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Trade, Protectionism and Self-Reliance: A Sense of Déjà vu

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This commentary attempts to find the connectedness between the recent lockdown induced economic upshots and the contemporary global trend of moving towards a deglobalized era. With a historical perspective this commentary examines how the entire world has been brilliantly balancing between free trade and protectionism for centuries. It also explores the relevance of Atmanirbhar Bharat in the context of such new normal.

1. Introduction

Amidst the global pandemic and in the wake of the wide-reaching containment efforts implemented by the governments in most of the countries, we have gradually entered a new global economic order both domestically and internationally. Globally this phenomenon has been christened as ‘new normal’ which naturally includes reshaping trade and commerce, social sectors’ magnitude, international relation and integration, mobility of capital and human capital, nature of transaction of goods and services and so on. Such intriguing restructure in every dimension of the society and economy, in particular, forced each one to follow the principle of complete closure of international borders.

2. Why and What ‘NEW’?

With COVID-19 showing little signs of abatement in India as well, the government has been rightly continuing with the partial lockdown policy leading to an induced hindrance on the movement of goods and factors of production. However, it should be noted that the mobility of financial capital has not been a matter of much concern till date as a spread of COVID-19 so far does not have an established connection with the online transaction of financial capital. In what follows, the international transaction of tangible goods and services requiring the physical presence of both buyers and sellers has gone down drastically in the recent past. This

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phenomenon is not typical to India only, all other countries are also experiencing a similar setback in production and transaction impeding smooth functioning of the global value chain. Such 'new normal' subsequently compelled the government of India to vouch for 'vocal for local' campaign, which was immediately supported by the 'self-reliant India' or 'Atmanirbhar Bharat' programme in conformity with the 'Make in India' initiative of the same government. However, the idea of 'Atmanirbhar' is beyond 'self-sufficiency': 'Atmanirbhar' also has the scope of production for export.

The basic principle of self-reliance is, however, very simple – produce whatever you need, produce whatever you desire to export, and also try to arrange for all the inputs you require carrying out production. It is not a case of 'no-export'. Thus, the question boils down to who would be buying our products as all are on the same boat in the sense that all countries are suffering from similar social and economic upheavals. However, tenets of a division of labour of David Hume and Adam Smith, comparative cost advantage principle of David Ricardo, love for variety and home market effect of Paul Krugman, etc. support a different scenario. All these globally acclaimed concepts are in line with globalizing the market. However, not to confuse that globalization and the market economy should not always be blamed for a rise in global inequality and other scratchy concerns. Helpman (2018) has compiled some interesting dimensions in this line. This is essentially the fallout of the failure of the State to control and channelize the virtues of globalization.

3. Protectionism in History

The concept of protectionism had been in vogue before. It is essentially an age-old idea which has a significant connotation for the *Corn Law*. And the repeal of the *Corn Law* was perhaps the first documented and accepted movement from protectionism to globalization. The *Corn Law*, in brief, is the imposition of tariff on imports of Corn which led to higher domestic price of Corn in Britain. Thus, the profit of agriculture and landlords went up while that of other manufacturing units went down. In addition, to compensate for higher corn price workers demanded a higher wage rate. This became the prime reason for decreasing profit in all other sectors, igniting the movement against the *Corn Law* and eventually the British government had to repeal it. The story of *Corn Law* was in the first half of the nineteenth century. Therefore, this naturally begets another question: What was there before?

To start with there did exist a sort of self-reliant economy though that was essentially in the spirit of self-sufficiency: produce, and consume what is produced. This very concept is succinctly analyzed with a modern look in a recent book – *The Great Convergence* – by Richard Baldwin (2016). He described this phenomenon as *bundling*. This is bundling of production and consumption at the same place – double coincidence of demand. We can think of it as spatial bundling, not like conventional bundling of goods and services or other related goods. Then came *first-unbundling* between production and consumption. But in reality, the idea was the creation and accumulation of more wealth. Trade or exchange was free then, except for transportation cost. Thus the point of concern is - how to acquire wealth? The simplest answer to this million-dollar question is 'sell more and buy less' or 'export more and import less'. This is perhaps the best alternative to war and a convenient pathway to

acquire wealth and become richer - popularly known as *Mercantilism*. One can easily understand that the basic essence of both *Mercantilism* and *Corn Law* is the same – building huge reserve through a trade surplus.

David Hume was, however, very critical of Mercantilist's view. He thought trade surplus is a temporary phenomenon and would not sustain for a longer period. His apprehension was very basic textbook kind of analysis. Huge trade surplus naturally leads to an increase in the purchasing power of the countrymen. This encourages the demand for domestic goods and subsequently the price of domestic goods rise. It has two effects: domestic consumers shift to cheaper foreign goods leading to an increase in import, and foreign consumers buy less domestic goods leading to a fall in export. Therefore, the trade surplus must shrink and eventually vanish.

Thus, the idea of *Mercantilism* lost its ground. A closer look at both *Mercantilism* and *Corn Law* reveals that these are fundamentally the routes to become both economically and politically powerful. Therefore, it is apparent that the proponents of *Mercantilism* were well aware of the fact that open and free trade has a levelling effect or has the potential to equalize every country economically (Bhagwati, 2003; Friedman, 2006). *Mercantilism* is a mix of two extremes: free trade in export and complete protectionism on import.

Later on, Adam Smith also criticized *Mercantilism* citing that it goes against efficiency, competition and productivity. And consequently, he came up with the idea of *Vent for Surplus*. Surplus land and surplus labour arise in an isolated economy mainly due to the narrowness of the domestic market. The only solution to this problem is accessing the foreign market and to go for export. But the question remains: where to export? who will buy it? To enable others to import they should also be allowed to export their products. This is how trade may lead to growth and development leading to the notion of *export-led growth*. As a consequence, we landed up in the era of free trade.

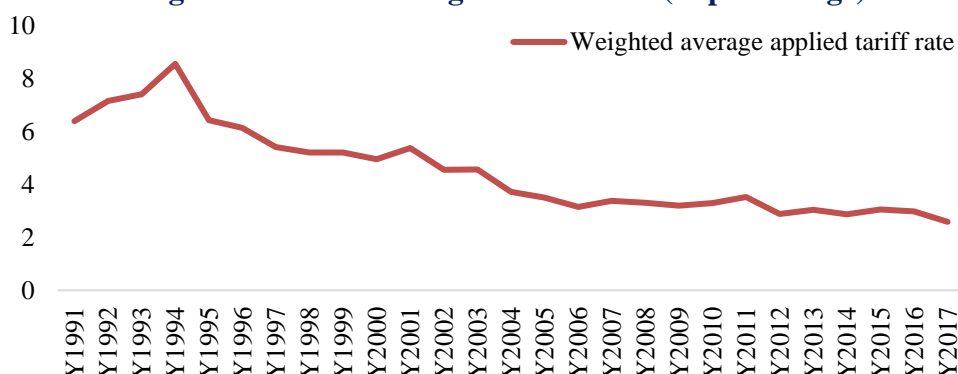
4. Free Trade, Hiccups, and Protectionism again

The main driving forces behind free trade were the division of labour, increased competition among agents, expanding the size of the market, and reduction in wastage of resources (Bhagwati, 2004). All these, in tandem, ensure low cost of production and price of the goods through more efficiency, less monopolization of the market, and an increase in economies of scale. Therefore, trade was welfare improving. Such free trade initiative was further accelerated by gradual reduction in tariff across the globe (Figure-1 and Figure-2 corroborate this). But, was everything good with free trade? The unambiguous answer is 'no'.

Trade leading to growth and development is not a zero-sum game; it is indeed a positive-sum game. In spite of that it creates both winners and losers, or some gains more and some gains less. This raises conflict of interest and pressure to shift from free trade regime (Feenstra and Hanson, 1996; Stiglitz, 2002). This contention got further impetus owing to some basic presumptions supporting free trade as an engine of growth. This includes the absence of a perfectly competitive market, externalities in both production and consumption, growth in the wrong direction indicating immiserization, exorbitantly high transportation cost, the effect on terms of trade, etc. On top of all these, an all-round increase in wage

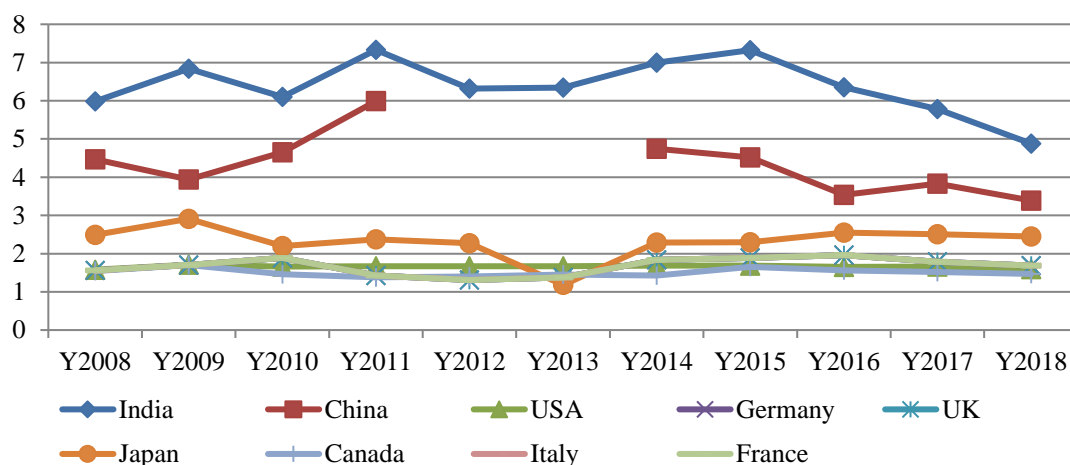
disparity between skilled and unskilled workers as a result of free trade generated another niggling problem (Helpman, 2018).

Figure 1: World Average Tariff Trend (in percentage)¹



Source: World Bank, UNCTAD, WTO, World Development Indicators

Table 2: Average Tariff Trend for Selected Countries (in percentage)



Source: World Bank, UNCTAD, WTO, World Development Indicators; China's data for some years are not available.

Accordingly, countries gradually moved to a protectionist era to solve few non-trivial issues like unemployment, trade deficit, setting up of indigenous industries, dependence on other trading countries, etc. Contrary to popular belief, protectionism also did not yield much-desired results.

From thereon we had two clear and parallel waves: globalization and protectionism (Bhagwati, 1998; Stiglitz, 2002). Protectionism is not in the form of very high tariff (as evident from the line diagrams) or quota, following WTO agreements, but the process of formation of various trading blocs was on. The main motive was to tilt the international terms of trade in favour of its member countries. During that time, globalization mostly took place through the more free movement of goods, labour, and capital. This wave of globalization was driven by a reduction in transportation or trading cost, which also helped trade in intermediate goods, outsourcing, global value chain, etc. This phase is known as *second-unbundling* (Baldwin, 2016).

Gradually, we have entered into the epoch of New Globalization. It is less open, restricted, and limited. We may call it *deglobalization* or resurgence of protectionism (Bello, 2005). This sort of opinion is, however, not accurate as protectionism has always been there incessantly in form of the customs union, trade blocs, etc. There were Buy American Act, Buy British Campaign, European Union export subsidy, etc. Very recently this protectionist approach took a serious turn with H1B Visa restriction, BREXIT, US-China trade war, etc. when we are no longer living in the era of *second-unbundling*. This is the time of *third-unbundling* (Baldwin, 2016; Marjit, Mandal and Nakanishi, 2020), where the cost of communication is negligible, global trade is dominated by services, distance is no more a matter of hindrance for service transaction, 40 per cent of world GDP is produced through the global value chain, 60 per cent of global trade accrues to trade in intermediate goods and services (Baldwin, 2016).

Recent *deglobalization* trend has been essentially propelled by three factors: (1) a tendency to shift back the centre of economic power to Asia; (2) world wealth share of developed countries rose from 20 per cent to 70 per cent during 1820-1990, but recently it slid back to the level of 1900; and (3) an increase in income disparity both within and between countries, and no signs of worldwide factor price equalization. These reasons forced the so-called developed countries to resort to an increase in the average tariff rate on imported goods, put a restriction on international labour mobility, and controlling inward and outward direct investment. Eventually, they had to find out a new name in favour of protectionist arguments as *protectionism* has already been stigmatized as harmful for global welfare. Thus, *deglobalization* surfaced though this term was used by Walden Bello, a Phillipino sociologist way back in 2005.

5. Trade War and the Golden Opportunity

Is the *Atmanirbhar Bharat* programme a remarkably pragmatic one? Is it a blend of economics, politics, and actionable plans? There is no clear answer to this query, though, of course, it diverts attention from some pertinent unpleasant economic issues. But that is surely not the only motive behind such nation wide promotion of a nationalistic economic plan of action as State guided campaign often induces a sort of *Bandwagon effect* helping it to become a ‘*movement*’, and that works for a good cause. During the global lockdown driven supply shock, a *Bandwagon effect* of the type we explained may be very handy when the economy is hobbling with the problem of the local supply shortage. The scope of self-reliance being much wider than catering only local market, such campaign and a nationwide concerted effort might be very constructive in exploring the export market. This should be done in a relatively cost-effective manner which again emphasizes the principle of comparative cost advantage. During the Coronavirus pandemic, some countries are forced to retreat from their respective export markets and naturally, those markets are now open to all for competition. This has been originally propelled by USA-China trade war and the loss of China’s credibility in the world market. India must appropriate such prospect and for that low-cost production is the major driving force which India would be able to manage owing to the huge pool of labour force.

Hence, international lockdown and complete shutting down of labour mobility due to the spread of COVID-19 may turn out to be a boon for the Indian economy. India must capitalize on the scope thrown to her through a combined advantage of demographic dividend, global supply shortage, and a fall in crude oil price in the world market. The *Atmanirbhar Bharat* campaign may act as an appropriate launching pad to break the shackles of low-level equilibrium trap and to move to the next level of development trajectory.

Endnote:

¹ This is the average of effectively applied rates weighted by the product import shares corresponding to each partner country. Data are classified using the Harmonized System (HS) of trade. Generally attempts are made to convert specific rates to their ad valorem equivalent rates and have been included in the calculation of weighted mean tariffs. When the effectively applied rate is unavailable, the most favored nation rate is used instead.

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About AIC

Considering the work of the ASEAN-India Eminent Persons Group (AIEPG), and its Report with recommendations for forging a closer partnership for peace, progress and shared prosperity, the Heads of the State/Government of ASEAN and India at the ASEAN-India Commemorative Summit 2012, held at New Delhi on 19-20 December 2012, recommended the establishment of ASEAN-India Centre (AIC), which was formally inaugurated by the Hon'ble External Affairs Minister of the Government of India on 21 June 2013 at RIS. AIC serves as a resource centre for ASEAN Member States and India to fill the knowledge gaps that currently limit the opportunities for cooperation. AIC is closely working with the Indo-Pacific Division of the Ministry of External Affairs (MEA), Government of India to undertake and disseminate evidence-based policy research and provide policy recommendations.

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