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Protectionism or Liberalism in International Economic Relations?

Current Issues in Japan and Germany

edited by

Theodor Dams

Takashi Matsugi



Duncker & Humblot · Berlin

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Economic Relations?**

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Herausgegeben von J. Heinz Müller und Theodor Dams

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Editors' Foreword

This volume contains the proceedings of the 11th Joint Seminar of the Faculties of Economics of Nagoya and Freiburg Universities, held in Nagoya in March 1988. The series of Joint Seminars is concerned with topical economic issues and with the Japanese and German economies in particular.

The current volume covers the question of the foreign trade strategy in leading developed economies. Since the late 1970s, tendencies towards a so-called "new protectionism" have been noted throughout the world. However, economists have not tired to argue in favor of free trade.

Obviously, the debate on "liberalism or protectionism" is a complex one, with different views to be taken into account. Therefore, it was considered an adequate subject for a Nagoya-Freiburg-Seminar. Management scientists, economic theoreticians, specialists of economic policy and public finance treat the issues from different angles. Special emphasis was laid on covering the intricacies of the Japanese and German economies. This holds for a discussion of small- and medium-sized enterprises in Japan or German assistance schemes for the setting-up of businesses, for instance. It is hoped that by covering a wide range of topics, this book can contribute to a more balanced view of an "eternal" economic problem.

Publication of these proceedings was made possible through the financial assistance from the Wissenschaftliche Gesellschaft Freiburg im Breisgau. Editorial work was carried out in the Institute of Development Policy of Freiburg University, coordinated by Dr. Werner Pascha, type-set by Hans Köhne. The cooperation of the Nagoya working group under its chairman, Professor Takashi Matsugi, is also gratefully acknowledged.

Freiburg, October 1990

J. Heinz Müller

Theodor Dams

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Is there a Macroeconomic Case for Protection?

Oliver Landmann¹

1. Introduction: The rise of protectionism

There can be no doubt: Protectionism is riding high again. Gone are the golden 1950s and 1960s when the trade barriers of the interwar period were torn down in a determined effort to liberalize economic relations among industrial nations. To be sure, even in that heyday of trade liberalization, there were pressures working toward increased protection. But they were weak and swamped by the impact of a number of countervailing forces which included the still fresh memory of the disastrous experience of the 1930s, strong U.S. leadership in the liberalization process, increasingly efficient means of transportation and communication, and perhaps most importantly, a background of rapid and steady economic growth².

The momentum of trade liberalization began to slow down in the 1970s as latent structural problems in many industrial countries became more pronounced due to the well known macroeconomic shocks of that decade. Even then, however, much of the protectionism - not all, but much - was confined to rhetoric rather than action. World trade continued to outpace the growth of world GNP, with increasingly outward-oriented developing countries appropriating an ever larger share of that trade.

Protectionist pressures intensified in the 1980s when the world economy was struck by another severe recession and the outbreak of the LDC debt crisis. The strain showed most in the United States whose balance of trade moved into deficit on an unprecedented scale.

¹) Valuable comments from Martin *Bronfenbrenner* and the participants of the 1988 Nagoya-Freiburg Seminar are gratefully acknowledged.

²) For an instructive review of the rise and eventual reversal of trade liberalization in the postwar period, see *Krueger* 1988.

U.S. manufacturing industries were especially hard hit by the desperate attempt of Latin American debtors to turn around their net export position and, of course, by the real appreciation of the U.S. dollar. Calls for protection grew louder and resulted in a number of import restraining measures in sensitive sectors. Even though the *Reagan* administration was ideologically more committed to free trade than most of its predecessors, it was not able to provide strong leadership in promoting the liberalization of world trade. Instead, it felt forced to make repeated protectionist concessions just to keep the pressure from getting even worse.

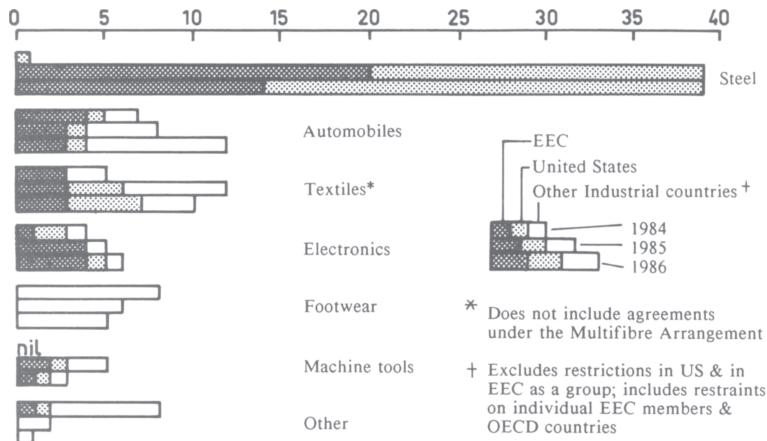
The spreading protectionism did not roll back the achievements reached within the framework of GATT. Tariffs continued to fall. Among developed countries they averaged little more than 5 % on industrial products after completion of the Tokyo round (see Figure 1). However, there was an explosive increase in the number of non-tariff trade barriers such as quotas, voluntary export restraints, idiosyncratic national standards and other forms of 'managed trade'. As far as the industrial countries are concerned, Figure 1 shows that the non-tariff barriers are heavily concentrated on aging industries - steel, vehicles and textiles, in particular. These are exactly the industries in which the highly developed economies are gradually losing their comparative advantage vis-a-vis developing and newly industrialized countries.

This is in line with the observation that the growing impediments to free trade were rarely part of any comprehensive macroeconomic strategy, but rather case-by-case emergency measures to save sensitive sectors from painful adjustments or at least to slow down the displacement of jobs. This is not to deny, of course, that a deteriorating macroeconomic environment greatly strengthened the forces opposing structural change. But only in exceptional circumstances, protectionist measures were taken explicitly to address a macroeconomic problem rather than a sectorial problem; and then the problem was likely to be a balance-of-payments emergency as in the case of *Nixon's* 1971 import surcharge.

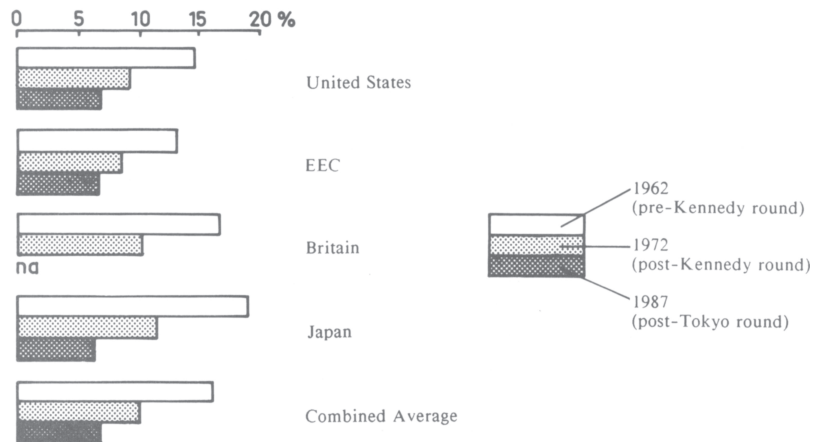
Today, however, protectionism is again very much present in the macroeconomic policy debate, especially in the United States. This is perhaps not surprising in view of the huge and persistent U.S. trade deficit and the general consensus on the need to do something about it. Not only politicians, but even respected U.S. economists have publicly advocated the use of protectionist policies to facilitate the

Figure 1 : More Barriers Block Trade while Tariffs have Tumbled

Number of restraint arrangements on manufactured exports



Average tariffs for industrial products



Source: The Economist, 20 February 1988; based on GATT data