Chapter 5
Trade Protectionism:
Pros and Cons

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ABSTRACT

The increased commercial protection of countries as a result of the Great Depression caused the effects of the global crisis to deepen and last longer. Many countries took short-term steps to minimize the negative social impacts of the crisis by implementing protectionism. However, the crisis was gradually deepened and exerted long-term impacts on macroeconomic variables. The international platform made several attempts to reduce protectionism. However, following the global economic crisis in 2007-2009, the barriers to international trade have increased in many countries, especially in the USA. In many countries, inward-looking protectionist economic policies have been increasingly preferred. Thus, the global impact of countries' adoption of protectionism in their international trade policies has begun to be discussed in terms of the pros and cons for partners. This study analyzes the pros and cons of international trade protectionism on the basis of the impact of trade on macroeconomic variables. The results show that not only protectionism but also free trade produces both winners and losers.

INTRODUCTION

International trade and trade theories are among the oldest branches of economic thought. From the ancient Greeks to the present day, the determinants of trade between countries, their impacts on the parties, and the question of which trade policies are best have been the subject of considerable debate. Depending on the gains from trade or on the losses of those damaged by imports, researchers have put forward different views (Irwin, 2001). It can be said that these views are basically divided into two opposite camps. The first camp focuses on the benefits of free international trade to the parties, especially on its contribution to economic growth and technological progress, while the second focuses on the idea that domestic industries, laborers and cultures are damaged by foreign competition. As it is seen, there is no consensus that free trade is the best trade policy.

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With respect to these two main perspectives, the first has been influenced by Classical thought and the second by Mercantilist thought. According to the Mercantilist thought prevailing in Western Europe in the 17th and 18th centuries, the most profitable situation, that is the source of wealth, is the case where the value of exported domestic goods exceeds the value of imported foreign goods. In other words, the case of foreign trade surplus was considered the most profitable situation. The Mercantilists camp stated that the export of industrial products is beneficial (their import is harmful), while the exports of raw materials are harmful (their import is beneficial). They justified this view by arguing that the increased volume of raw materials in a country provides a cost advantage and by extension leads to an increase in production and employment; thus, the export of high value-added products contributes to the country's economy. They further noted that for the proper functioning of this process, it is necessary to support it with government policies. They, therefore, proposed a highly interventionist system by using trade taxes that change the commodity composition of trade in favor of its homeland. Thus, the entry of gold into the country is supported, while the exit of gold from the country is hindered. One-way free trade in favor of the home country is advocated in line with the basic tenets of Mercantilist thought, which is consistent in itself. In other words, the dominant view is trade protectionism for the main country. However, how is this strategy supposed to work if all partner countries of international trade behave the same? In other words, not every country can have a foreign trade surplus, export only high value-added products or import raw materials. Mercantilism has been subjected to the following criticism: "How can trade be done between countries if each country tries to enjoy a foreign trade surplus?".

The Mercantilist thought that held sway over international trade lost its dominance with the acknowledgment of Adam Smith's book "An Inquiry into the Nature and Causes of the Wealth of Nations" published in 1776. In this work, anti-mercantilist thought was based on important grounds. Thus, the foundations of a new world were laid, which is based on individuality, has no need for government intervention, and is enriched by the dominance of free trade. It was argued that the individual interests of rational people lead to an increase in productivity with the increased division of labor and specialization in the economy, thereby multiplying the capital savings of countries. To put it differently, the "invisible hand" which operates according to the law of nature ensures social order and paves the way for enrichment; thus, there is no need for government intervention. An intervention disrupts the natural functioning. David Ricardo, one of the advocates of the same thought system, supported and advanced Adam Smith's theory of "Absolute Advantage" with his theory of "Comparative Advantages". In his "On the Principles of Political Economy and Taxation" published in 1817, David Ricardo defended the advantages of foreign trade to countries. Firstly, he emphasized that the expanding market and the resulting increase in production lead to an increase in specialization and labor force, thereby boosting productivity and reducing the cost of production per unit. Secondly, he underscored that international competition reduces the monopoly power of domestic producers and force them to design and achieve higher production yields. Finally, he noted that consumers are able to buy a wide range of products at low prices and benefit from the increased purchasing power for their limited incomes (Abboushi, 2010). The advocates of free foreign trade from Ricardo to the present day have highlighted the advantages of the aforesaid liberalization of foreign trade to the parties and sustained their efforts into the removal of obstacles to the liberalization of trade. In a nutshell, the Mercantilist understanding that total wealth is stable and all countries cannot gain in the foreign trade (one country's gain is another's loss) was replaced by the understanding that total wealth is unstable and all countries may gain with the liberalization of foreign trade. This thought held sway until the Great Depression of 1929.