whether resource allocation has improved. Moreover, they cannot know in advance what the market will discover. Thus, interveners cannot engage in the discovery process; it is *unsimulated*. Intervention that erects barriers to entry diminishes competition and will *stifle* the rivalrous discovery process (Hayek 2002). Potential discovery is limited to entrepreneurs currently within the borders or those willing to scale them. Due to their counterfactual nature, it is impossible to know the degree to which artificial barriers to entry stifle discovery. Finally, because solving the coordination problem produces profits, and it is unlikely that intervention will approach perfect coordination, intervention creates alternative, *superfluous* profit opportunities. Intervention blocks existing profit opportunities, which redirects entrepreneurial discovery to new possibilities not necessarily desired or known to political

actors. Entrepreneurs typically will not comply with an intervention but attempt to innovate around the intervention, capture profits, and render it moot.

Political actors and bureaucrats lack the relevant information to allocate resources because they cannot simulate the discovery process. Intervention and the prospect of future intervention create a demand for data filled by rent-seeking, special interest groups. Intervention is driven not by perceived market-generated profit opportunities or benevolent bureaucrats attempting to maximize society's wealth but through special interest groups who recognize potential profit through government intervention. This unproductive entrepreneurship (Baumol 1990) benefits special interests by using society's scarce resources on political influence that fails to efficiently allocate resources.

2.2 The Dynamics of International Intervention

A global market has the same fundamentals as the above market with greater competition, economies of scale, and product variety. The essential market process, moving resources from lower to higher-valued uses, is still at work. Similarly, intervention into the unhampered international market will produce a dynamic process.

2.2.1 The Dynamic Process

International intervention through trade policy disrupts the discovery process, leading to unintended consequences that force the government to either repeal the policy or intervene further. Suppose Domestic's industry H receives protection from foreign rival F through trade policy (e.g., tariffs, quotas, etc.). Initially, H will experience a revival of good fortune as they no longer compete with F . Though the goal is to enable H to compete with F eventually, it lacks an immediate incentive to discover new profit opportunities through innovation. H 's current profit opportunities lie in continued protection rather than innovation. Thus, H relies on continuous

protection from foreign rivals, not innovation, to compete with them. Suppose F perceives large profit opportunities in Domestic. In that case, F will invest resources in circumnavigating the trade barrier, reapplying pressure to H . Domestic's government will have to either give up on protection or intervene a new. Further, if F 's government retaliates with trade barriers on Domestic's industry I , Domestic will be forced to intervene domestically to support I and internationally to combat F .

2.2.2 Undiscovered Discovery

When a contemporary protectionist policy, such as voluntary export restraints, is ratified, the government is attempting, intentionally or not, to protect the current market structure. Formerly successful firms believe they are entitled to their current market share and deserve protection from new foreign competition. Infant industries argue that if given time to move along the learning curve and drive down costs, they will be able to compete internationally. In both cases, the competition from foreign producers jeopardizes the ability of domestic producers to make a profit under the *current market conditions*. When trade policy limits foreign competition, domestic producers do not have the same urgency to anticipate the future state of the market. Entrepreneurial discovery is forward-looking, struggling to earn future profits. Trade policy is backward-looking; countries seek to make their current endowment successful in today's market. Because of this backward-looking stance, the attempt to fix a perceived market failure with government intervention precludes entrepreneurial discovery. When discovery is discouraged in this manner, so also is economic growth. Though an isolated industry may benefit, consumers everywhere pay more for goods and services, and efficiency-improving innovations go undiscovered.

2.2.3 Unsimulated Discovery

Let us now assume that undiscovered profit opportunities exist not from government intervention but because the market failed to discover the best allocation of resources. In this case, we ask how the government recognized the market's failure and determined the best use of society's scarce resources? It used political, not economic, mechanisms. The government cannot reason economically since government officials cannot capture pecuniary profit (Kirzner 1985: 140). When the government uses trade policy to protect domestic industries, it cannot discern the actual cost because the entrepreneurial discovery process is unsimulated. The market solves the knowledge problem through entrepreneurial discovery and economic calculation (Hayek 1945; Kirzner 1973). However, bureaucrats who face the same knowledge problem cannot use these tools because trade policy is void of the discovery process.⁷ As stated, its policy is predicated on current and past circumstances and looks to prolong those conditions which diminishes economic growth. On the other hand, entrepreneurs capture profit opportunities when they are alert to an inefficiency in the current market and discover a future solution that improves resource allocation.

2.2.4 Stifled Discovery

Not only does protection leave profit opportunities undiscovered, but it also stifles potential competitors from entering the market. Trade barriers impose higher transaction costs on foreigners which limits their ability and desire to compete, stifling their entrepreneurial skills. As entrepreneurial discovery begets more and new avenues for entrepreneurship (Holcombe 1998), the stifling of foreigners will also slow, or even stop, the virtuous circle of entrepreneurship in

⁷ For more on the inability of government actors to calculate, see Mises (1920), Hayek (1948: Ch. 1-3), and Lavoie (1985)

the protected industry. Moreover, the intervention stifles entrepreneurs' specialization across borders, limiting potential economies of scale and a global division of labor. Alternatively, in a world without trade barriers, economic actors will specialize in their global comparative advantage. If a US automobile manufacturer cannot compete with foreign competitors, the assembly may move overseas, allowing the foreign firms to take advantage of economies of scale. Entrepreneurs then redistribute the now unemployed US factors of production to more globally efficient uses.⁸ Entrepreneurs capture profits in an agile, minimally regulated economy by reallocating factors to more efficient uses. Protecting the domestic industry from foreign competition hinders this creation of value.

2.2.5 Superfluous Discovery

Wholly superfluous discovery diverts economic resources in search of new profit opportunities under a new trade regime. Companies do not simply accept the higher tariff-induced prices but attempt to innovate around them. First, when Congress levies steel tariffs, domestic steel-using companies find substitutes, lay off workers, and petition the government for exclusions. While these workarounds improve efficiency under the current regime, actors could use entrepreneurial energy more effectively without the trade barrier. The truly efficient use of resources would be to import steel tariff-free. Second, when tariffs target specific goods, importers invest time and resources to have their products classified alternatively, diverting resources away from innovation and product development. Finally, superfluous discovery leads to the failure of protection. Protection creates a quasi-monopoly rent for domestic firms (Rothbard [1970] 2006).

⁸ Of course, the domestic industry need not fold. Through innovative entrepreneurship, domestic actors can discover new areas for profit-making and compete with their foreign rivals.

However, superfluous discovery erodes this rent as entrepreneurs discover new ways to compete with the protected good.⁹

3 Trade War Applications

3.1 The Chicken War 1963¹⁰

3.1.1 Historical Background

In the 1930s, the US chicken industry shifted from individual family farms to massive, technical production. From 1920–60 the industry was transformed by breeding experiments, vertical integration of processing, shifting regional production, and consolidation and expansion of farms.¹¹ Production in 1929 was 34 million broilers¹² and by 1961 was 2.2 billion (Talbot 1978: 3). Yearly per capita consumption quintupled from five to twenty-eight pounds (1945–61). Retail, ready-to-cook prices fell from \$0.595 to \$0.358 per pound (1946–61, non-inflation adjusted).¹³ Surplus supply and the Institute of American Poultry Industries (IAPI) encouraged Congress to ratify Public Law 480, the Agricultural Trade Development and Assistance Act (1954). Under the auspices of P. L. 480, the USDA and IAPI established a West German market. From 1955-1962 the West German market expanded significantly (See Table 1).

⁹ Blonigen and Prusa (2001) provide examples of how companies avoid AD duties. For example, they can shift production to the export's destination, a third country, or adjust pricing during the period of assessment. These are examples of superfluous discovery.

¹⁰ Ross Talbot (1978) wrote the authoritative work on the Chicken War.

¹¹ Farms consolidated from 50,094 to 35,126 (1959–1964); surviving farms tripled production (Talbot 1978: 8).

¹² A broiler is a chicken 8–12 weeks of age and is the primary chicken export (Talbot 1978).

¹³ *The Poultry and Egg Situation*, Bureau of Agricultural Economics, United States Department of Agriculture March 1947 and January 1962.

Table 1: US Shipments of Poultry to West Germany

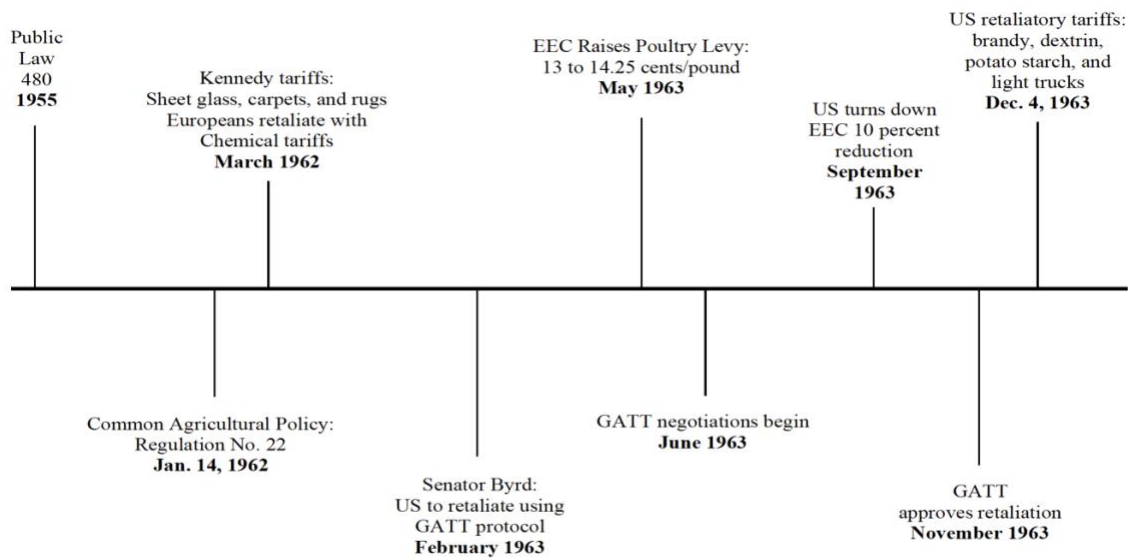
<i>Year</i>	<i>Millions of Pounds</i>
1955	1.2
1956	4.0
1958	7.7
1959	52.0
1960	86.0
1961	137.0
1962	152.0

Source: Talbot (1978: 11)

At the same time, Europe was also evolving economically. In March of 1957, "the Six" (France, West Germany, Italy, the Netherlands, Belgium, and Luxemburg) established the European Economic Community (EEC). A long-run agreement was not possible without the support of the agricultural community. The EEC included the Common Agricultural Policy (CAP) to gain this support. Its Regulation No. 22 sought a progressive establishment of a common poultry market (Talbot 1978: 15). At the time, poultry was a small portion of the EEC's agricultural output (e.g., France's poultry output was 7 percent of its agricultural output). However, Table 1 indicates increasing European poultry consumption (in 1961 rest of the Common Market imported 6 million pounds from the US (Talbot 1978: 36)). European agricultural interests desired to enter the poultry market but could not compete with the mature American industry. To build the Common Market's poultry industry, Regulation No. 22 established multiple prohibitive trade barriers.¹⁴

¹⁴ There were five different protective measures placed on broiler exports to the EEC by No. 22: (1) a "sluice gate price" with a (2) supplementary variable levy dependent on c.i.f. price and gate price difference, (3) an EEC 2 percent ad valorem duty, (4) a member-state ad valorem duty of 10.5 percent and (5) an equalization fee to account for differential feed grain prices (Talbot 1978: 67; see pages 68-69 for an in-depth explanation of each).

Figure 2: Chicken War Timeline



Note: EEC = European Economic Community; GATT = General Agreement on Tariffs and Trade
Source: Talbot (1978)

3.1.2 The Chicken War: from economic to political decision making

The USDA's support of the IAPI through P. L. 480 was the first market intervention. The law enabled W. Germany to pay for surplus American poultry with German marks. Entrepreneurs' energy turned to the German market and American broiler exports grew (Talbot 1978: 54). The IAPI, and other leaders in American poultry, set up the International Trade Development Committee (ITDC) to protect their German investment.

The Chicken War began on January 14, 1962, when the EEC Council of Ministers approved the CAP's Regulation No. 22 effectively banning US chicken imports. President Kennedy retaliated in March of 1962 with tariffs on EEC exports of sheet glass, carpets, and rugs. The EEC responded with tariffs on selected chemicals and chemically treated cloth that impacted \$27 million of US exports to the EEC per year (Talbot 1978: 71). Here we see the power of intervention to cycle into increasing central, rather than market, allocation. Kennedy chose to levy the above tariffs and not others (e.g., baseball gloves and ceramic mosaic). There

was no economic calculation of profit and loss, no market feedback that said American sheet glass had a comparative advantage to baseball gloves. Instead, special interest groups convinced Kennedy that protecting sheet glass was protecting America. Thus, the economy veered away from economic calculation toward political calculation. When the EEC passed Regulation No. 22 into law, it forced a nodal point on the United States. Kennedy chose to intervene more, and in response, so did the Europeans.

Broiler exports to West Germany fell from 5.4 million pounds in January to 3.5 million pounds in August of 1962. Instead of complying with US calls for concession over the next year (until summer of 1963), the EEC alternated raising the overall barrier and making small, unaccepted concessions. In February 1963, Senator Harry Byrd called a special meeting of the Finance committee, which made it clear the US would seek a GATT retaliatory provision. On June 25, 1963, negotiations under the auspice of GATT began. In September of 1963, the US turned down the EEC's offer of a 10 percent reduction in rates and waited for the GATT Panel's advisory opinion.

On November 20, 1963, the GATT Panel determined that the EEC had violated the September 1960 binding (Talbot 1978). The GATT panel assessed injuries at 26 million dollars, far below the US claim of 46 million dollars. The EEC accepted the decision, and on December 4, 1963, the US ratified GATT-approved retaliatory tariffs on tariffs on brandy, lightweight trucks, dextrin, and potato starch. Thus, moving both nations, indeed the world, away from economic to political decision-making.

3.1.3 Entrepreneurial Distortions

The protection of the European Common Market poultry has increased. In 1997 the EU banned imports of chlorinated chicken, completing the ban on United States' chicken imports. While

these restrictions have allowed the EU to develop a competitive poultry industry, it has arguably done this in a manner that has hindered the development of the EU economy. Profit opportunities have gone undiscovered as the European producers have not had to compete with the Americans. As of the summer of 2021, the United States is the world's second-largest exporter of chicken meat, and the EU, though a net exporter, still is the world's fifth-largest *importer* of chicken meat (Mezoughem, 2021). Shutting out the world's second-largest producer of broilers will increase the cost of broilers in the EU. By deciding to fix the market failure of chicken imports in 1963 and 1997 with protective trade barriers, the EEC precluded the market's discovery of a competitive alternative to American chicken. The higher price in Europe incentivizes local entrepreneurs to put resources into poultry production that would have been used elsewhere without the trade barrier. Thus, the trade barriers make it impossible to know the actual value of a European chicken.

Moreover, the trade barriers stifled American entrepreneurs' European discovery, limiting the American market's extent and its economies of scale. Also, US firms had established offices in West Germany from which they held cooking schools, demonstrations, and in-store promotions. They participated in trade and food fair exhibits, market surveys, advertising in newspapers and magazines, in trade papers reaching butchers, chefs, and buyers (Talbot 1978: 54–55). With the 1964 trade barrier came the demise of these entrepreneurial ventures, discouraging German butchers, chefs, and consumers from interacting, learning, and benefiting from American ideas.

Throughout the trade war, both the EEC and the US made decisions about which products to support not through profit and loss calculations but political influences. The use of government regulation to “fix” the market opens society to vast misuse of resources as

businesses use their capital to pursue protection and government assistance instead of innovation. Instead of market discovery and profit-seeking in the European poultry market, there was political rent-seeking. The United States poultry organizations argued for their "historical" (1960) right to a fixed portion of the West German market. The EEC was building a Common Market partially contingent on European agricultural interests gaining protection from non-European competition. The success of these special interests stifled the discovery process and shifted chicken production from efficient American to relatively inefficient European producers.

Superfluous discovery occurs when entrepreneurs innovate around regulations and barriers effectively rendering the protection moot. One clear case of this is the tariff on brandy. While brandy imports valued over \$9 per gallon appear to have drastically reduced from \$11.5 million to \$1.79 million (Talbot 1978: 122), the brandy importers' creative accounting made these numbers dubious. First, to ship at lower costs beginning in 1964, all advertising expenses were excluded from invoices. Second, customs agents generally assumed that any brandy that came in containers larger than one gallon was not worth more than \$9 per gallon and was not subject to the tax. The shipment of large containers grew (Talbot 1978).

Japanese entrepreneur's superfluous discovery demonstrates the complete cycle of the dynamics of intervention. In the 1970s, Japanese truck manufacturers innovated around the 25 percent tariff on light trucks by importing the cab chassis and the bed separately (Ikenson 2003). As the goal of protecting the Big Three was now in jeopardy, the US government faced a nodal point: do they allow entrepreneurial ingenuity to circumnavigate the tariff, or do they intervene further? In 1980, the UAW and Big Three helped answer that question. They successfully lobbied to reclassify a cab chassis as a truck and subject to the 25 percent tariff (Porter 2008).

The light truck tariff is the only of the four retaliatory tariffs that remain. The initial market impact was swift. Volkswagen truck prices rose \$237 per truck (1964 US dollars), and compared to 1963, sales in the first three months of 1964 were nearly cut in half (3,993 to 2,159) (Talbot 1978). Year-over-year, light truck imports from West Germany dropped from \$15 million in 1963 to \$5.7 million in 1964 (Talbot 1978). If the goal here was to protect the US truck market, then the tariff clearly was successful. However, the stated purpose was to gain US companies access to the European poultry market, which they are still denied.

In 2009 Ford, whose F-150 is a great benefactor of the Chicken Tax, found it necessary to innovate around the tariff (superfluous discovery). During the 2008 recession, with gas prices at all-time highs, commercial drivers desired increased gas milage in their vehicles. Since 2002 Ford had manufactured the Transit Connect van whose lightweight narrow frame and high ceiling was the perfect solution. However, it was manufactured in Turkey; importing it would require paying a 25 percent tariff. To avoid this, Ford installed rear seats, seatbelts, and windows so the customs agents would classify it as a passenger vehicle and only charge Ford a 2.5 percent tariff (Dolan September 23, 2009). Upon arrival in Baltimore, MD, Ford removes and recycles the rear seats, seatbelts, and windows to convert the van for commercial use (Dolan September 23, 2009). Ford thus transforms the imported "wagon" into a "commercial van." The Ford Transit Connect clearly demonstrates the unintended long-run consequences of international intervention. In 1963 no one would have foreseen Ford importing trucks from Turkey. One of the companies that lobbied for protection, and benefited the most from it, required superfluous discovery to avoid its consequences.

This light truck tariff impacted world vehicle production. By 2001 US domestic manufacturers had shifted toward truck production. The Big Three produced slightly more than

50 percent of the cars sold in the US, but 86.61 percent of the light trucks (Ikenson 2003). To compete, by 2001, all significant foreign competitors (Toyota, Nissan, Mazda, and Isuzu) manufactured their trucks in the United States. In the same year, of the three million trucks sold in the US, only 6,981 (0.23 percent) were imported (Ikenson 2003). Moreover, the 25 percent tariff has limited American consumers to only six brands of trucks, compared to more than twenty brands of the sedan. The Toyota Hilux, VW Amarok, and the Mercedes X Class, all sell millions outside of the US (Jenkins March 30, 2018).

Is the concentration of truck production within the United States, and lack of variety for the US consumer, the most efficient allocation of resources? While this does improve efficiency, it is a political outcome driven by the current regulatory regime. If Congress repealed the 25 percent tariff, it might be more cost-effective for Toyota to manufacture its trucks in Japan and ship them to the US. However, worldwide truck entrepreneurship has been shaped by the US tariff for over fifty years, and thus we cannot know what free trade production would look like.

3.2 US vs. Canada: The Softwood Lumber Disputes (1983-Present)

3.2.1 The Rationale: Canadian Stumpage Fees

Softwood lumber, primarily used in home construction, has consistently been an essential commodity in the US-Canada trade. From 1958 until the 1980s, the countries traded it freely (Zhang 2007). In 1982, Canada's softwood exports met 30 percent of US demand and comprised 60 percent of Canada's production (Kalt 1988: 340). That year the Coalition for Fair Lumber Imports (CFLI)¹⁵ alleged that the Canadian government's lumber policy was harming US lumber producers (Kalt 1988). They filed a petition to the US Department of Commerce (DOC) and

¹⁵ 350 US forest product companies and the eight major lumber and timber trade associations composed the CFLI (Kalt 1988).

International Trade Commission (ITC), arguing that Canadian non-market “stumpage” fees amounted to a subsidy. Canadian lumber companies harvest trees from governmentally owned land for a government-determined price. On the contrary, in the United States, the land is privately owned, and companies purchase trees through auction. The CFLI argued that the formula-based stumpage fee was below market price, giving Canadian companies an unfair advantage (Kalt 1996). This foundational complaint has not changed.

Figure 3: Lumber Wars Timeline

Lumber I	Lumber II	Lumber III	Free Trade	SLA 1996	Lumber IV	SLA 2006	Lumber V
Outcome: ITC determines no injury from stumpage.	Outcome: MOU 15% Canadian Export tax 1987–91.	Outcome: CVD 6.51% 1992–94		Outcome: Tariff-rate Quota	01-02: CVD and AD 19–31% 02-03: CVD 16.37%; AD 3.78% 03-06: CVD 8.7%; AD 2.1%	Outcome: Export tax range 0–15% or export charge 0–5% plus volume control	17-20: CVD and AD 20% 8/20: WTO rejects 12/20: CVD and AD
1982	1986	1991	1994	1996	2001	2006	2016

Note: ITC = US International Trade Commission; MOU = Memorandum of Understanding; CVD = countervailing duty; SLA = Softwood Lumber Agreement; AD = anti-dumping duty; WTO = World Trade Organization.
Sources: Kalt (1996); Zhang (2007); Softwood (2020); Vieira (2020); Statement (2020).

3.2.2 The Lumber Wars

The lumber wars demonstrate the influence of special interests on the dynamic process of intervention. During Lumber I, the CFLI was formed to consolidate the voices of the lumber industry in the West, South, and Northeast. However, the CFLI's efforts fell short, and the countervailing duty (CVD) investigation in 1983 denied their petition. The ITC found that the Canadian subsidy was generally available and did not violate US trade law, momentarily forestalling the interventionist process (Kalt 1996).¹⁶ Yet, in a US steel case against Brazil, the DOC created a “dominant use” standard. This trade law innovation stated a CVD was justified if

¹⁶ A subsidy must benefit a specific enterprise or industry to violate United States trade law (Kalt 1996).

the “dominant user” of a subsidy was found to injure its US competitors materially (Kalt 1988: 342).

Lumber I maintained free trade; Lumber II would not. The new dominant-use clause and the 1986 senatorial election motivated the CFLI to petition the DOC for a CVD in 1986. In October of 1986, the DOC levied a 14.5 percent CVD. The Canadians retaliated quickly with a 67 percent CVD on US corn. This harsh retaliation led to a memorandum of understanding (MOU) which obligated Canada to remove the corn tariff and impose a 15 percent export tax on softwood lumber. In turn, the US agreed to remove the 14.5 percent CVD (Kalt 1996: 270). The goal of this measure was two-fold. First, the export tariff leveled the playing field. Second, the CFLI preserved American market share.

Between December 1986 and 1991, Canada reformed its stumpage system and removed the export tax in 1991. If the goal of the policy was a reformed stumpage system, then this should have ended of the Lumber Wars. However, in Lumber III the CFLI expanded their complaint to include Canada's Log Export Restraint (LER) and did not accept the stumpage reform. The CFLI argued that the price Canadian sawmills paid for logs was below the world price due to the LER. In 1992 the DOC determined a CVD of 6.51 percent was justifiable based on stumpage and LERs (Log Export Restraint) (Kalt 1996). After several appeals through the new Canada-US Free Trade Agreement (FTA) panel, the CVD was revoked in 1994 (Zhang 2007). Though initially, Lumber III maintained protection, the FTA appeals panel and the 1993 adoption of NAFTA re-established free trade in softwood lumber. The reformed stumpage system and LERs remained indicating failure of the trade policy.

After a brief period of free trade from 1994–95, negotiations in 1995 led to a five-year softwood lumber agreement (SLA) signed in April 1996. SLA 1996 imposed a tariff-rate quota

(TRQ) system on Canada and prohibited further trade actions by the United States. Under this agreement, the US restricted imports from British Columbia, Alberta, Ontario, and Quebec to 14.7 billion board feet annually. If exports rose above this mark, increasing prohibitive tariff rates would apply (Zhang 2007). The SLA gave government control to manage the softwood lumber trade and maintained the desired 70 percent of the US market.

Once the SLA expired, the CFLI commenced Lumber IV, adding antidumping (AD) allegations to the stumpage/LER argument. In May of 2002, the DOC determined that an 18.79 percent CVD and 8.43 percent AD were warranted (Zhang 2007). Over the next four years, Canada and the United States fought through NAFTA Panels, the WTO, and Administrative Review.¹⁷ Lumber IV concluded when SLA 2006 established a new TRQ system, refunded 82.5 percent of CVD and AD duties collected from 2002–06, created a dispute settlement tribunal from the London Court of International Arbitration, and stipulated a seven-year duration with a possible two-year renewal and twelve-month cooling off period (Zhang 2007). In 2016, the Obama administration and the Canadian Minister of International Trade held talks to move toward a new SLA (Statement 2016). Yet, in late November 2016, the CFLI initiated Lumber V (Softwood 2020).

In November 2017, the DOC determined a combined CVD and AD rate of about 20 percent, and in December, the ITC approved this decision (Softwood 2020). In August 2020, the WTO ruled that the US incorrectly calculated these duties since they relied on benchmark prices in one Province for all of Canada instead of regional prices (Vieira 2020). In September, the US

¹⁷ Yearly, foreign, or domestic companies may request a reassessment of CVD or AD determinations from the US government.

promptly appealed this ruling and then issued a final determination of a combined CVD and AD of 8.99 percent (Softwood 2020; Statement 2020).

US companies continue to fight for a market stumpage system in Canada; Canada wants to return to the TRQ system of SLA 1996. Both options maintain the protection of US lumber interests and managed trade, trumping the market process. The repeated DOC investigations demonstrate the failure of trade policy to achieve its goal. Moreover, the addition of LERs and AD complaints reveal the superfluous entrepreneurship of the CFLI. Rather than investing in cost-cutting innovation, lumber invested in discovering new methods of political control. The protective tariff did not create an even playing field, but a consistent percentage of the US market controlled by Canadian exports that continue to benefit from state-subsidized stumpage fees. Trade policy has not satisfactorily changed Canadian stumpage laws, nor has made the US more efficient. Instead, it stifled the market process by politically determining the “best” allocation of scarce resources before the entrepreneur could discover their most valued use.

3.2.3 Entrepreneurial Distortions

Because the softwood lumber market has been kept in stasis by trade policy, the American firms lack incentives to compete directly with the Canadians. Lacking the necessity to compete with foreign firms, American lumber companies only compete with other American companies. Profit opportunities go undiscovered as these firms do not have to compete with the Canadians.

Similarly, the trade barriers limit the amount of profit that Canadian lumber mills can earn in the United States. Even if a Canadian company discovers a way to serve the American customer better than the status quo, it could not capitalize on the discovery. Canadian entrepreneurs are thus led by a visible hand to seek alternate means to earn profits, leaving the American consumer out of their calculations. More profits are available on both sides of the border by lobbying

Washington DC than discovering better ways to harvest trees in Washington or British Columbia. If protection from DC was not an option, how much more advanced would the American lumber industry be today? How much cheaper would housing be?

Because trade barriers are established without market discovery, they lead to an environment where the price does not convey the value of goods and services: American and Canadian lumber sell at a comparable price due to trade barriers, not market valuation. Diminished competition then hampers the market process. Since the TRQ system forces the American consumer to buy a predetermined amount of lumber from US and Canadian companies and the CVD and AD barriers mandate an artificially high price, an accurate valuation is impossible. This fact requires politicians and trade lawyers to rely on experts for information. So, the on-going Lumber War has incentivized American and Canadian companies to develop a highly skilled lobby.

On the American side of the border, the Coalition for Fair Lumber Imports (now known as the US Lumber Coalition (USLC)) is the primary actor. At every interval in the lumber wars the CFLI brought allegations (1986, 1991, 1994–5, 2001, 2006, and 2016). Expenditure on lobbying in 2000 and 2005 demonstrate the importance of trade barriers to these organizations. In 2000 the CFLI spent 2.113 million dollars, and in 2005 they spent 1.39 million dollars on lobbying (Open Secrets 2020).

In 1986 the CFLI won their first battle. There were senate races in Washington, Oregon, Idaho, Georgia, and Alabama. Each of these states had numerous softwood lumber industries, and the CFLI used the elections as a catalyst to get CVD investigations initiated. In Lumber II there was no opposition to the CFLI. The National Association of Home Builders (NAHB) was the only organization that may have contested their claims since its members are the chief

purchasers of softwood lumber. From 2005-2009 in the US, new housing starts fell 74 percent, and consumption of softwood lumber fell 41 percent (Hoover and Fergusson 2018). However, in 1986 the NAHB estimated only a 2 percent increase in housing costs from the CVD, while the 1986 Tax Reform Act would have ended the mortgage interest deduction (Carliner 1996). Therefore, they directed their political power against the Tax Reform Act.

Recently, the NAHB has determined lumber inputs to be a more significant amount of the input costs, consisting of one-fifth to one-sixth of the material costs in a single house. Higher lumber prices because of the CVD and AD will increase the prices of new homes, hurting the members of the NAHB. In 2016 the NAHB formed the American Alliance of Lumber Consumers (AALC) with the National Retail Federation and the National Lumber & Building Materials Dealers Association to lobby for free trade softwood lumber (NAHB 2016). In a letter to the USTR on April 22, 2021, NAHB chair John Fowke (2021) argued that the USTR should not ignore the NAHB members' role in the economy. They construct 80 percent of the new homes in the US with materials sourced worldwide. Fowke (2021) points out that an already stressed lumber market combined with current disruptions in supply led to a tripling of lumber prices between April 2020 and 2021. Shortly after this effort by the NAHB, the US Federal Register of May 27, 2021, reported the new AD and CVD rates. By company, West Fraser had the lowest total (11.38 Percent) and Resolute the largest (30.22 percent); the average company faced total duties of 18.32 percent (Federal Register 2021)

Canadian companies also lobby the DOC. In a letter to Joseph Laroski, Deputy Assistant Secretary for Policy and Negotiations Enforcement and Compliance, on behalf of The Conseil de l'industrie forestière du Québec and The Ontario Forest Industries Association, Baker Hostetler LLP made the case that Canadian lumber policy is fair (Feldman, Snarr, and Anwesen, 2020).

They raise multiple issues that attest to the trade barriers’ distortion of the lumber market and the influence of special interests and government on the American market. First, they alleged that US lumber interests want to use trade policy to undo Canada's comparative advantage in lumber production rather than counter the stumpage subsidy. The tariffs do not level the playing field; they remove Canada’s comparative advantage. Second, they point out that the American lumber industry receives government assistance. Federal, state, and local governments fund US road and environmental concerns. Canadian logging companies are responsible for the roads and environmental concerns. This makes it difficult to determine if the stumpage system gives Canadian companies an advantage over US companies. Third, both Québec and British Columbia have developed stumpage auction systems, but the US has not validated them. Fourth, it is arguable that import quotas from the 2006 SLA slowed the economic recovery in 2009. Finally, the Center for Sustainable Economy has calculated that commercial logging in the US received \$1.2 billion (about \$4 per person in the US) from public sources in 2017 (See table 2).

Table 2: US Special Interest Group Public Funding

Years	Organization	Amount	State	Type
2011–2017	PotlatchDeltic	1.5 million	Arkansas	Sales
2011–2018	PotlatchDeltic	612,154	Arkansas	Use
2001-2010	Potlatch Corp	2.5 million	Nevada	Sales & Use Tax Abatement
1995*	Weyerhaeuser Company	103 million	Kentucky	Credits/Rebates
2003-2019	Weyerhaeuser Subsidiaries	305 million	Multiple & Federal	
2006-2017	Stimson Lumber Co.	1.4 million	Oregon & Washington	Credits & Training Reimbursements
2016	Seneca Sawmill Co	71,045	Oregon	Energy Incentive Program
2010	Hawkins Inc.	1.3 million	Mississippi	subsidized lending
2013	Hawkins Inc.	100,000	Mississippi	State grants and loans
2007-2018	Swanson Group	497,643	–	Tax abatements and training reimbursements

2008-2017	Pleasant River Lumber Co	857,690	Maine	Property Tax Abatements and Tax Rebates
2018	Pleasant River Lumber Co	4,226,000	Maine**	Grant for a Sawmill Expansion

Source: Feldman, Snarr, and Anwesen 2020. *Approved in 1995 but received over the next several years. **The grant came out of a \$45 million bond that the Maine Technology Institute manages for the State of Maine.

Joseph Kalt (1988: 355, 359) calculated the potential welfare effects of the two different 1986 trade policies: the 15 percent US CVD and the 15 percent Canadian export tax. The primary difference between the two is which government gains at the expense of the consumer. Because Lumber II concluded with the export tax, according to Kalt’s (1988) calculation, the Canadian government received 117.6 million dollars from the US government to appease the CFLI and maintain the Canadian FTA. However, the United States government does not pay Canadian taxes. They are paid primarily by the American consumer in higher home prices. So, American home prices rise to pay the export tax and maintain American lumber’s position in the market.

Following Tullock (1967: 228), American lumber interests will be willing to invest in lobbying for this transfer until the marginal return on the last dollar spent is equal to the anticipated return on the transfer. Thus, 400-plus million dollar (Kalt 1988: 355) potential transfer led to an ever-present lumber lobby. In 1995 as the Canadian share of the market expanded under free trade, a CFLI fundraising letter was leaked that requested 75 million dollars to protect the industry through Congress. The letter also stated that the Canadian industry had spent between 50 and 100 million dollars (US) on the last case (Zhang, 2007).

In 2000, Senator Robert Byrd attached a rider to the agricultural appropriations bill that increased the potential transfer. The rider gave the AD and CVD to the companies that petitioned

for them (Zhang, 2007). The Byrd rider passed just before AD was added to the CFLI's case. To initiate an AD investigation, 50 percent of domestic producers must support it. The incentive to receive a portion of the duties collected at the border was ample motivation to gain at least 50 percent support. (In Kalt's analysis, the government would collect 117 million dollars; under the Byrd rider, private companies would collect the entirety.)

4 Conclusion

Trade barriers hinder the international market process. Though their justifications are manifold, the above theory and illustrations argue that those justifications require reassessment. Using trade policy to protect a country's industries from foreign competition results in a dynamic, cyclical process driven by unforeseen entrepreneurial discovery.

I have illustrated this process with the Chicken and Lumber Wars. Since intervention circumvents the market discovery process, the resulting shape of the market is not based on market valuation, but on the negotiations of bureaucrats and special interest groups. This results in allocation by special interests and trade barriers, not to most valued use. In fact, the world value of resources is not possible to determine. Lightweight trucks, poultry, lumber, all these goods are not produced by the individuals with comparative advantage, but by the countries with the prevailing trade barrier. Due to the unsimulated discovery process of intervention, there is a proliferation of special interest groups and rent seeking (see Table 2). Also, entrepreneurial energy is diverted to unproductive innovations in rent seeking such as the dominant use clause and the Byrd Rider.

Trade barriers stifle entrepreneurial discovery. Foreign companies will only innovate to compete to the point that quotas or tariffs make it cost-effective. The domestic consumer is

denied the variety of foreign products and the lower prices that result from competition. For example, the W. German consumer was denied the US poultry companies innovations in cooking, American homeowners pay more for their houses, and the American truck market is expensive and limited in scope. Finally, the ubiquitous presence of entrepreneurial discovery leads to superfluous opportunities that no one, not a special interest, bureaucrat, nor congressperson, could anticipate. These opportunities, such as the Japanese truck imports or the Ford Connect, reveal that it is not possible to know how a trade policy will play out in the market. The use of tariffs to protect specific industries has led to political, not economic, efficiency. The above price and production changes are responses to shifts in the political, not the economic, environment. When the government protects its industries from low-cost foreign competition, they divert entrepreneurial energy from efficiency-improving ingenuity aimed at customer satisfaction to political maneuvering.

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