Protectionism and Free Trade: A Country's Glory or Doom?

Regine Adele Ngono Fouda

Abstract—**This paper does not only go over the ground of the generally traversed, and examined arguments commonly used, but, it carries the inquiry further than the controversialists on either side, yet ventured to go; also a sought to discover why protection retains such popular strength in spite of all exposures of its erroneous beliefs; to trace the connection between the tariff question and more important social questions, now rapidly become the "burning questions" of our times; and now to show what radical measures the principle of free trade logically leads to. Thus harmonizing the truths which free traders perceive with the facts that protectionists make their own theory plausible, it's perceived that this might open ground upon which those separated by seemingly irreconcilable differences of opinion may unite for that full application of the free-trade principle which would, secure both the largest production and the fairest distribution of wealth. Also facts emanating a posteriori will contain the general viewpoint of a country's recommended choice, as well as my view point.**

Index Terms—**Free trade, protectionism, glory(advantages), Doom(drawback), industries, taxes, import/export, case study(on economic growth).**

I. Introduction

Free trade is a system in which the trade of goods and services between or within countries flows unhindered by government-imposed restrictions and interventions. Interventions include taxes and tariffs, non-tariff barriers, such as regulatory legislation and quotas, and even inter-government managed trade agreements such as the North American Free Trade Agreement (NAFTA) and Central America Free Trade Agreement (CAFTA) (contrary to their formal titles.) Free trade opposes all such interventions. One of the strongest arguments for free trade was made by classical economist David Ricardo in his analysis of comparative advantage explains how trade will benefit both parties (countries, regions, or individuals) if they have different opportunity costs of production. Protectionism, in the other hand is an economic policy of restricting trade between nations. Trade may be restricted by high tariffs on imported or exported goods, restrictive quotas, a variety of restrictive government regulations designed to discourage imports, and anti-dumping laws designed to protect domestic industries from foreign take-over or competition.

II. Protection of Home Industries in Disfavor of Foreign Goods

Manuscript received July 22, 2012; revised August 25, 2012.

Regine Adele Ngono Fouda is with Shanghai Maritime University, China(e-mail: reginemilena@yahoo.fr)

Protectionism, an economic policy of restraining trade between nations, through methods such as tariffs on imported goods, restrictive quotas, and a variety of other restrictive government regulations is designed to discourage imports, and prevent foreign take-over of local markets and companies. This policy is closely aligned with anti-globalization. This term is mostly used in the context of economics; protectionism refers to policies or doctrines which "protect" businesses and "living wages" within a country by restricting or regulating trade between foreign nations. Adam Smith famously warned against the 'interested sophistry' of industry, seeking to gain advantage at the cost of the consumers. Virtually all modern day economists agree that protectionism is harmful in that its costs outweigh the benefits, and that it impedes economic growth. A lot of situations made it possible that the international world called upon a general meeting to try to solve this crisis. This was true in 1947 when the General Agreement on Tariff and Trade (GATT) was signed with objectives of encouraging international trade, and reducing tariff as possible. [1]

A. A Country's Protectionism: Blooming Glory

A country's protectionism will mean the protection of home industries or 'infant industries' (until they are large enough to achieve economies of scale and strong enough to compete internationally.), producers and consumers. The fundamental of internal trade wouldn't involve trade activities across national borders. Therefore this will reduce the special problem which often subsequently arise during import and export; crisis such as, deals might have to be transacted in foreign languages, foreign laws customs and regulation (protectionism frees such trauma). Moreover, information from particular firms needed in order to trade might be difficult to obtain, as well as the exporting countries' numerous cultural differences may have to be taken into account when trading. All these complicated tribulations rendered a lot of countries to "think twice" by 'staying at home' and enjoying home industries' goods and products, denying therefore to practice import and export.

Furthermore, having to export products from foreign countries will mean taking into consideration its currency; worst of all if the exchange rate variation is wider than the protectionist (country). Therefore such situation will create an exposure of taking debts to fulfill the contract (partnership agreement) of import and export, e.g. Cameroon in its thirst of practicing import/export, is always stock in currency transaction, forcing it to take debts from the world bank in order to keep the agreement moving, or else will have to face a penalty of **'**breach of contract**'.**

Also, there is a greater political risk (such as the imposition of restriction on imports etc); commercial risks are broad too, such as markets failure, products not appealing to foreign customers as it's the case of many goods nowadays in foreign soils; more again, there are financial risks, such as adverse movement in exchange rates; and finally, transportation risks.

B. Protectionism As A Fatal Failure: The Doom.

No nation has all of the commodities that it needs. Some countries are abundant in certain resources, while others may lack them. For example, Colombia and Brazil have the ideal climate for growing coffee beans. The US is a major consumer of coffee, yet it does not have the suitable climate to grow any of its own. Consequently, this has made Colombia and Brazil big coffee exporters and the US big coffee importer. In this case, if the US were practicing protectionism, then they can't import coffee; this is true too for Cameroon, producer of cocoa and France consumer. In short, the uneven distribution of resources around the world would not give room for protectionism.

Moreover, a country might claim that it has more than enough particular items to meet its needs and enough technology to manufacture or transform its natural products, however, this country might be consuming more than it can produce internally and thus will need to import from others depicting equilibrium in trade.[2]

Protectionism results in deadweight loss. It has been estimated by the economist Stephen P. Magee (International Trade and Distortions in Factors Market 1976) [3] that, the benefits of free trade outweigh the losses as much as 100 to 1. Moreover, Alan Greenspan, former chairman of the American Federal Reserve, has criticized protectionist proposals as leading "to an atrophy of our competitive ability. ... If the protectionist route is followed, more efficient industries will have less scope to expand, overall output and economic welfare will suffer."

Protectionism has also been accused of being one of the major causes of wars. The constant warfare in the 17th and 18th centuries among European countries whose governments were predominantly mercantilist and protectionist; the American Revolution, which came about primarily due to British tariffs and taxes; as well as the protective policies preceding World War 1 and 2. According to Frederic Bastiat, "When goods cannot cross borders, armies will." History following this enunciation is not lacking example such as; in 1930, facing only a mild recession, US President Hoover ignored warning pleas in a petition by 1028 prominent economists and signed the notorious Smoot-Hawley Act, which raised some tariffs to 100% levels. Within a year, over 25 other governments had retaliated by passing similar laws. What was *the result?* World trade came to a grinding halt, and the entire world was plunged into the "Great Depression" for the rest of the decade. The depression in turn led to World War II. An enhanced clarification is, when the government of Country "A" puts up trade barriers against the goods of Country "B", the government of Country "B" will naturally retaliate by erecting trade barriers against the goods of Country "A". *What was the result?* A trade war in which both sides lose. But all too often a depressed economy is not the only negative outcome of a trade war . . .

III. A Country's No Restriction or Taxes on Its Import/Exports

Opponents often argue that the comparative advantage for free trade has lost its legitimacy in a globally integrated world—in which capital is free to move internationally. Herman Daly, a leading voice in the discipline of ecological economics, emphasizes that although Ricardo's theory of "comparative advantage is one of the most elegant theories in economics", Free capital mobility totally undercuts Ricardo's comparative advantage argument for free trade in goods, because that argument is explicitly and essentially premised on capital (and other factors) being immobile between nations. Under the new globalization regime, capital tends simply to flow to wherever costs are lowest—that is, to pursue absolute advantage. Moreover, economist and trade theorist Paul Krugman once stated that, "If there were an Economist's Creed, it would surely contain the affirmations 'I believe in the Principle of Comparative Advantage' and 'I believe in Free Trade'.''[4]

A. Practicing Free Trade: As an Advantage.

The literature analyzing the economics of free trade is extremely rich with extensive work having been done on the theoretical and empirical effects. Though it creates winners and losers, the broad consensus among members of the economics profession in the U.S. is that free trade is a large and unambiguous net gain for society. A fruitful example of this vision is that, in a 2006 survey of American economists, "87.5% agree that the U.S. should eliminate remaining tariffs and other barriers to trade" and "90.1% disagree with the suggestion that the U.S. should restrict employers from outsourcing work to foreign countries." Quoting Harvard economics professor Gregory Mankiw. [5] Few propositions command as much consensus among professional economists as that open world trade increases economic growth and raises living standards. This fact grew up drastically when again it was found out that, Free trade creates more jobs than it destroys because it allows countries to specialize in the production of goods and services in which they have a comparative advantage. Moreover, Economists, such as Milton Friedman [6] and Paul Krugman have argued that free trade helps third world workers, even though they are not subject to the stringent health and labor standards of developed countries. This is because "the growth of manufacturing — and of the penumbra of other jobs that the new export sector creates — has a ripple effect throughout the economy" that creates competition among producers, lifting wages and living conditions.

A simple economic analysis using the law of supply and demand and the economic effects of a tax can be used to show the theoretical benefits of free trade as shown below;

It is believed that growth in productive capacity was fostered best in an environment, where people were free to pursue their own interests. Moreover stressed that, a government policy of laissez faire (allowing individuals to pursue their activities within the bounds of law and order respect for property rights) would best provide the environment for increasing a nation's wealth, thus home industries boom up.

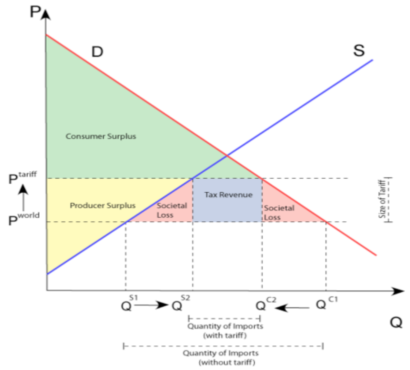

Fig. 1. A simple economic analysis using the law of supply and demand and the economic effects of a tax to show the theoretical benefits of free trade

More again, self interest is a catalyst, whereby, any normal business person or entrepreneur will definitely like to work in an environment, where no barriers are levied to hinder what he/she is planning to set forth. Again, it would lead individuals to specialize and exchange goods services based on their own special abilities. Furthermore, competition is the automatic regulation mechanism, because, if there are taxes, there can't be competition; the reason being that many people can't afford the higher ratios. Again, the father of economic Adam Smith, in his work saw little need for government control of the economy. In *The Wealth of Nations*, 1776, [7] Adam explained not only the critical role the market played in the accumulation of a nation's wealth but also the nature of the social order that it achieved and helped to maintain.

B. Free Trade As A Grave Setback

A strong argument lies on infant industries, where if developing countries have industries that are relatively new, then at the moment these industries would struggle against international competition. However if they invested in the industry then in the future they may be able to gain Comparative Advantage. Protection therefore would allow them to progress and gain.

The Senile industry argument is that which, If industries are declining and inefficient they may require large investment to make them efficient again. Protection for these industries would act as an incentive for firms to invest and reinvent themselves.

To diversify the economy, free trade tries to maintain but denies facing the fact that, many developing countries rely on producing primary products where they currently have a comparative advantage. However relying on agricultural products has several disadvantages such as; Prices can fluctuate due to environmental factors, as well as, Goods have a low income elasticity of demand. Therefore with international economic growth, demand will only increase a little. [8]

Free trade is incapable of raising revenue for the government. This is because, Import taxes can be used to raise money for the government, however this will only be a small amount of money. Furthermore, free trade does help the Balance of Payments; reducing imports can help the current account. However in the long term this is likely to lead to retaliation.

Finally, Cultural Identity which is not really an economic argument but political and cultural. Many countries wish to protect their countries from what they see as an Americanization or commercialization of their countries. More again, there's a need of protection against dumping. The EU sold a lot of its food surplus from the CAP at very low prices on the world market. This caused problems for world farmers because they saw a big fall in their market prices. Also, environmentally, it is argued that free trade can harm the environment because LDC may use up natural reserves of raw materials to export. Also countries with strict pollution controls may find consumers import the goods from other countries where legislation is lax and pollution allowed. However supporters of free trade would argue that it is up to individual countries to create environmental legislation.

IV. Analysis of Pertinent Cases: Case Study

In this analysis, I would base myself on logical world situation nowadays such as, the Japanese consumers pay five times the world price for rice because of import restrictions protecting Japanese farmers. European consumers pay dearly for EC restrictions on food imports and heavy taxes for domestic farm subsidies. American consumers also suffer from the same double burden, paying six times the world price for sugar because of trade restrictions. The US Semiconductor Trade Pact, which pressured Japanese producers to cut back production of computer memory chips, caused an acute worldwide shortage of these widely used parts. Prices quadrupled and companies using these components in the production of electronic consumer goods, in various countries around the world, were badly hurt. However, my main case study will be the banana war as examined below.

A. The Banana Trade: Case Study

The progressive reduction of tariff barriers has caused World Trade to increase by several hundred per cent since 1945, and there is no doubt that this has created both work and prosperity. [9] It has also improved products: although the planned economies of the former Soviet Union and the other countries created industries that produced nearly as much as Western companies, the products were much less sophisticated, reliable or marketable, consequently they were excluded from the competition. Today, most economists argue that nations which try to shelter declining industries behind tariff barriers are simply resisting the inevitable, and that they could use those subsidies to create new jobs in more modern industries. In other words, tariff barriers penalize consumers, for example Japan (as stated above). As for many years, the banana industry had a special status. The European Union allowed former British and French colonies in Africa (notably Cameroon), the Caribbean and the pacific islands to export to Europe as many bananas as they wished, at slightly above world prices. Banana production costs are higher in the Caribbean than on the American owned plantations in Latin America, due to the small size of family-run farms, the difficult terrain, and the climate.

In 1999, for example, the US-based company Chiquita Brand made a $500,000 donation to the Democratic Party. The very next day, the US government complained to the World Trade Organization about Europe's banana trade, and put a 100% import tariff on various European goods. Opponents of the American case pointed out that only 7% of the 2.5billion tones of bananas imported into Europe every year come from the Caribbean. The EU's banana policy only cost American companies about $200 million a year, whereas trade between the US and the EU is worth about 200billion Euros. Half the population of the Caribbean relies on the banana industry to supply their basic needs such as food, shelter and education. Small states such as Dominica depend on banana exports to the EU for around 70 per cent of all export earnings and much of their employment. No other countries in the world have the same degree of dependence on a single product. Nevertheless, if the Caribbean banana industry was taken away without farmers being given enough time to develop other ways of using the land, the countries' economy would collapse. Moreover, the results of entirely free trade in banana could be disastrous.

It could also be pointed out that American, Japanese and Europe farmers are currently subsidized by billions of dollars every year. Yet, America itself erected massive tariff barriers in the 19th century. Furthermore, the Americans wanted to end subsidies to Caribbean banana producers, even though the consequences might have included many of the farmers turning to drug production and trafficking, or trying to immigrate illegally to the US. The 'banana wars' ended in July 2001 when the American ended their special import taxes on selected European goods after the European Union agreed to import more Latin American bananas from the large US banana companies, while still also buying bananas from their former colonies.

B. *Point of View: A Country's Economic Growth*

Protectionists fault the free trade model as being reverse protectionism in disguise, that of using tax policy to protect foreign manufacturers from domestic competition. By ruling out revenue tariffs on foreign products, government must fully rely on domestic taxation to provide its revenue, which falls heavily disproportionately on domestic manufacturing. As Paul Craig Roberts [10] (US Falling Behind Across the Board) notes: "Foreign discrimination of US products is reinforced by the US tax system, which imposes no appreciable tax burden on foreign goods and services sold in the US but imposes a heavy tax burden on US producers of goods and services regardless of whether they are sold within the US or exported to other countries."

Moreover, it is the stated policy of most First World countries to eliminate protectionism through free trade policies enforced by international treaties and organizations such as the World Trade Organization. Despite this, many of these countries still place protective and/or revenue tariffs on foreign products to protect some favored or politically influential industries. This creates an artificially profitable industry that discourages foreign innovation from taking place. Moreover, protectionist quotas can cause foreign producers to become more profitable, mitigating their desired effect. This happens because quotas artificially restrict supply, so it is unable to meet demand; as a result the foreign producer can command a premium price for its products. These increased profits are known as *quota rents (CEE)*. [11]

My point of view, as a freshman economist is to try to understand the degree in which countries have suffered or gained out of these two principles. In spite of evidence of damage caused by trade restrictions, pressure for more "protectionist" laws persists. Who is behind this, and why? Those who gain from "protectionist" laws are special-interest groups, such as some big corporations, unions, and farmers' groups – all of whom would like to get away with charging higher prices and getting higher wages than they could expect in a free marketplace. These special interests have the money and political clout for influencing politicians to pass laws favorable to them. Politicians in turn play on the fears of uninformed voters to rally support for these laws. Who are therefore the losers in this international game*? YOU* and all other ordinary consumers. Your freedom is being trampled into the dust by these laws, and *you* are literally being robbed, through taxes and higher prices, in order to line the pockets of a few politically-privileged "fat cats." This situation made it clear to economist's *mind that some are favored while other*s…also *"Protectionism is a misnomer. The only people protected by tariffs, quotas and trade restrictions are those engaged in uneconomic and wasteful activity. Free trade is the only philosophy compatible with international peace and prosperity."* by Walter Block [12] (Senior Economist, Fraser Institute, Canada). Moreover, another great economist pointed out the fact that, the world enjoyed its greatest economic growth during the relatively free trade period of 1945-1970, a period that also saw no major wars. Yet we again see trade barriers being raised around the world by short-sighted politicians. Will the world again end up in a shooting war as a result of these economically-deranged policies? Can we afford to allow this to happen in the nuclear age? Well, I think not really…because I suppose there is still much to cover, for this better world we're all fighting for. Another great economist pointed out the fact that, the economic war fought in our world today is due to a huge variety of economic philosophy of nationalism, as quoted below. *"What generates war is the economic philosophy of nationalism: embargoes, trade and foreign exchange controls, monetary devaluation, etc. The philosophy of protectionism is a philosophy of war." Ludwig Von Mises (Great Economist).*

Furthermore, for thousands of years, the tireless efforts of productive men and women have been spent trying to reduce the distance between communities of the world by reducing the costs of commerce and trade. Over the same span of history, the slothful and incompetent protectionist has endlessly sought to erect barriers in order to prohibit competition – thus, effectively moving communities farther apart. When trade is cut off entirely, the real producers may as well be on different planets. *"The protectionist represents the worst in humanity: fear of change, fear of challenge, and the jealous envy of genius. The protectionist is not against the use of every kind of force, even warfare, to crush his rival. If mankind is to survive, then these primeval fears must be defeated." Ken Schoolland (Former US International Trade Commission Economist).*

V. Conclusion

Being an economist nowadays is full of ambiguity situations, this because after some international analysis of economic principles such as protectionism and free trade, you get filled with a lot of glories and dooms witnessed in both parties in the international aspects. Nevertheless, one can easily realize after the above analysis that protectionism is out dated for so many countries round the globe, yet still the standing peak of many others. Whereas, free trade is the mostly appreciated in a lot of countries nowadays, and of course progressively dragging many other countries to suddenly reduce protectionism and click in favor of free trade, in order to avoid "economic wars" led by restrictive borders tariffs, quotas, barriers etc. For *Ludwig V. Mises*, the whole basis of economics is human action, and human action means *change*. Human conditions also change: populations grow and shift, and younger members replace the older ones, bringing fresh ideas with them. Production methods change too, with new processes being invented and old ones fading into disuse.[13] This facet also leads for a wise elucidation that, "economic in the international trade world changes as time goes by, especially as knowledge and technology inflates" by (Regine Adele Ngono Fouda, student in Masters in International Trade science Dept. Nov. 2008).

ACKNOWLEDGMENT

I will like to say thank you firstly to my supervisor Mr. Huang Y. F. Rector/president of Shanghai Maritime University; my vice-supervisor Mrs. Chen and all my other lecturers at the university. I also want to thank my parents, my brothers and sister for all their moral and spiritual support; as well as thanking my friends who in one way or the other contributed in finalizing this paper such as: Elijah M., Aissata D., Gerald O., and all the others which I couldn't name.

REFERENCES

[1] K. Bagwell and R. W. Staiger, "Multilateral Tariff Cooperation during the Formation of Regional Free Trade Areas," *International economic Review*, vol. 38, 1997.

[2] E. R. Baldwin, "Equilibrium in International Trade: A Diagrammatic analysis," *Quarterly journal of Economics*, vol. 62, 1948.

[3] P. S. Magee, *International Trade and Distortions In Factor Markets*, New York: Marcel-Dekker, 1976.

[4] P. Krugman, *Is Trade Passe? Economic Perspective*, pp. 131-144, 1987, *A Raspberry for Free Trade*, Nov. 21, 1997, *In Praise of Cheap Labor*, Mar.21, 1997.

[5] G. Mankiw, *Eastern Economic Journal*, vol. 35, pp. 14 – 23, 2009.

[6] Milton and R. Friedman, *Free to Choose*, New York: Harcourt Brace Jovanovich, Inc., 1980, pp. 40–41, See also Robert McGee, "The Cost of Protectionism," *The Asian Economic Review*, vol. 32, no. 3, December 1990, pp. 347–64, *A Trade Policy for Free Societies*, New York: Quorum Books, 1994, Walter Block and Robert McGee, "Ethical Aspects of Initiating Anti-Dumping Actions," *International Journal of Social Economics*, vol. 24, no. 6, 1997, pp. 599–608, "Must Protectionism Violate Rights?" *International Journal of Social Economics*, vol. 24, no. 4, pp. 393–407, 1997.

[7] A. Smith, *Free trade, and protection, a reprint of Book IV & Chapters II& III of Book V of "The wealth of nations"*, New York: Random House, Inc.,1937, pp. 415.

[8] A. G. Kenwood and A. L. Lougheed, 1999. *The Growth of the international Economy 1820-2000*, 4th ed. London: Routledge.

[9] K. R. Andrew, "Do We Really Know That the WTO increase Trade?" *The American Economic Review*, vol. 94 , no. 1, 2004.

[10] P. C. Roberts, *US Falling Behind Across the Board*, July 26, 2005.

[11] B. Jagdish, "CEE: Protectionism," *Concise Encyclopedia of Economics*, Library of Economics and Liberty, Also, Termites in the Trading System: How Preferential Agreements Undermine Free Trade.

[12] W. Block, "The Necessity of Free Trade," *Journal of Markets & Morality*, vol. 1, no. 2, pp. 192-200, October 1998.

[13] L. Von Mises, *A Primer*, The Institute of Economic Affairs (IEA), Great Britain, 2010.

Regine Adele Ngono Fouda is a Student at Shanghai Maritime University in Shanghai, China. She is from Cameroon, and studies in the Department of Logistics Management.

She has a background studies in Private Law, International Politics, International Trade and now Logistics. She is a very hard working person, who is determined to reach her goal.