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CEPAL REVIEW
August 1979

Comtemporary protectionism and the exports of developing countries

*Gary P. Sampson**

It is an undeniable fact that in recent years protectionism has increased in the developed countries, with all its harmful consequences for international trade and the development of the periphery.

Since this is an established fact, it appears to be worthwhile studying the arguments used by the centres to justify it, and the means by which they put it into practice. In dealing with the first of these points the author concentrates on two "pressures" towards protection: the desire to attain balance-of-payments equilibrium, and arguments that imports from the peripheral countries "disrupt" factor and product markets in the centres; and he demonstrates, with a wealth of illustration, that these arguments are not very convincing.

In this treatment of the second point —the nature of protection— he presents in orderly fashion the various instruments currently used to establish protection. He analyses the quantitative restrictions, such as the so-called voluntary measures, orderly marketing arrangements and organized free trade, as well as the qualitative ones, including price limits and governments subsidies to enterprises hurt by imports.

In the face of this bleak picture, the author suggests a number of measures which would help to redirect this "neomercantilist" tendency in the centres and alleviate its effects on the periphery. He is aware, however, that it is not easy to arrive at solutions since, in the last analysis, everything depends on the prevailing power relations in international trade.

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Contemporary protectionism and exports of developing countries

For some time there has been a growing concern over the return to protectionism. This prompted Johnson to base his 1973 Presidential Address to the British Association for the Advancement of Science on the "New Mercantilism".[1] Last year the General Agreement on Tariffs and Trade (GATT) found it necessary to restate the case for maintaining an open economy in times of recession,[2] while the McCracken Report,[3] after attributing much of the post-war growth in OECD countries to an "open multilateral system for international trade and payments" warns of the "danger that the edifice of free trade, so carefully built, may begin to disintegrate".[4] For developing countries, the importance of market access for their exports to developed countries has long been recognized, and has recently received new support from several empirical studies.[5]

Nevertheless, it is not difficult to establish that there is a growing incidence of protection in developed market economies. Recent protection is perhaps even more difficult to "measure" than it has been in the past,[6] but opinions have been formed as to its importance. In forming these opinions the importance of new barriers to imports from developing countries is frequently played down, as it is argued that it principally affects the "star performers" who are doing very well anyway.

[1]H. G. Johnson, "Mercantilism: Past, Present and Future", in H. G. Johnson (ed.), *The New Mercantilism*, New York, St. Martins Press, 1973.

[2]GATT, *Trade Liberalization, Protectionism and Interdependence*, R. Blackhurst, N. Marian and J. Tumlir, Geneva, 1977.

[3]OECD, *Towards full employment and price stability*, (The McCracken Report), Paris, 1977.

[4]*Ibid.*, p. 11.

[5]For a discussion of the results of theses studies, see A. Krueger, "Effects of exports from new industrial countries on U.S. industries", in W. Kasper and T. G. Perry (eds.), *Growth, Trade and Structural Change in an Open Australian Economy*, Centre for Applied Economic Research, University of New South Wales, 1978; and B. Balassa, "Exports Incentives and Export Performance in Developing Countries: A Comparative Analysis", World Bank, *mimeo.*, 1977.

[6]Many of the difficulties relate to the nature of recent protectionist measures imposed. This will be returned to at a later stage in the paper.

Eight developing countries accounted for 78% of the increment in developing country manufactured exports to developed market economies between 1970 and 1976. As far as pressures for increased protection are concerned, a great deal of importance is frequently attached to the low level of economic activity in industrialized countries and the concomitant excess capacity of labour and capital as factors of production.[7] The implication, whether explicit or implicit, is that higher growth rates would be coupled with both less forceful demands for protection and less willingness on the part of national authorities to succumb to these pressures.

While one should avoid "crying wolf" at any increase in protection, particularly in times of economic slack, it seems there are legitimate grounds for concern on the part of developing countries and sound reasons for considering the above views on recent trade restrictions to be unduly optimistic. Such views frequently ignore the existing state of protection to which the new obstacles to trade should be added, narrowly define protection as restrictions on imports and neglect the problems associated with removing any trade obstacles once they are mounted. Similarly, little attention appears to be paid to the type of protectionist measures being resorted to in recent years.[8] Tariffs are now unpopular and preference is given to non-tariff barriers which have a long and unsuccessful history in multilateral trade negotiations directed to reducing trade barriers.

As far as the level of economic activity in industrialized countries is concerned, it is also possible to assign to it an important, but not dominant, role in the recent increase in protection. Growing rigidities in factor markets of the OECD countries have been lamented, and there appears to be greater unwillingness on the part of OECD governments to give up some chosen share of the domestic market of an increasing number of non-strategic industries.[9] If this is so, a more dramatic (but legitimate) interpretation of what is taking place today would consider recent changes in commercial policy to be the tip of an iceberg. What is at stake is access to the markets of the eighties. The problem is in reality nothing less than deciding who will produce what in the future with all its associated ramifications, and import controls are only one of a multitude of policy tools being drawn on to implement the decisions. Viewed in this context, the fact that only the "star performing" developing countries are affected by recent changes in commercial policy is a measure of the importance of the recent protectionist policies and not the contrary. If just a handful of developing countries can be the source of considerable market disruption, what does the future hold as more developing countries reach some sort of industrial maturity.

If one views recent developments in commercial and other domestic policies against the backdrop of existing protection, its importance lies in its closing off many areas which hitherto received relatively liberal treatment in international trade. This is particularly important for developing countries. Certain areas where they have long held a clear comparative advantage have been tightly controlled, as major importing industrial countries sought time to structurally adjust their threatened sectors.

Agricultural markets in food-importing developed countries have always been closely regulated and there has only been limited market access for developing country products.[10] While only last year tariffs on non-competing tropical products were partially reduced, these concessions are currently withheld by the U.S. until

[7]O. Long "The Protectionist Threat to World Trade Relations", *Inter Economics*, November-December 1977, for example, points to the role of the recession in increasing demands for protection and the role of protection in prolonging the recession.

[8]A notable exception is the comprehensive discussion to be found in UNCTAD, *Growing Protectionism and the Standstill on Trade Barriers Against Imports from Developing Countries*, TD/B/C.2/194, Geneva, 1978.

[9]OECD, *Textile Industry in OECD Countries*, Paris, 1977.

[10]For a discussion of trade barriers facing developing country agricultural exports to Sweden, see G. P. Sampson and A. J. Yeats, "Do Import Levies Matter: The Case of Sweden", *Journal of Political Economy*, Chicago, Ill., Vol. 84, N.° 4, part 1, 1976, and for imports of food and agricultural products under the Common Agricultural Policy (CAP), see Sampson and Yeats (1977).

See G. P. Sampson and A. J. Yeats, "An Evaluation of the Common Agricultural Policy as a Barrier Facing Agricultural Exports to the European Economic Community", *American Journal of Agricultural Economics*, Menasha, Wisc. Vol. 59, N.° 1, February 1972.

reciprocity is received.[11] Such trade barriers have frequently been imposed due to the special structural problems facing the agricultural sector.[12] Similarly, exports of cotton textiles and clothing have been restricted since 1962, because, as with agriculture, developed market economies sought time to structurally adjust these sectors of production.[13] The voluntary export restraints which emerged in the late fifties and early sixties were institutionalized in the LTA. This "temporary" agreement adopted a broader commodity coverage and tighter controls under the Multifibre Arrangement (MFA) in 1973.[14] Given the importance of exports of agricultural products, textiles and clothing to developing countries, arrangements such as CAP and the LTA have long been a source of grievance.

Always implicit, however, was the belief that developing countries should concentrate their efforts on producing those manufactured goods for export where developed market economies did not face the same structural problems.[15] However, new restraints are now found on many manufactured goods which previously received liberal treatment in international trade. Manufactured goods exported by developing countries and subject to new quantitative restrictions include non-cotton textiles and clothing, footwear, electronics, mechanical and engineering goods. These sectors currently face structural problems in many developed market economies, as do steel products and shipbuilding-areas of some current importance and considerable future importance for developing countries.

As the continuation of the LTA and other domestic support schemes through the sixties indicates, even in times of economic buoyancy it is difficult to change the structure of production. Labour and capital resist changes that are necessary to ensure that they are efficiently employed in areas of the economy where they are internationally competitive. In periods characterized by anything less than economic buoyancy, it appears that structural change is almost impossible. The important question to address, however, is how much of the recent protection is due to low levels of aggregate demand, and how much is due to growing rigidities and distortions in factor markets and a political desire to maintain internationally uncompetitive industries regardless of economic costs. The paucity of *positive* structural adjustment programmes in many developed countries and the proliferation of domestic support schemes seems to point to a lack of political will to change the structure of production.

Thus, in summary, for structural adjustment to take place it appears necessary to have more than a favourable economic climate. The true motive behind the protection is of crucial importance, for mercantilist protection requested as temporary assistance to adjust structurally has a history of becoming rapidly institutionalized and permanent. Competing with domestic developed country producers and other developed country exporters on anything other than economic grounds holds little promise for developing countries. The problem which emerges for developing countries is how to select those products to develop for export. Uncertainty now surrounds future market access, and uncertainty is perhaps the most effective non-tariff barrier to trade.[16]

The purpose of this paper is to investigate

[11]T. Ibrahim, "Developing Countries and the Tokyo Round", *Journal of World Trade Law*, London, Vol. 12, N.° 1, January-February, 1978.

[12]The European Economic Community (EEC), for example, adopted the Common Agricultural Policy (CAP) in 1962 to gain the time necessary to structurally reorganize the agricultural sector; to raise productivity and increase international competitiveness. Nevertheless, the *ad valorem* incidence of variable levies on grain imports are currently at an all time high.

[13]The U.S., for example, has since 1962 negotiated voluntary export restraints under the Long Term Arrangement Regarding International Trade in Cotton Textiles (LTA) to gain *temporary* relief and to facilitate the shifting of labour and capital to more internationally competitive areas of the economy.

[14]The EEC has recently broken with the MFA to unilaterally impose stricter measures, and some countries are now being faced with quota reductions.

[15]A clear statement of the mood of the late sixties as to the advantages of outward-looking export orientated growth strategies for developing countries can be found in D. B. Keesing, "Outward Looking Policies and Economic Development", *Economic Journal*, London, June 1967.

[16]The role of uncertainty in distorting trade flows is discussed in GATT, *Trade Liberalization...*, *op. cit.*

some aspects of the new protectionism which may be of interest to developing countries. The paper focusses on the contemporary sources of protectionist pressure and the *nature* of the protection itself, as such an investigation facilitates the discussion of the principal points raised above. The paper closes with a conclusion and policy recommendations.

I
Pressures for protection in developed market economies

In 1970, Baldwin considered fixed exchange rates and structural adjustment problems to be the major sources of protectionist pressures and resistance to trade liberalization: "Greater exchange-rate flexibility and much more effective adjustment assistance are the two most crucial needs if the major trading nations are to achieve a significant increase in the mutual benefits of international trade... Exchange-rate flexibility is needed not only to ease balance-of-payments pressures when balanced cuts in trade barriers are not possible but, even more importantly, to prevent the substitution of trade distorting commercial policies for exchange-rate policy".[17]

Today exchange rates fluctuate widely and despite OECD-sponsored declarations to the contrary, member countries still use commercial policy for balance-of-payments purposes. In addition, national legislation in many countries now provides funds for industries suffering from import competition, but industry-specific protection is growing.

1. *Balance of payments*

The orthodox role of the exchange rate in macro-economic models of internal-external balance is to switch factors of production and expenditure between the traded and non-traded goods sectors of the economy. The switch is brought about by a currency realignment, and the extent of the relative price change in the two sectors is a measure of success of the realignment.[18] When the change in the exchange rate is coupled with the appropriate absorption-changing policy, internal and external balance can be secured-commercial policy is not needed to ensure external balance.

Recent developments in the literature provide numerous explanations of why fluctuating exchange rates do not live up to their expectations, and nothing more than a cursory discussion is varranted here.

Consider a country which is a price taker on world markets facing a balance-of-trade deficit and internal balance.[19] The appropriate policy then would be to devalue and reduce absorption. However, the devaluation may not lead to the relative price change of tradeable and non-tradeable goods. There may, for example, be real wage resistance to the devaluation-induced price increase and the resulting fall in real wages.[20] If the reduced absorption is to be secured by a tax increase on wage earners, for example, attempts to force a return of the direct payment of the post-tax real wage to the original level may negate the absorption reduction policy.

Also, as Corden has pointed out, there may

[17]R. Baldwin, *Non-Tariff Distortions of International Trade*, Washington D.C., The Brookings Institution, 1970, pp. 17 and 18.

[18]W.M. Corden, *Inflation, Exchange Rates and the World Economy*, Oxford, Clarendon Press, 1977; and R. Dornbush, "The Theory of Flexible Exchange Rate Regime and Macro-economic Policy", in *Scandinavian Journal of Economics*, Stockholm, Vol. 78, No. 2, 1976.

[19]Capital flows are ignored, but the analysis that follows would not be greatly changed with their inclusion (see Corden, *op. cit.*, p. 42). It is also assumed that the partial equilibrium price elasticities for the demand and supply for imports and exports are such that one would expect an improvement in the balance of trade following a devaluation.

[20]See R. H. Snape, "The Impact of Inflationary Recession in Developed Countries on the Developing World", *UNCTAD*, mimeo., Geneva, 1978.

even be increased pressures for protection.[21] If the real wages claimed by wage earners are above the marginal product at full employment, this is inconsistent with internal balance. To meet such real wage claims requires a redistribution of income —a redistribution which can be achieved through quotas or other commercial policy. If the import-competing sector is labour intensive and the export sector capital intensive, protection of imports would achieve a price effect similar to that of a (successful) devaluation, but also a redistribution of incomes from profits to wages. The latter effect would not result from a devaluation.

The foregoing analysis assumes that switching is appropriate as some structural change is necessary. It can be argued that exchange-rate changes may be monetary phenomena that do not indicate real changes in a country's competitive position. A currency realignment will not remove the source of imbalance in the balance of payments if imbalance is due to an excess domestic demand for money over the receipts of foreign money —an excess that can only persist if supported by domestic monetary policy. For these and other reasons, fluctuating exchange rates may not secure external balance and do not remove the need for commercial policy for balance-of-payments purposes.

Thus, twenty-four countries were applying import surcharges and sixteen had import deposit schemes in effect for at least part of the period 1970-1974. All were member countries of GATT operating outside of the appropriate regulation (Article XII) in which any measure other than a quota is outlawed as a control device to regulate balance of payments.[22]

Indeed, in view of the above discussion, it is not secret why import deposit schemes, for example, are so attractive. Under such a scheme, an importer is required to lodge a certain percentage of the value of the import in a frozen account at the reserve bank. This makes importing less attractive (and indeed imports more expensive), and if there is not a complementary increase in the money supply, there is a reduction in absorption following the blocking of funds with the central bank. The joint objectives of lower imports coupled with reduced absorption are thus assured without direct market price changes and direct monetary and fiscal action.

The use of commercial policy for balance-of-payments purposes, however, does not appear to be a source of protection likely to cause particular concern for developing countries. It appears to be restricted to small countries which act unilaterally and in a non-discriminatory fashion by invoking measures which are essentially temporary in nature.[23] What is perhaps useful to speculate on, however, is the possibility that fluctuating rates in fact are the source of some demands for increased protection for non-balance-of-payments reasons.

In discussing an argument which he attributes to Mundell and Laffer, Corden points to the fact that a floating exchange rate may lead to rate fluctuation induced by capital movements. Changing expectations and divergent interest-rate policies cause portfolio preferences of asset holders to switch between important currencies.[24]

For these and other reasons, small countries see the value of their own currency fluctuating against that of their major trading partners. Thus, governments intervene to bring some sort of stability into their effective exchange rate. Over the period September 1974 to July 1976, the Australian government intervened to maintain a constant effective exchange rate. Over the same period, however, there were large differences in country-specific exchange rates. The U.K. and New Zealand are both important trading partners for Australia, and both these currencies devalued 24

[21]W.M. Corden, *Inflation, Exchange rates..., op. cit.*, p. 31.

[22]See F.C. Bergsten, "Reforming the GATT: The Use of Trade Measures for Balance of Payments Purposes", *Journal of International Economics*, Vol. 7, No. 1, February. 1977.

[23]While developing countries are major offenders in using commercial policy for balance-of-payments purposes, Bergten, in calling for a major revision of Article XII, has argued convincingly that developing countries do in certain circumstances have the right to use commercial policy for this purpose. See "Reforming the GATT...", *loc. cit.*

[24]W.M. Corden, *Inflation, Exchange Rates..., op. cit.*

per cent against the Australian dollar over the period. To the extent that import agents refrain from taking a windfall gain and do, in fact, pass on the currency change in lower prices, fluctuating exchange rates do provide a source of "industry disruption" protectionist pressure.[25] As far as foreign currency revaluations are concerned, however, there is unlikely to be any symmetry in demands for reduced protection, as consumer interests are notoriously diffuse and domestic producers of importables have the option of increasing prices or expanding their domestic market share.

2. *Market disruption*

Of considerable concern to developing countries, particularly the emerging producers of manufactured goods, is the protection that is granted in response to claims that the imports from these countries are disrupting domestic markets. For exporters there are two important considerations that should be noted. While safeguard action is both necessary and appropriate in many circumstances, there should be some guarantee that this safeguard action is temporary and takes into due consideration the disruption in the exporting market that follows the imposition of the protectionist measure. Secondly, it should be clear that it is in fact the imports from the developing country that are responsible for the market disruption. Before discussing these considerations in some detail, it is necessary to have a clear idea of how markets are disrupted.

Presumably the only market disruption that concerns the authorities in the importing country is that which occurs in the factor markets. Importing cheaper (non-strategic) products may not be a problem in itself, but if it results in unemployed labour and capital there is cause for concern. Within this context it is important to draw the distinction between over-capacity in capital and redundancies of labour that result from the low level of economic activity, and those that result from structural changes of a more micro nature. In the first case, the role of protection is clear —there is a bolstering of the domestically produced share of importables at the expense of the foreign suppliers. The domestic problems associated with insufficient demand are exported to the foreign supplier. Pressures are then felt on "third markets" as alternative outlets are sought.

The second case is less clear as there are many sources of structural change in both product and factor markets.

(a) *Factor market disruption*

— Factors may become unemployed if, with an unchanged production function, long-term relative price changes lead to factor substitution. Real wages moving ahead of labour productivity may result in substitution away from marginal workers and an increase in the capital-labour ratio. Labour will remain unemployed until real wage claims and marginal products move closer into line, or new investment results in job openings where real wage claims are warranted.[26]

— There may be technical change which shifts the production function neutrally and bears equally on all factors needing less inputs for a given output. Factors remain unemployed until the level of output (demand) increases.

— Biased technical change may lead to changing factor proportions (substitution) with a given factor-price ratio. As with the preceding case, an increase in output (demand) is necessary to return to full employment.

b) *Product market disruption*

— Factor markets may be disrupted due to changes in the product market.

— The pattern of demand may change due to a change in tastes, indirect taxes, etc.

— A product may come on the market

[25]Within this context it is interesting to note exceptions such as the extent of protection granted to U.S. industries competing with Japanese goods. In April (1978) the President imposed a 21 per cent tariff on imported citizen band radios comming from Japan and negotiations are underway to secure voluntary export restraints from Japanese car exporters. Due to the revaluation of the yen, Toyota increased its prices in April for the third time in six months bringing the total average price increase for its products over this period to 21 per cent. (*Financial Times*, April 18.)

[26]See R. H. Snape, "The Import of Inflationary Recession...", *op. cit.*

which is more competitive in price. This may be supplied by domestic producers, foreign developed-country exporters or developing-country exporters.

The interesting feature which emerges is that the only role developing countries can play in disrupting domestic markets is indirectly through the product market as one of the suppliers of more competitively priced goods. Even here their role may be secondary, since their comparative advantage may improve due to a relative improvement in their own cost structure, or a worsening in the cost structure in the importing country. What is important is that before protection is implemented, the true source of market disruption should be identified. It has been suggested that imports from developing countries are frequently used as "scapegoats" for internal structural problems.[27] Similarly, for a variety of sociological reasons, government officials feel comfortable in protecting domestic labour and capital from "cheap imports from developing countries".[28]

The extent to which developing countries are a source of market disruption is an empirical question. Krueger has found that import growth has not been a significant factor affecting the growth of output and employment from 1960-1975 in the U.S.[29] Cable has arrived at similar conclusions for the U.K.[30] He estimated that jobs lost in the U.K. footwear industry during 1970-1975 due to net import penetration amounted to only 0.4 per cent of employment, and in the clothing industry, where the loss of jobs was highest, the loss was 1.7 per cent of total employment. In fact, in no labour-intensive sector, except men's shirts and suits, did output suffer from import growth. A recent study for Germany has revealed that if there were increased penetration by manufactured imports from developing countries, the associated growth in exports to developing countries would mean that there would be no net loss of jobs.[31]

[27] A. Krueger, "Effects of Exports...", *op. cit.*

[28] V. Cable, "British Protectionism and LDC Imports" in Overseas Development Institute Review, N.° 2, 1977.

[29] A. Krueger, "Effects of Exports...", *op. cit.*

[30] V. Cable, "British Protectionism...", *loc. cit.*

[31] UNCTAD, "Growing Protectionism...", *op. cit.*

Interesting data on the penetration of the exports of developing countries in developed country markets can be found in the UNCTAD *Handbook of International Trade and Development Statistics* (table 7.1). Developing country imports are expressed as a share of total apparent consumption in major developed country markets and the data are reported for 14 major product groups in the EEC (6), U.K., Japan and the U.S. over the period 1959-1960 to 1975. If agriculture, fuels, mining and clothing are excluded, developing-country imports comprise considerably less than 6.5 per cent of apparent consumption for all product groups, all countries and all years. While there is a tendency for the share of developing-country imports in domestic apparent consumption of the group of countries as a whole to increase over the period (from 3.3 per cent to 6.2 per cent), this increase is largely due to the increase in fuels and other primary products (11.6 per cent to 24 per cent). Where disruption may be expected to follow increased market penetration is in the manufactured goods sector. Here, imports as a share of domestic consumption increased from 1.2 per cent to a meager 2.0 per cent over the fifteen year period.

Within the manufacturing sector of developed countries it appears that one of the areas where disruption has been most severe is the clothing and textiles sector. As exports of clothing and textiles from developing countries have long been controlled under multilateral agreements, and have recently been the object of new and more restrictive measures, a close look at some relevant statistics appears to be warranted.

The total imports of textiles by developed market economies grew from 11 to 19 billion dollars between 1972 and 1976. Imports of clothing grew from 7.5 to 15.5 billion dollars over the same period. In 1976, only 13 per cent of the imports of textiles were supplied by developing countries and 39 per cent of clothing imports. Developing countries did not secure an increased share of the increased value of trade in textiles over this period, and in clothing only raised their share of the increased trade value by 16 per cent. Developed countries were the source of over 75 per cent of the increased imports of textiles into developed countries between 1975 and 1976 and 40 per cent of the increase in clothing imports. Developed countries, however, are not subject to controls under the new MFA.

For the U.S. over the period 1972 to 1976, total exports of textiles grew more rapidly than imports of textiles from developing countries, while total clothing exports and clothing imports from developing countries grew at the same rate. Of some additional interest is the fact that developing countries are net importers of the intermediate goods and raw materials for the manufacture of clothing and other textile goods. In 1975, the U.S. had a one-billion-dollar trade surplus with developing countries in textile fibres (SITC 26) plus textile machines (SITC 717).

As far as the domestic market shares are concerned, the UNCTAD *Handbook* reveals that in the United States, for example, imports of textiles from developing countries accounted for less than 2.5 per cent of apparent domestic consumption in 1975 and less than 10 per cent of consumption of clothing in the same year. In the U.K., for example, where import penetration in clothing is the highest (13 per cent in 1975), it is interesting to note that exports were 18.7 per cent of apparent consumption in the same year.

While it is difficult to accept that textiles and clothing imports from developing countries warrant the severe treatment that has recently been imposed under the MFA (1974 and 1976), one cannot deny the often repeated claims that textile and clothing markets in OECD countries are "disrupted". Clearly of importance is the penetration of markets classified at a more disaggregated level. The EEC, for example, has frequently referred to unemployment created by cheap imports of sensitive products from developing countries. Textile and clothing products have been classified accordingly —the sensitive products frequently being labour-intensive clothing.

Within the context of the earlier discussion, however, it is interesting to note if other sources of market disruption are present. While this is a subject for a lengthy and detailed empirical investigation, suffice it to point to the fact that in recent years there has been massive investment in labour-intensive clothing production in the EEC and OECD countries generally. The result has been enormous increases in labour productivity in clothing manufacture. The figures below for all apparel excluding footwear, are aggregative but illustrative.

CHANGES IN LABOUR PRODUCTIVITY OF CLOTHING MANUFACTURE 1970 TO 1975

(1970 = 100)

Germany	124.7
Belgium	131.6
Netherlands	135.0
United Kingdom	144.4
United States	123.3

Source: Percentages calculated from output and employment data in OECD (1977), *Textile Industry in OECD Countries*, Paris.

In the U.K., for example, a failure to increase output of clothing over the period 1970-1975 would result in unemployment of 40 per cent of the work-force. As outlined above, labour productivity increases may be due to technical change or a substitution away from labour following real wage increases. What is sure is that it is *not* due to imports from developing countries.[32]

Re-employment of labour means locating displaced workers in other industries, or expanding the market —more can be exported, domestic consumption can be increased or imports can be reduced. The EEC appears to be favouring the final alternative to the detriment of developing countries. Current negotiations on clothing are outside the MFA and thus the GATT framework, the result being that new restraints on developing-country exports involve a *reduction* in previously established quotas.[33]

[32]Where the imports of developing countries may play a role is by forcing modernization, etc., of existing equipment through supplying competitive products.

[33]Quota reductions for exports from Hong Kong, Taiwan and South Korea to the EEC are reported in the *Financial Times*, 6 January 1978.

Given data such as these, it is reasonable to ascribe an alternative role to the MFA — quite different to the spirit in which it was signed. Instead of looking for a breathing space to phase out internationally uncompetitive products, the MFA may be used to secure time to increase productivity in the domestic industry and achieve international competitiveness. If this is not achieved, the vested interests of the "interest groups" are strengthened and *protection is institutionalized.*

In this respect the role of the government in recent years has been an interesting one. There is an increasing unwillingness of governments to allow the decline of uncompetitive industries. While there is a role for governments in devising *positive* structural adjustment schemes, protection coupled with domestic subsidies is more frequently the rule of the game. Thus in France there has been massive support schemes for the outdated Boussac textile empire through deferred social security payments, subsidized loans, etc. Similarly, the Temporary Employment Subsidy subsidizes salaries for 250,000 workers in the U.K., most of which are located in the clothing, textiles and footwear industries.

II
Nature of protection

The characteristic which is common to almost all the recent increases in protection in developed economies is that they have proved virtually impossible to negotiate away within the existing institutional framework established for multilateral trade negotiations (MTNs). Indeed, this may be one of the important explanations of the changing nature of protection, for in an increasingly interdependent world, governments take measures to achieve the autonomy they feel they are losing in areas such as international trade.[34]

In successive rounds of MTNs conducted under the auspices of GATT, considerable success has been achieved in reducing most favoured nation (MFN) tariff rates. There are at least three reasons why tariffs are good material for multilateral negotiations. Firstly, the data are recorded in national schedules and freely available to all. Secondly, their *ad valorem* incidence is known (or can be calculated) so they can be compared with other country tariffs, fed into tariff cutting formulae, etc. Finally, governments appear willing to reduce tariffs. There are numerous reasons why this is so. A cynical approach is to suggest that tariffs are blunt instruments, slow to act with an uncertain outcome.[35]

There are innumerable ways in which trade flows can be distorted.[36] It is not the purpose of this section of the paper to discuss trade distortions as such, but rather to attempt to discern if there is a trend in the use of contemporary protectionist devices.[37] It would appear that there is. Firstly, there is a "hardening" in commercial policy that comes with a move away from tariffs to direct price and quantity controls. Voluntary export restraints are just country-specific quotas and minimum import prices (with penalty duties) are sliding-scale tariffs. Quotas certainly have a long history, and sliding-scale tariffs date at least from the Corn Laws. Secondly, there would appear to be increasing government involve-

[34] R.N. Cooper, *The Economics of Interdependence: Economic Policy in the Atlantic Community*, McGraw-Hill Book Company, 1968. A. Lindbeck (1977), "Economic Dependence and Interdependence in the Industrialized World", *Seminar Paper* N.º 83, Stockholm, Institute for International Economic Studies, June 1977.

[35] Ohlin G. (1968), "Trade in a Non-Laissez Faire World", in P. Samuelson (ed.) *International Economic Relations*, Macmillan, London. H.G. Johnson, "Mercantilism: Past, Present, Future", *op..cit.*

[36] For a definition of terms such as trade distortion and non-tariff barrier to trade, see R. Baldwin, *Non-Tariff Distortions of International Trade*, Washington D.C., The Brookings Institution, 1970. For a comprehensive classification of trade distorting devices, see A. J. Yeats, *Trade Barriers facing Developing Countries*, MacMillan. At Press.

[37] Any detailed discussion of recent changes in commercial policy is extremely tedious. A large proportion of trade restraints are bilaterally negotiated so the list is long.

ment which directly affects the working of the market. More responsibility appears to be taken by governments in deciding which industries should flourish or survive and a wide variety of industries now appear to be considered by governments to be in their realm of responsibility.

1. *Quantitative restrictions*

Broadly speaking, recent quantitative restrictions are bilaterally negotiated by GATT member countries without passing through the appropriate GATT channels.[38] With some exceptions, quantitative restrictions are outlawed by GATT (Article XI) and country-specific non-MFN treatment runs contrary to the whole GATT philosophy (Article I).

New quantitative restrictions frequently carry the title of "voluntary export restraints", "orderly marketing arrangements" or "organized free trade", but are simply quotas agreed to under the threat of more restrictive action. Normally they are "safeguard action" in the face of the threat of market disruption. GATT is bypassed because the appropriate safeguard article of the Agreement (Article XIX) is considered too restrictive by many member countries, and a softer interpretation of the threat of market disruption is frequently found in national legislations.[39] Furthermore, safeguard action within GATT has to be applied uniformly to all member countries, but it appears that country-specific treatment is preferred. Finally, such safeguard action has to be temporary and the duration of the restriction is monitored by GATT.

Quotas have proved extremely difficult to negotiate away in GATT. Perhaps this is due to the fact that they have, in recent years, been traditionally applied to agricultural products —an area where GATT has achieved few positive results. This may be due to the nature of the restriction itself and the difficulties of trading concessions in negotiations, or perhaps because quotas are frequently imposed as safeguard action. Even more important for future negotiations, however, is the fact that a comprehensive file of recent restrictions does not exist. Many are not recorded by GATT and in some instances not even by national authorities in the importing country.[40]

Also of importance is the fact that many recently negotiated export restraints only involve varying degrees of government involvement. They are briefly discussed below.[41]

(a) *Voluntary export restraints*

Voluntary export restraints may be bilaterally negotiated between industries in importing and exporting countries with minimum government support. Implementation is left to the industry in the exporting country. There may also be government-to-government intervention, but again with the implementation left to agreement among the exporters in the exporting country. Then, there are voluntary export restraints negotiated under the umbrella of intergovernmental bilateral or multilateral agreements, and which involve direct action by the government in the exporting country to regulate quantities and/or prices of the exports concerned.[42]

[38] There are of course exceptions, and details of recourse to Article XIX, etc., can be found in various issues of *GATT Activities*. It should be added however that movement outside of the GATT Articles is not new and historically, selected products and countries have been excused. There have always been quantitative restrictions on agricultural imports to the EEC. In fact, the formation of the EEC itself was contrary to GATT rules. Similarly, non-MFN quantitative restrictions on textiles and clothing have been imposed by developed countries and formalized with GATT under the LTA.

[39] J. N. Bhagwati, "Market Disruption, Export Market Disruption, Compensation and GATT Reform", *World Development*, Oxford, Vol. 4, December 1976.

[40] In the U.S., for example, voluntary export restraints are not recorded in the Federal Registry as they are considered a trade restriction imposed by the trading partner. See T. Murray, W. Schmidt and I. Walter (1978), "Alternative Forms of Protection Against Market Disruption", *mimeo, 1978*.

[41] For a comprehensive discussion of these protectionist devices, see UNCTAD, "Growing Protectionism...", *op. cit.*

[42] Export restraint by Japanese motor vehicle exporters to the U.K. is an example of a restraint resulting from intercompany consultations, while Korean footwear exports to the U.S. were restrained as the result of intergovernmental consultations.

(b) *Orderly marketing arrangements*

As already indicated, the extent of government involvement in "voluntary" export restraints varies. In the case of orderly marketing arrangements, government intervention is explicit and formal, with specific agreements being negotiated between exporting and importing countries. Under such agreements, the exporting country agrees to restrict to specified levels exports which are causing or threatening to cause serious injury to the importing country's industry.[43]

(c) *Organized free trade*

The concept of organized free trade is gaining in popularity, but there is no clear statement of what this seemingly contradictory group of words means. However, some of its main features are already evident. Organized free trade would envisage market-sharing arrangements at the sectoral level under a global umbrella which would limit to specified levels imports of competitive foreign goods. The organized free trade concept implies essentially "orderly marketing arrangements" on a global scale and its adoption would thus amount to an institutionalization of the commercial policy device described and would confer on it the status of an internationally accepted practice.[44] Bilateral and multilateral agreements regulating trade in textiles provide a clear illustration of orderly marketing arrangements.

III
Implication of new quantitative restrictions

Tariffs are preferable to quotas for a host of well-known reasons.[45] In view of the recent interest expressed in the growing interdependence of nations and the return to protection to gain greater control over the national economy, one or two specific points are worthy of note. Quantitative restriction of the type described can introduce greater *uncertainty* into world trade than tariffs. Tariff rates are recorded in national schedules, so import prices are known in advance. To the extent that they are applied in a most-favoured-nation fashion, all countries face the same barriers and can assess their competitive position. Similarly, tariff changes are traditionally negotiated in GATT so changes in competitive positions are common knowledge. To the extent that a country participates in a bilateral quota, price certainty is replaced by quantity certainty. Non-participating countries, however, have neither price nor quantity certainty, and the trading "rights" of competitors for the import market are not always common knowledge. Furthermore, quantitative restrictions in general introduce greater price *instability* into world markets than tariffs.[46] While much has been written on the equivalence of tariffs and quotas, the definition of equivalance differs between authors. Corden[47] offers the most rigorous requirements —a single tariff rate which would have the same effect as an import quota on the volume and value of imports, on the domestic and foreign price, and on the volume of domestic output. Under the appropriate assumptions one can show equivalence as defined in this static sense. If, however, the import demand or export supply

[43]Marketing arrangements, for example, are in force between the U.S. and the Republic of Korea on certain non-rubber footwear; the U.S. and Japan, EEC, Sweden and Canada on stainless and alloy tool steel; the EEC, and Japan and the Republic of Korea on carbon steel; the U.K. and the Benelux countries and Japan on television sets, radios and calculators (see UNCTAD, "Growing Protectionism...", *op. cit.*).

[44]Ibid.

[45]The case for tariffs in preference to quotas has recently been very lucidly restated by T. Murray and I. Walter, "Quantitative Restrictions, Developing Countries and GATT", *Journal of World Trade Law*, London, Vol. 11, N.° 5, September-October, 1977.

[46]Developing countries have expressed considerable concern over price uncertainty in international markets as is evidenced by support for the UNCTAD multi-commodity price stabilization schemes.

[47]W. M. Corden, *The Theory of Protection*, Clarendon Press, Oxford, 1971, p. 212.

curve shift, the impact on world price is not the same for the tariff and quota. Regardless of which curve shifts and the direction of the shift, the world price fluctuations are greater with the quota than the tariff. The extent of the difference depends on the elasticities of the curves. As countries move to isolate themselves from world price fluctuations by using quantitative controls, they exacerbate future world price fluctuations —presumably increasing the "case" for protection.[48]

Voluntary export restraints and orderly marketing agreements virtually force firms in the exporting country to form cartels. Once the export market is carved up, the entry of new firms is extremely difficult —this is particularly important for new firms in developing countries. Nor does future market growth offer hopes for new firms as some export growth for the exporting firms is usually a condition of the voluntary export restraint. Price cutting through greater efficiency has nothing to do with market access and even the rent can be divided up in a gentlemanly way between quota holders in the importing country and exporters. Voluntary export restraints are acceptable to established exporters, importers, import competing firms and governments wishing to increase autonomy without being bothered by GATT. It is no secret why their incidence is spreading.[49]

Similarly, voluntary export restraints and orderly marketing arrangements encourage cartelization in the importing country. As the government intervenes to deal with the problems in the industry by negotiating export restraints on behalf of the affected firms, it has expanded its intervention and sometimes even encouraged the formation of cartels. Major European makers of synthetic fibres have recently announced their plants to establish a three-year production cartel. This move was initiated by the EEC Industry Commission.[50] Similarly, the Swedish government, after negotiating voluntary export restraints for Swedish steel, has now dropped its theoretical opposition to mergers and is offering loans and guarantees to sponsor the merger of three of Sweden's biggest special steel firms.[51]

But perhaps most important for developing countries is that it is largely bargaining power which determines whether a claim for voluntary export restraint receives government approval in the importing country. Government support depends on the political clout of industry leaders.[52] How individual developing countries fare in securing a share of the import market also depends on bargaining power. The lack of success of developing countries in trade negotiations where bargaining power is important (e.g., Kennedy and Dillon Rounds) does not auger well for their obtaining benefits from future trade restrictions of the "voluntary" type.

1. *Price restrictions*

The setting of minimum import prices has much in common with quantitative restrictions. In fact, given the domestic demand and supply schedules for a product, a fixed import price, set below the domestic market clearing price, establishes the quota. Such minimum import prices have long been applied to many agricultural imports into European countries (for example, all grains imported into the EEC) and more recently, steel products imported into the EEC and U.S.[53]

How these minimum import prices are administered is of some importance. For grains imported into the EEC, for example, an internal *target price* is set and a minimum import price (threshold price) is determined accord-

[48]Agricultural import quotas made possible by the use of a sliding scale tariff in the EEC are a classic case of a country isolating itself from world price fluctuations, but exacerbating such fluctuations, see G. P. Sampson and R. H. Snape, "Variable Levies, World Prices and their Instability", *mimeo*, 1978.

[49]It is with considerable foresight that Shibata predicted the future popularity of voluntary export restraints for very similar reasons. See H. Shibata, "A Note on the Equivalence of Tariffs and Quotas", *American Economic Review*, Vol. 58, March 1968.

[50]Reported in *Financial Times*, 8 February 1978 and *International Herald Tribune*, 3 May 1978.

[51]Reported in *Economist*, 11 March 1978.

[52]J. N. Bhagwati, "Market Disruption, Export Market Disruption...", *op. cit.*

[53]The importance of minimum import prices for agricultural products has grown with the expansion of the EEC.

ingly. The minimum import price is maintained by a sliding scale tariff —the EEC isolates itself from world price fluctuations and holds the target price constant. The sliding scale tariff extracts both the rent and the production or export subsidy that could go to the producing country. The rent is frequently substantial as evidenced by the fact that the *ad valorem* equivalent of variable levies on grains imported into the EEC in July of 1977 ranged between 88 and 161 per cent for the major grains. One would expect supplying countries to form cartels (as there are few major suppliers) but they do not. Protection in this case is rationalized on the basis of the desire to maintain, for social reasons, domestic inefficient farming regardless of economic costs. The U.S. minimum import price for steel products, however, is rationalized as protecting efficient domestic producers from dumping. The U.S. publishes its minimum prices (*trigger prices*) and invites foreign suppliers to sell at this price. Sales at less than this price trigger a lengthy and complicated anti-dumping enquiry. To avoid the anti-dumping enquiry, suppliers sell at the minimum price. If the major suppliers are simply more efficient, as they claim (particularly Japan), this mechanism (unlike the sliding-scale tariff) ensures exporters keep the rent.

Minimum import prices for agricultural products serve to reduce exports from developing countries. Domestic production is expanded in the importing country and high internal prices limit domestic consumption; by restricting demand world prices are depressed and, while it may be argued that food-importing developing countries benefit from low world prices, it should be noted that this form of protection destabilizes world commodity markets (e.g., in times of over-supply the EEC target price does not drop accordingly). Commodity price stability appears to be high on the priority list for developing countries.

New restrictions on steel will not affect most developing countries, which are at present high-cost producers. However, imports from the most efficient producers in developing countries, such as Korea, Brazil, India and Mexico, although they are minor suppliers, will probably be curtailed. Similarly, future access to major markets is likely to become increasingly difficult as minimum import prices are now being coupled with voluntary export restraints. The EEC, for example, has recently negotiated restraints with Japan, Sweden, Czechoslovakia, South Africa, Spain and Australia.

2. *Subsidies*

The most disturbing general feature about direct government assistance to industry is that it appears to be granted on an *ad hoc* basis with little consideration given to economic efficiency. Governments may simply wish to preserve industries that they judge desirable, regardless of economic costs.[54] There may be special problems, such as regional unemployment, associated with a scaling down of the industry,[55] or members of governments may simply be responding to political pressure.[56]

For developing countries, of principal concern is the long-term support given to industries where they have a comparative advantage at present (or will have in the future). In the EEC, for example, there are 9,500 shoe companies in small towns, supporting labour-intensive industries such as tanning. Automatic import licensing was introduced in May 1978 and voluntary export restraints have been negotiated. In addition, direct subsidy payments are now being paid to EEC shoe manufacturers.[57, 58] Under the temporary Employment Subsidy in the U.K., companies receive £ 20 per week (per worker) subsidy payable for a maximum of twelve months for each job "maintained", and a further £ 10 per week (per worker) for the ensuing six months should the company face further difficulties. To receive the payment it is

[54]H. C. Johnson, "Mercantilism: Past, Present, Future", *op. cit.*

[55]A. Krueger, "Effects of Exports from New Industrial Countries...", *op. cit.*

[56]This would appear to be of special importance in recent years as many governments in OECD countries hold rather tenuous majorities.

[57]Reported in *Economist*, 4 March 1978.

[58]It has been estimated that developing countries currently have an excess capacity of 100 million pairs of shoes per annum, (*Financial Times*, 20 March 1978).

necessary to prove that without a subsidy the worker would be redundant. The scheme currently covers a quarter of a million workers at a cost of a quarter of a billion pounds.[59] As already mentioned, what is disturbing for the developing countries is the fact that over one half of the workers are located in the clothing, footwear and textile industries. No provision is made in such schemes to move labour and capital to other sectors.[60] An area of less obvious, but potentially highly important export interest to some developing countries is shipbuilding —a heavily subsidized industry in OECD countries. A recent report indicates that if developing countries are using only half their production capacity in 1981-1982, they will have 30 per cent of the world market (compared with 5-6 per cent today). The report concludes that due to lower production costs, their growth is "unstoppable".[61]

Support for industries needing assistance in the face of import competition is formalized in many national legislatures. There has recently been an enormous increase in requests for trade adjustment assistance in many countries. In the U.S. for example, over the fifteen years from 1962-1975 there were 107 successful (i.e., formally approved) requests for assistance with resulting payments affecting 53,800 workers, and 36 firms. Between April 1975 and May 1977 there were 690 successful petitions affecting 209,100 workers and 78 firms.[62] While such figures would appear encouraging to exporters, it should be noted that most of the assistance measures serve to introduce greater rigidities by subsidizing the existing factors and discouraging the shift to other sectors. Furthermore, there has been an important change in the legislation. Under the Trade Expansion Act of 1962, it was necessary to prove that increased imports are "the major factor causing or threatening serious injury to the firm or its workers". Under the Trade Act of 1974 it is sufficient to prove that the "increased imports must be a substantial cause of the injury or the threat of such".[63]

IV
Policy implications and conclusions

Perhaps it is most useful to discuss the policy implications of the foregoing discussion within the context of the immediate, medium- and long-term future.

In the immediate future, it would appear that there is a proliferation of trade restrictions of the type mentioned above and very little can be done about it apart from drawing the attention of offenders to the consequences of their action.[64]

"Crying wolf" does have a role to play if the wolf is there, but is kept at bay. OECD-sponsored declarations on "standstills" appear to count for little and any institutional reform seems impossible before the completion of the current round of MTNs. Such institutional reform is necessary since even a "successful" completion of the current round of negotiations (within the existing structure of institutional arrangements) will leave unsolved many of the problems addressed above. It would appear that the most fundamental problem with respect to any "standstill agreement" is that no sanctions can be applied to offending parties, so pledges count for little.

[59] The estimates are reported in OECD, *Economic Surveys: United Kingdom*, Paris, March 1978, p. 53.

[60] Perhaps it should be mentioned that other special employment schemes introduced due to the "severity of the post-1974 recession", are the Job Release Scheme, Job Creation Programme, Work Experience Programme, Community Industry Scheme, Youth Employment Subsidy and miscellaneous training schemes. These schemes, however, are almost trivial when compared with the Temporary Employment Subsidy (OECD, *ibid.*).

[61] H. P. Drewy, *The Emergency of Third World Shipbuilding*, London, Brook Street, 1978.

[62] See H. R. Williams, "U.S. Measures to Relieve Injury caused by Import Competition: The Eligibility Test", *Journal of World Trade Law*, Vol. 12, N.º 1, January-February 1978.

[63] *Ibid.*

[64] See, for example, GATT, *Trade Liberalization...*, *op. cit.*

At the moment, countries are protecting their domestic markets but are not playing according to the rules of the game. It is clear that in the medium-term the rules have to be changed. The articles of GATT were devised as a code of conduct for countries wishing to liberalize trade restrictions and it appears they are poorly suited to countries' desires for increased protection. This is particularly so for safeguard action and the use of commercial policy for balance-of-payments purposes. In the formulation of any new safeguard clause, it is important that the true sources of market disruption should be identified and due consideration be given to disruption in the exporting country. In this area it has been suggested that developing countries be compensated for such disruption.[65] Such issues should find a place on the agenda of UNCTAD in May 1979, where it would seem reasonable for developing countries to ask for some assurance that uncompetitive industries in developed countries will be phased out, and not supported in what appears often to be a vain effort to regain international competitiveness. It would also seem reasonable that developing countries press for their receipt of the often substantial rent that is involved in current commercial trading transactions. The receipt of such rent could be written into the voluntary export restrictions that developed countries seem to insist on. This is true not only for quantitative restrictions on manufactured goods, but also for sliding-scale tariffs on agricultural products. Developing countries do not receive such rent under the current systems of generalized preferences. It would also seem reasonable and appropriate that UNCTAD draw attention to the "special and differential treatment" promised for developing countries in the Tokyo Round Declarations. As tariff preferences for developing countries will be further reduced following the current round of MTNs, a case could be made for developing country exemption from global quantitative restrictions. This would seem compatible with the developed country acceptance of preferential treatment agreed to in UNCTAD and restated in the Tokyo Round Declaration.

It is clear that in the longer term there is a need for institutional reform in those international organizations dealing with international trade, finance and money, and perhaps even the need for the creation of a new world trade organization.[66] At least some sort of code of conduct should be established to facilitate the smooth transition of the structural change that is associated with the changing comparative advantage of different sectors of different countries. Here much of the responsibility rests with national governments to pursue positive structural adjustment policies and refrain from short-sighted "beggar my neighbour" policies.

Finally, the most important conclusions that arises out of the discussion of contemporary protectionist pressure is that the sources are outside the control of developing countries. Balance-of-payments difficulties, structural adjustment problems and mercantilistic desires to maintain certain domestic industries all lead to domestic policies which developing countries cannot directly influence. Furthermore, the nature of much of the contemporary protection is such that strong bargaining is important in gaining market access. With no control over the sources of protectionist pressure, and little influence on their share of predetermined markets, developing countries should be concerned about the state of commercial policy in the world today.

[65] J. N. Bhagwati, "Market Disruption...", *op. cit.*

[66] American Institute of International Law, *Re-making the System of World Trade: A Proposal for Institutional Reform*, West Publishing Company, St. Paul, Mn., 1976.