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The Changing Nature of Protectionism: Are "Free Traders" Up to the Challenges It Presents?

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In the economic model that underlies the WTO the only group that can be expected to ask for protection is producers in importing countries. The existing multilateral trade architecture reflects that assumption. Much of the recent criticism of the multilateral trade regime has arisen as a result of new groups explicitly asking domestic politicians for protection. As these groups were not expected to ask for protection, the international trade regime does not allow domestic politicians to extend protection on the basis of the new demands. Further, countries are expected to perceive benefits from trade liberalisation. These benefits must be balanced against the expected political benefits of protectionism (and their associated welfare costs) when trade negotiations are being conducted. Failed economies, however, see few benefits from liberalisation and, hence, are biased toward protectionism, particularly if trade restrictions are a source of corruption incomes. This article explains the sources of new appeals for protectionism, outlines the relationship with traditional producer protectionism and lays out the challenges the new pressures present for trade-liberalising multilateral institutions.

Keywords: consumers, environmentalists, failed economies, producers, protectionism, welfare

> In every country it always is and must be the interest of the great body of the people to buy whatever they want of those who sell it the cheapest. The proposition is so very manifest, that it seems ridiculous to take any pains to prove it; nor could it ever have been called in question, had not the interested sophistry of merchants and manufacturers confounded the common sense of mankind. Their interest is, in this respect, directly opposite to that of the great body of the people. As it is the interest of the freemen of a corporation to hinder the rest of the inhabitants from employing any workmen but themselves, so it is the interest of the merchants and manufacturers of every country to secure to themselves the monopoly of the home market. Hence … the extraordinary duties upon almost all goods imported by alien merchants. Hence the high duties and prohibitions upon all those foreign manufactures which can come into competition with our own.
>
> Adam Smith, 1776[1]

Introduction

When Adam Smith turned his sights on protectionists, there was no doubt about who the targets were and the vested interest they had in obtaining (or retaining) relief from having to compete with imports. Those seeking protection were primarily businessmen (including the owners of agricultural land) whose ability to compete with imports was declining. Those defending existing protection were firms whose profitability, and possibly survival, would be threatened if foreign alternatives were given unfettered access to their home market. While Smith well understood the form and scope of the interests seeking protection, at the time this was not generally the case as those narrow vested interests had managed to cover themselves with the cloak of legitimacy by having protectionism identified with the general good. The ruling paradigm of the day was mercantilism, which eschewed imports because they drained the economy of bullion. Stocks of bullion had a central role in national security as they could be used to finance defence expenditures and essential imports in times of war or other disruptions to international commerce. In the mercantilist's creed, imports were to be curtailed not because of the positive price effect protection provided for domestic competitors but because restricting imports slowed down the drain on the country's bullion reserves. Enhancement of domestic prices was only an "unimportant" side effect of trade policy initiatives.

Smith and the "free trade" advocates that followed him over the next century and a half were primarily concerned with debunking theories that legitimised protectionism by correlating it with the national interest. Not only mercantilism but

also balance of trade, infant industry, national security, revenue-raising tariff, infant economy, import substitution industrialisation and a host of other theoretical arguments were shown, in their turn, not to be generally welfare enhancing (Kerr and Perdikis, 2003). The result was that by the time the General Agreement on Tariffs and Trade (GATT) was being negotiated in the late 1940s protectionists had lost the intellectual battle and no theory that associated trade restrictions with the general good had survived the intense scrutiny of the economics profession.[2] According to Kerr and Perdikis,

> Currently, protectionism's acceptability as a government objective is on the wane. It is clearly identified with particular vested interests rather than the national good (2003, 47).

This loss of intellectual credibility makes concessions granted to protectionists much more difficult to obtain and to defend. Protectionists understand this vulnerability and, hence, seek legitimacy, even if the means of achieving it are indirect.

The process of stripping away the legitimacy of protectionist arguments is closely associated with the development and refinement of the dominant international trade theory based on the neoclassical paradigm. This elegant and intellectually consistent model is the powerful analytical tool that underlies the GATT. While the trade model based on the neoclassical paradigm is formulated in a general equilibrium framework, trade policy is conducted on a product-by-product basis. When transposed into a partial equilibrium framework to facilitate the analysis of trade policy, the effects of trade restrictions (or liberalisation) are amenable to the standard economic tools used to examine changes in welfare (Gaisford and Kerr, 2001). This is the model that provides the intellectual foundation for the GATT and subsequently the WTO.

In the partial equilibrium trade model, trade restrictions unambiguously make consumers in the importing country worse off – consumer surplus declines – while they benefit domestic producers – producer surplus increases. Hence, only producers have an interest in asking for protection. Consumers are not expected to ask for protection – it is not in their interest to do so. It is also easy to show that trade liberalisation is welfare increasing for both exporters and importers and, hence, globally. This was the intellectual starting point for the negotiation of the GATT.

While it was recognised that trade restrictions could not be easily removed due to politicians' needs, at times, to respond to vested interests, it was clear who those vested interests were – producers in importing countries. The GATT was to work to remove trade barriers over the long run while recognising the constraints vested producer interests (particularly existing vested interests) represented. It is also clear that no other protectionists were expected – in concert with the underlying economic

model. Further, this approach to trade policy gave no legitimacy to the imposition of trade barriers. Their imposition was simply pandering to special interest and a recognition of the politics of protectionism. Given this intellectual underpinning, the GATT had considerable success in removing trade barriers. Being stripped of any legitimacy, protectionists could still achieve local successes but the cost of these successes was high and difficult to sustain.

The New Faces of Protectionism

The convergence between the economic model and the making of trade policy multilaterally continued up and through the Uruguay Round. In the post–Uruguay Round period, however, the underlying economic model has looked less robust and trade policy making has become much more complex. This is largely due to the arrival of new protectionist interests. Their rising influence has forced domestic politicians to reckon with them (Isaac, 2003) but the multilateral trade policy regime has not yet found a way to deal with their issues operationally (Perdikis and Kerr, 1999).

While there are a plethora of new protectionist interests, three seem to have garnered sufficient domestic policy-making influence to put the international trade regime under stress. These groups are, broadly defined, 1) consumer issue–based; 2) environmental issue–based; and 3) failed economy–based.

As suggested above, in the economic model that underlies the WTO, consumers are not expected to ask for protection. The WTO has no mechanism to allow protection based on consumer concerns (Perdikis and Kerr, 1999). This means that domestic politicians have no institutional mechanism within the WTO to allow them to extend protection in response to issues raised by consumers. Thus, the WTO does not extend the same institutional compromise that allows domestic politicians to respond to traditional producer-based requests for protection. This creates considerable friction and denies the political reality of domestic politicians' relation to vested interests in trade policy making.

It should be made clear that consumer issue–based groups asking for protection, for the most part, represent subsets of the consumer population. They are usually comprised of individuals who have strong preferences related to a particular issue. Some of the issues that have come to the fore since the end of the Uruguay Round include animal welfare, labour standards, the use of growth hormones in animal production and the use of biotechnology in food production. In each of these cases, subsets of consumers with strong preferences have been asking their domestic politicians to limit market access to foreign products that contravene their preferences.

In a political sense, this is no different from a firm or industry association asking for limits on market access for competing products. The WTO does allow restrictions on imports of products that represent a recognised hazard for consumers (Isaac, Phillips and Kerr, 2002), but in the cases above either no hazard exists or those consumers with strong preferences refuse to accept the current international standards for scientific evidence for establishing when a hazard exists (Kerr, 2003).

In the cases of labour standards and animal welfare, neither issue has yet come to a head at the WTO, although the EU has brought a proposal on animal welfare forward to the WTO (Hobbs et al., 2002) and labour standards side agreements are increasingly being included in regional trade agreements. In the case of the use of growth hormones in beef production, with no way to respond directly to the concerns of consumer groups, the EU attempted to use the Agreement on Sanitary and Phyto-sanitary Measures (SPS) to justify the imposition of an import ban despite its own scientific evidence to the contrary – evidence that had no impact on the strong preferences of those who opposed beef produced using growth hormones being granted access to their markets. In the end, the EU lost its case at the WTO but chose to accept retaliation rather than grant market access (Kerr and Hobbs, 2002). The EU's attempt to cynically subvert the science-based SPS weakened the agreement's credibility and thus may have nullified one of the major accomplishments of the Uruguay Round. The failure to grant market access after losing in the dispute settlement process calls into question the efficacy of the WTO's dispute resolution system, another major accomplishment of the Uruguay Round. Again, it is the inability of the current international trade architecture to deal directly with consumer-issue concerns that has forced the EU down this particular path – it was the only option available to respond to consumer demands for protection.

A much bigger confrontation is brewing over the issue of granting market access for agricultural products that are produced using biotechnology (Isaac and Kerr, 2003). Unlike the case of beef produced using growth hormones, the potential value of trade affected is large and, consequently, the disruption to trade that could arise if the barriers to trade in the products of biotechnology are upheld, or if acceptance of retaliation by the EU is the eventual outcome, is very large.

The difficulties associated with dealing with consumer-based issues have also endowed traditional producer protectionist interests with a legitimacy they have not had since before the establishment of the GATT. Restrictions on trade imposed on the basis of consumer-based issues also provide economic benefit to domestic producers of products that would compete with imports. Domestic producers of goods that compete with imports produced in countries where labour standards are low or poorly

enforced benefit from trade restrictions imposed due to consumer concerns. Beef producers in the EU benefit from the import ban on imports of beef from North America. As a result, traditional producer protectionists are able to channel their often considerable resources into the fray in support of consumer issue–based groups, increasing the influence of those groups in the domestic political process.

Further, it has been shown that when the strong assumption of the neoclassical model pertaining to perfect knowledge of consumers is replaced by information asymmetry, as can be the case with biotechnology, trade liberalisation is no longer unambiguously welfare enhancing (Gaisford and Lau, 2000). As a result, politicians may have a legitimate reason to impose trade barriers. The question of an open trade regime becomes an empirical one that, relative to the normal unambiguous result, confers considerable legitimacy on protectionism, regardless of its source. As there was no need to deal with consumer concerns in the past, empirical techniques to deal with them are poorly developed and their results open to question by protectionist interests.

The convergence of consumer issue–based requests for protection and traditional producer vested interests makes it difficult to determine the true underlying source of protectionist pressure. Given the resources often available to traditional producer protectionists, there is a concern that ostensibly consumer issue–based organisations may simply be well financed fronts for traditional producer protectionist interests, or that the influence of legitimate consumer issue–based civil society groups can be artificially enhanced by transfers of financial resources from producer issue–based protectionists. This issue of "capture" will be particularly difficult to deal with if the current trade architecture is to be revised to take into account consumer issues.

The second prominent new group asking for protection is environmentalists. In some cases their issues pertain to consumption – requests to deny market access to products not produced in an environmentally friendly fashion, e.g., dolphin unfriendly tuna – and yield the same problems as other consumer issue–based requests for protection. In other cases, however, the risk trade presents for the environment is the concern. In some cases the perception is that economic growth is bad for the environment and, as trade liberalisation leads to economic growth, it should be opposed. This perception is at the heart of the anti-globalisation protests against the WTO. As the trade–economic growth–environmental degradation paradigm is controversial it has not become a major domestic political issue in most countries. More popular is the "race to the bottom" hypothesis, whereby lowering environmental regulations will impart a competitive advantage for tradable goods. Environmental groups worry about the deleterious effect this "trade incentive" will have on the global

environment. The hypothesis also, however, gives legitimacy to traditional producer protectionist interests and their allies such as labour unions that are concerned with the loss of competitiveness and the offshore movement of investment and jobs. These groups are able to make common cause with environmental groups and lend their resources to fostering a cause that has considerable legitimacy – even if the hypothesis itself remains controversial.

Finally, environmental groups often want higher standards of scientific evidence to be used for determining when imports are to be considered safe for the environment. In particular, they have pushed to have the precautionary principle enshrined in trade law. The problem with the precautionary principle is that it remains a principle and, as yet, there is no international agreement on how it can be operationalised for decision making purposes (Kerr, 2003; Van den Belt, 2003). As currently constituted, the precautionary principle can be interpreted by each individual country, and therefore not open to dispute, leaving it wide open to capture by protectionist interests of all stripes.

International policy making pertaining to the environment is not perceived as primarily a trade issue and has been developed through the negotiation of multilateral environmental agreements (MEAs). For the most part these have not had trade provisions, but in recent years some MEAs have incorporated trade rules – in particular the Convention on International Trade in Endangered Species (CITES), the Basel Convention on the Transboundary Movement of Hazardous Wastes and Their Disposal and, more recently, the Biosafety Protocol (BSP) dealing with trade in products of biotechnology (Kerr and Hall, 2004). These agreements are largely negotiated by environment ministries that have no particular stake in the smooth functioning of the international economy, and may be antipathetic to trade liberalisation. While they could contravene WTO commitments, CITES and the Basel Convention have not proved to be controversial. The Biosafety Protocol, in contrast, looks likely to be the source of considerable international tension, as it contains a number of provisions that appear to directly contravene the WTO (Phillips and Kerr, 2000) and a number of countries, including the United States, do not belong or have failed to ratify it (Isaac and Kerr, 2003). Further, the BSP is supposed to be about the preservation of biological diversity and the introduction of living modified organisms such as plant seeds into the environment of the importing country, but it also includes trade provisions that pertain to consumer issues. The latter represent an attempt to circumvent the WTO by having the issues dealt with in an alternative international institution (Isaac, Phillipson and Kerr, 2002). Given that the volume of trade

constituted by products of biotechnology is growing rapidly, competing rules for trade are likely to lead to acrimonious trade relations.

The problem of trade rules being incorporated into MEAs was considered sufficiently important for the framers of the Doha Round to formally charge the WTO's Committee on Trade and Environment with clarifying the relationship between the WTO and MEAs. As yet, little progress has been made, again emphasising the difficulty the current multilateral trade institutions have in dealing with new groups requesting protection.

The final group of new protectionists arise in failed (or near failed) economies. While in most countries traditional producer protectionist interests are tolerated within the general context of the benefits of a liberal trade regime, failed economies are sufficiently dysfunctional that they, at best, can expect to receive only marginal benefit from an open trade regime. Further, regulating trade becomes one of the most lucrative means for domestic politicians to extract corruption rents that can, in part, be used to keep them in power. This may either be through opportunities for bribery or the exercise of an import monopoly. Hence, instead of protection benefiting producers it benefits domestic politicians. Trade liberalisation is a direct threat to their livelihood and possibly their political survival.

Instead of the political compromise between the need for strong rules of trade to secure the benefits of market access for exports and the need, at times, for politicians to extend protection against imports to domestic vested interests, decision makers in failed economies see no benefits from liberalisation. This translates into intransigence in international negotiations and an insistence on wide ranging "special and differential" treatment. Further, instead of the incentive of economic benefit, incentives for trade liberalisation concessions can become tied to other international issues. Without the incentive of economic benefit, opportunities for hold-up arise given the WTO's need to seek consensus on trade liberalisation. While much is made of the incompatibility of economies that have a high degree of state intervention in prices (such as China) with the WTO (Hobbs and Kerr, 2000), there has been little examination of the compatibility of failed economies with the WTO. With the leadership of failed economies likely the major beneficiaries of protectionism, the absence of a legitimate justification for protectionism is not a concern. Given the failure of developed countries to deliver on their Uruguay Round commitments to developing countries, the leaders of failed economies have all the justification they need for their defence of protectionism. Their intransigence gives legitimacy to traditional producer protectionist interests in non-failed economies. The member states of the WTO have yet to address the issue of protectionism in failed economies

and, in particular, the hold-up problem that it creates in the institution's decision making.

Conclusion

The world is no longer as simple as the economic model that underlies the WTO. The seeking of protection is no longer confined to producer interests in importing countries but rather includes new groups that have different motives and incentives. The current multilateral agreements and institutions have not yet found ways to respond to the new groups seeking protection. Further, traditional producer protectionists are willing to capitalise on any intellectual legitimacy given to the new groups seeking protection and to provide resources to foster that legitimacy.

Economists have, as yet, given little attention to how the new sources of protectionism can be incorporated into their analytical models. As in Adam Smith's day, until that work is done it will be difficult to determine whether the new pleadings for protection have any more public policy legitimacy than those of traditional producer protectionism. It is well to keep in mind Adam Smith's observation regarding "balance of trade" arguments for a restrictive trade policy:

> That it was the spirit of monopoly which originally both invented and propagated this doctrine, cannot be doubted; and they who first taught it were by no means such fools as they who believed it.[3]

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Endnotes

1. See Smith (1994, 527).
2. The one exception that might come to mind is the special set of circumstances associated with "optimum tariff" arguments developed by Metzler in 1949 – which was, however, after the negotiation of the GATT.
3. See Smith (1994, 527)

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