in brief...

# Freedom fries: when international relations damage international trade

When public attitudes towards a foreign country turn negative, what are the effects on trade, and especially trade in firm inputs? **Guy Michaels** and **Xiaojia Zhi** explore this question using the deterioration in Americans' opinions of France following the two countries' dispute over the invasion of Iraq – a deterioration so drastic that French fries were renamed 'freedom fries'.

When the French government opposed US efforts to obtain a United Nations mandate to use military force against Iraq in 2002, the resulting standoff led to a massive deterioration in Americans' opinion of France. Our research uses this episode to track the impact of such worsening international relations on the business decisions of firms involved in trade between the two countries. We find significant effects: worsening attitudes decreased trade.

According to US polls of public opinion, in February 2002, 83% of Americans viewed France favourably; by March 2003, this proportion had declined to 35%. Even three years later, in February 2006, the fraction of Americans with a positive view of the French had recovered only as far as 57%.

Very negative attitudes towards France became common even among affluent, college-educated Americans, so they were likely to be prevalent among managers. By contrast, attitudes towards Germany worsened much less and recovered quite quickly, and attitudes towards Britain, Italy and Spain changed very little.

The US government also singled out France in particular: Condoleezza Rice, then the president's national security

International trade flows may be sensitive to large changes in relations and attitudes

## US imports from France declined sharply following the two countries' standoff over Iraq

adviser, was quoted by Reuters in March 2003 telling associates to 'punish France, ignore Germany and forgive Russia'. There were also calls in the media to ban French products, and the House of Representatives cafeteria began to serve 'freedom fries' instead of French fries.

This shock to relations between France and the US provides an ideal opportunity to examine the effect of attitudes on trade. In other circumstances, international trade may in itself affect attitudes. For example, perceived gains from trade may motivate the US and China to improve relations. But at the same time, increased trade may cause Americans to fear that China threatens their jobs, worsening attitudes.

But in the case of the United States and France, there are clear reasons for the worsening attitudes and those reasons are unrelated to trade. The US-France setting also avoids the problem that worsening attitudes may be correlated with increased personal risk; this may be a problem in other circumstances, where worsening attitudes may cause risk of war or terrorism. And using other OECD and eurozone countries as plausible counterfactuals for France makes it possible to net out the short-run changes in trade that may have taken place in the absence of worsening relations.

Our study finds that US imports from France fell by about 15% and US exports to France fell by about 8% compared with other OECD or eurozone countries. This decline was due in large part to a fall in France's share of the quantity of inputs traded with the United States. There was a similarly large decline in both US business trips and tourist visits to France, suggesting that worsening relations did indeed affect transactions between firms.

One interesting aspect of this natural experiment is that it is difficult to rationalise the decline in trade of inputs using standard arguments of firms choosing inputs that minimise their costs of production. The attributes of inputs produced in France and by competing input producers, and the characteristics of firms' production processes in the United States are not likely to have changed in the short run. This suggests that tastes – and not only simple cost-minimising calculations – may affect firms' choice of inputs.

These results also suggest that international trade flows may be sensitive to large changes in relations and attitudes. We conclude that the effect of attitudes may be particularly strong where there are strong incentives to punish a foreign country – as in the case of commodities used by governments – or where the availability of close substitutes lowers the cost of changing a firm's input suppliers. This result may be especially important for understanding the robustness of trade flows between Western countries and other important trade partners.

This articles summarises 'Freedom Fries' by Guy Michaels and Xiaojia Zhi, CEP Discussion Paper No. 815 (http:/cep.lse.ac.uk/pubs/download/dp0815.pdf).

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