

PROTECTION IN A DEMOCRACY: A Conversation with H. Peter Gray and Roy Licklider*

Gentleman: I have heard it said that protection of the U.S. automobile industry costs consumers about \$1,000 per car. Clearly, there is a sacrifice of real income inherent in protecting American industries from foreign competition. Why then is there so little public opposition to protectionism?

H. Peter Gray

The automotive example is not a unique experience and the failure of the public to insist on free trade is surprising. We believe it is worth focusing on three mutually-reinforcing explanations: uncertainty about the real economic effects of free trade; a failure by government to supply appropriate information and lead public opinion; and the omission of critical non-economic factors from the arguments of those who advocate free trade. In a sense, all three are consequences of the democratic form of government.

Conventional free trade arguments understate or neglect some major economic costs (and benefits) of the policy so that the uncertainties about the "side effects" of free trade might well warrant shunning the policy. The argument for free trade is based on a static analysis of a world in full-employment equilibrium and tacitly assumes that the domestic economy is an efficient allocator of resources. The benefits of free trade are strengthened if the efficiency of the domestic market is marred by monopolies, imperfect competition and what Leibenstein termed x-inefficient firms, foreign competition will erode these imperfections.

The full-employment assumption is questionable on three counts. The needed wide range of factor substitutability may not exist in modern economies. Acceptance of free trade implies the integration of labor markets in industrialized countries with Third World pools of surplus labor. The (adjustment) costs of reallocating factors of production from declining to expanding sectors may be both substantial and long-lasting. Little is known about these costs and, as Michalski has pointed out, good economic policies have not yet been developed to assist the market mechanism. The skills required by the old and new industries may differ so much that adjustment will take a long time, possibly exceeding the work life expectancy of many workers, and could require the creation of major training facilities, presumably at the expense of the public sector. Some workers may find the newly-required levels of skills beyond their abilities. Given the ignorance of these important costs, the public may reasonably decide against free trade.

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A second source of uncertainty derives from the very potential of free trade for improving the operational efficiency of the domestic economy. No one will be able to diagnose who will bear what share of the consequent costs. A worker or capitalist in a protected monopoly will obviously lose, but the repercussions will be widespread and not subject to identification. This aspect of resistance to free trade will be reinforced by the possibility of severe structural changes in the domestic economy. Free trade implies complete laissez-faire and laissez-passer internationally, and that may imply substantial laissez-faire at home. Few people are willing to risk existence in a purely Smithian world. The quantum leap would be simply too great for either voters or analysts to contemplate.

Aside from the costs of adjustment, there is significant uncertainty about the actual macroeconomic impact of free trade in the real world. This uncertainty is greater if the move to free trade is not universal. Economic uncertainty would require, at a minimum, an elaborate system of safeguards before a commitment to free trade could be obtained. The free trade argument does not countenance this need for groping towards what may be a desirable goal.

I recently chanced across a British report which argued that voters simply did not understand the arguments against protection. Do either of you concur with this assessment.?

Roy Licklider

This explanation of protectionist sentiment was plausible in the 1930s, when political élites in the industrialized countries generally favored protectionism. However, since World War II, free trade has become the dominant ideology of these groups, particularly in the United States--presumably because of the American economic position in the international trading system. Perhaps the best evidence of this intellectual dominance is that today protectionism must be rationalized in industrialized countries in terms of justified **exceptions** from free trade, as in "impacted industries" or retaliation for violations of the "rule of the game" by other states.

In other words, tariff increases must be rationalized in political terms as exceptions to an established and accepted doctrine. Since free trade is the prevailing ideology in most industrialized nations, educational efforts by governments to "sell" free trade are unlikely to be very productive.

H. Peter Gray

There is no denying the political problems for the governments of the developed world in allowing a surge of imports from the Third World. But the electorates' lack of appreciation of the gain inherent in free trade is a matter for leadership and performance in fulfilling the information function of government.

Is not the emphasis that you both place on non-economic rationalizations of protectionism something new?

Gray

No indeed. I am reminded that Harry Johnson, who was the single most influential proponent of free trade in the 1960s and 1970s, attempted to explain away the inconsistency by arguing that maximizing income was not the goal of the public; he postulated that industrial production was, in fact "a collective consumer good". Protection of industrialization becomes an end in itself under such conditions. Nevertheless, Johnson's important insight misses the key point that the democratic form of government rather than industrial production is the collective good; industrial production is important because it contributes to maintaining democracy.

Roy Licklider

It also seems relevant to note that, in a democracy there are two kinds of impediments to free trade. First, the democratic system may become unstable in the absence of protection and, second, protectionist pressure groups are an inescapable feature of democracy.

Hager has argued that protection can be justified if the effect of free trade on income distribution is likely to tear at the social fabric. He suggests that Germany free trade in would create a bimodal income distribution with significantly greater inequality and that it would aggravate inter-class tensions and possibly destroy the political serenity of recent years. The Cambridge economic Policy Group in the United Kingdom has asserted that protection there is warranted because the adverse terms-of-trade effects of relinquishing protection would create politically intolerable strains.

Regardless of its effect on the economy, protection may be a cost of democratic government. People and organizations which expect to be seriously injured by free trade are much more influential politically than the much larger number of consumers who each suffer relatively small individual losses from continued protection. In an economy which suffers from ongoing inefficiencies, potential losses will be greater. In an electoral system in which voters pick candidates or parties instead of expressing preferences on separate issues, the voter who is willing to switch his vote because of one particular issue becomes disproportionately important. This power of the few is increased by a system of geographic constituencies, where individual representatives are likely to reflect the interests of threatened industries in their districts.

The willingness of the majority to tolerate protectionism is attributable to the mechanics of the political system. Surely it is better to tolerate protectionism than to submit to a beneficent authoritarian government in economic matters, if only because such authority tends to undermine beneficence. The problem is closely analogous to that of law enforcement. The public is deeply concerned about the crime rate. However, many people prefer to tolerate such high rates rather than advocate a more aggressive enforcement policy which would require abandoning constitutional safeguards. Essentially, then, they have decided that crime is one of the costs of political democracy in the U.S. We may have to adopt the same position toward protectionism, at least in the medium term, while working to clarify the real economic and political uncertainties about the impact of free trade.

How can the "uncertainty" aspects you are emphasizing be incorporated into the explanatory models on which we have come to rely?

H. Peter Gray

With great difficulty, if at all. Consumer tolerance of the economic losses associated with protectionism exists because there is uncertainty about the degree to which free trade might expose the economy and society to fundamental change. Uncertainty "makes us rather bear those ills we have than fly to others that we know not of." Johnson's emphasis on causes other than income-maximizing was correct. The free trade argument must be presented in terms of Simon's satisficing rather than Hicks/Samuelson maximization. Uncertainty involves both economic and political dimensions. The economic reservations can be countered by a gradual progression toward free trade, but the political objections may, given the characteristics of democracies, be intransigent.

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