

# Developing and developed countries and protectionism economics essay



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It represents economic policies that a government employs to restrict trade in goods and services between countries. There are tariff and non-tariff barriers to trade. Some costs of protectionism include trade retaliation, competitive devaluation and production inefficiencies.

## **Evaluating the argument for developing countries**

The infant industry argument is one of the soundest and most common arguments that developing countries (LDCs) apply to justify their use of protectionism. They argue that it is extremely difficult for their sunrise industries to compete with the established ones in the developed countries (DCs). This is true because established industries would have had the opportunity to improve their production capabilities with technological advancements, and thus able to make profits even while keeping their prices low. A similar industry in an LDC, which is just starting out, would be doing so at a severe disadvantage as it lacks the production technology and experience, and thus would be producing much less efficiently. If immediately forced to compete in the global arena with the “ bigger boys”, such industries are likely to be forced out of business. This is where protectionism becomes imperative for its survival.

Protectionism will help cushion the initial higher production costs of such industries in LDCs. As these industries gradually grow and develop, their efficiency will improve, and their costs will be kept low. Here, it is worthwhile to note that protectionism would be more justified if the time period for which it is practiced is explicitly stated, and the firm is aware of the specific goals that it has to achieve within the given time frame. This allows firms to be slowly weaned off protectionism, and able to stand independently[2].

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Contrary to popular belief, most of today's DCs developed and achieved economic growth not through the policies of free trade that they fiercely advocate. Rather, these nations also relied largely on protectionism - tariff protection and subsidies - to develop their industries. Britain and the US are some of the more notable examples of the many DCs which used tariff protection most aggressively[3]. Britain heavily employed dirigiste trade policies during its period of trade policy reform in the 18th and 19th century. Similarly, during the 19th century, the US was one of the most extensively protected economies in the world. When criticized for such drastic protectionist measures, these nations argued that adopting free trade would come only after it could do without protectionism.[4]. While it is not conclusive that these protectionist measures guaranteed the economic success of the DCs, there is substantial evidence which reflects that it may very well be a necessary element in stimulating economic growth and development. If the DCs of the world went through a phase where they shielded their industries to such a great extent, why are LDCs of today deprived of a similar opportunity?

Although it is not an absolute right for LDCs to receive this opportunity, it would not be unreasonable for DCs to graciously allow LDCs some leeway for protectionism as a means to aid their economic growth and development. The DCs had a head-start in industrializing and so were able to reap the "first-mover" advantages of it. It is fair for the LDCs to apply protectionism to try and "catch-up". Giving the latter the opportunity to develop under protectionism so it can grow richer - faster - and allow its people to lead more dignified lives provides substantial justification for its actions.

Switzerland and the Netherlands were exceptions that maintained free trade since the late 18th century but this was because they were already technologically advanced. These exceptions, in fact, reinforce the importance of production technology if a country were to benefit more from free trade. This further supports the LDCs stand to protect their infant industries so it can build up its technological capabilities before opening up its economy.

However, there is a common argument against the above. Going by Ricardo's theory of comparative advantage, protecting infant industries would mean industries in LDCs would, in the short run, not be allocating resources as efficiently as they would be on the basis of comparative advantage. It follows that there is no maximization of economic efficiency. But the reason for this lies in the fact that Ricardo's theory on comparative advantage is a static theory which applies only to one point in time. The infant industry argument, on the other hand, looks at the dynamic theory of comparative advantage[5].

In most LDCs, the industries in which they have a comparative advantage in tend to be their natural resources and their agricultural produce. The prices of commodities in these industries are known for being extremely volatile. If an LDC were to adopt the static theory of comparative advantage, its GDP would vary wildly with these prices. Furthermore, the expertise needed to produce goods in these industries differs from that required in industrial economies and therefore, focusing only on the static comparative advantage would hinder the industrial development of the country and prove to be an obstacle in its bid to move up the "value-chain"[6].

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Protecting infant industries in LDCs play an essential role in generating learning effects that will lead to efficiency improvements and ultimately, economic growth. This facilitates economic growth in LDCs and would allow them to enhance the welfare of their people much faster.

### **Evaluating the argument for developed countries**

Protecting one's senile industry is one of the common arguments cited by DCs in justifying their use of protectionism. Senile industries are usually declining industries that have since become inefficient, especially so with rising competition from LDCs[7]. A classic example would be the protection of the steel industry in the US by then President George W. Bush. His protectionist policies ended up hurting the steel consumers much more than it helped those within the steel industry. As many of these steel consumers were small market players and therefore, price takers, the increased steel prices led to significant job losses in many states. The US government was able to mitigate the effects of this severe unemployment through relief and subsidies[8].

Protecting a senile industry is likely to translate into adverse implications on a lot of other industries. Senile industries are matures ones that have established itself in the country and many industries would be dependent on and related to it. The relief and subsidies that went into mitigating the unemployment is merely a short-term solution, and these financial resources could have been channelled to better use in innovation and productivity improvement. DCs are armed with the knowledge and capability to seek other approaches in tackling their trade woes, and should not simply resort

to protectionism. Furthermore, protecting senile industries is usually an excuse to shield the industry's inefficiency[9].

Another reason why DCs protect is because they can use protectionism to intimidate other countries into reducing their export protection. This tool can force foreign markets to open up and the DC would benefit from both its own, and the other country's free trade. However, if these threats remain permanent, it would not help in opening up the other country's market. In addition, if protectionism takes the form of "voluntary quotas", the direct consequence would be a re-direction of trade by LDCs as imposed on them by the DCs, and there would be no freer trade as a result[10].

DCs also argue that protectionism is justified when it has monopoly power in producing a certain good as this could enhance the welfare of the country. A country that produces a significant portion of the world's output of a particular good can use an "optimum" tariff to gain the most out of the producer's monopoly power. But it must be noted that few countries ever have substantial market power that makes this a sufficiently important consideration to go against free trade. Moreover, the likelihood of inviting trade retaliation is very high and this would reduce the overall welfare gain of the country, thereby weakening this argument[11].

## **Conclusion**

After looking at the justifications from both DCs and LDCs, it is evident that LDCs have a stronger case for why they should employ protectionism.

Protectionism can play a crucial role in speeding up the rate of growth and development in LDCs and the world can be a much better place when the

there is progress in LDCs. Undeniably, there is the danger that once protectionism is put in place, it is very difficult to remove. But if the pros of the particular protectionism outweigh the cons, LDCs should go ahead and reap the maximum benefits possible. While doing so, they should be mindful that protectionism should have a “ used-by” date; which would allow them to capitalize on its short-term gains, and to avoid its long-term pains.

Protectionism, as a means of facilitating economic growth in LDCs, can in fact benefit both the LDCs, and the rest of the world.

(1, 498 words excluding footnotes)