

FREE TRADE VS. PROTECTIONISM

FREE TRADE

PROTECTIONISM

International trade is to develop on its own, free of political restrictions

Definition

The government restricts international trade through measures such as tariffs, subsidies, import quotas and other limitations

- Free international trade
- Abolition of trade restrictions



Objectives



- Protects domestic industries against foreign competition
- Reinforces competitiveness

Australia

Australia has its own free trade agreement with the USA. This has led to the elimination of over **99%** of customs tariff headings in trade with the USA, and an average of **4.3%** of customs duties that would otherwise be incurred by exporting US products to Australia



Examples

European Union

The EU's Common Agricultural Policy (CAP) increases prices for domestic farmers on agricultural markets through customs duties to boost farmers' incomes. Some agricultural products, such as beef and dairy products, are subject to duties exceeding **75%**



- Competitive advantages through product/service specialization
- More varied goods
- Development of expertise and skills
- Promotion of efficient division of labor



For



- Protects domestic companies, particularly in new industries
- Helps safeguard limited resources/raw materials in their own countries
- Protects jobs

- A situation where the government exercises no influence does not match the market reality
- Increased economic dependency between nations
- Imbalanced development of economic sectors
- Pollution

Against



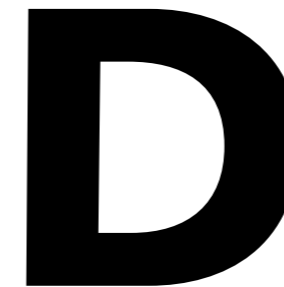
- No competition between domestic companies
- Elicits retaliatory measures between nations
- Limits the degree of specialization



RELYING ON OUR OWN STRENGTHS

Practical tips for German companies on handling the Trump administration

Dr. André Wolf heads the research department in economic activity, the global economy and international trade at the Hamburg Institute of International Economics (HWWI)



DIALOG: Dr. Wolf, the US president has criticized his country's trade deficit with a number of countries. This relates to very different economic regions – for example China and the EU. Aren't the reasons for these deficits very different?

Dr. André Wolf: The deficits that the USA has with its key trading partners are indeed very complex. With regard to China, the wage gap has long been the dominant factor. The possibility to relocate production – either partially or wholly – was for many American companies a lifeline for many American companies, and allowed them to safeguard their own price competitiveness. This offered China the great opportunity to become an indispensable part of the global value chain. It also spawned an interesting symbiosis. Chinese trade surpluses were reinvested in the USA as a safe haven, channelling the US deficit back to the country in the form of capital inflows. The artificial devaluation of the Chinese renminbi thus rendered this system ever more prominent over time. This will make it virtually impossible for both countries to shed their mutual dependence in the fore-

seeable future. When it comes to the EU and Germany in particular, things are somewhat different. From the USA's perspective, the cause has less to do with interlaced value chains. The primary reason for the imbalance is the greater qualitative competitiveness of EU industry, particularly in trade-intensive areas that generate significant added value, such as engineering and car manufacturing.

DIALOG: The American administration shows major skepticism toward free trade – something easy to criticize. But just how free is free trade? And above all, is it fair?

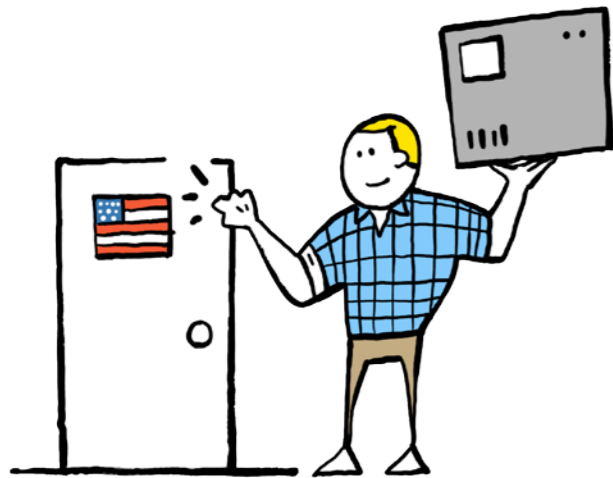
“From a sober perspective, global free trade has seen better days, even disregarding the actions of the new US administration.”

AW: From a sober perspective, all is not well with global free trade, even disregarding the actions of the new US administration. The current dip in the growth



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of global trade is largely attributable to a general move toward protectionist tendencies. According to Global Trade Alert, the USA alone introduced over 600 discriminatory trade protection measures between 2008 and 2016, i.e. during Barack Obama's term of office. Unlike previously, most such measures no longer constitute customs barriers, but rather discrimination in the form of specific product standards, or approval procedures that drive up costs. Other countries like China focus on macroeconomic instruments, such as currency market management, to artificially increase their competitiveness. All these intransparent measures ultimately harm not just the freedom but also the fairness of world trade, as they



impair the international competitive position of certain companies and products more or less arbitrarily.

DIALOG: BMW AG employs 8,000 people in its plant in Spartanburg, South Carolina. Other large German companies also have production sites in the USA, so they don't panic at Donald Trump's threats. However, most medium-sized companies, for which the USA is a crucial export market, lack such aces. How can they best protect themselves from possible sanctions?

AW: There are several possible approaches open to internationally oriented medium-sized German businesses if this risk were to materialize. One is to diversify sales markets. The East Asian region in particular, with its robust economic growth and developing middle class – but by all means Africa, too – offers interesting sales potential for German medium-sized companies. Plus, countries like China have already indicated that they would be more than willing to fill the gap as a sales partner in the event that the USA were to further isolate itself. Another option, which is more about each entity consolidating its own position in the US market, involves concluding cooperation agreements with local American partners. Customs barriers could be circumvented by switching parts of the value chain concerned with production and sales to the USA. As the introduction of punitive tariffs could be expected to face trade-related political countermeasures on a par with the EU, such cooperation might also be in the interests of medium-sized American businesses, if access to the EU market is secured in return.

DIALOG: The new American administration's apparent unpredictability and frequent changes of direction are what touch a nerve, more than its fundamental isolationist tenor. How can industrial companies requiring certainty in their planning adapt to this situation?

AW: Amid the current climate of general uncertainty, the key first and foremost is to monitor trade-related political developments in the USA at all times. What matters here is not to be intimidated by every statement issued by the US president but rather to read between the lines and to focus on the role of Congress in particular, which has the final say, because it is still far from certain whether and to what extent President Trump will be able to implement his trade agenda. That aside, remembering personal strengths is also important under current circumstances, as the radical about-turn in US politics definitely opens up opportunities, especially in fields where German expertise leads the world. For example, the retrograde step of the USA in environmental and energy policy boosts the competitive chances of German companies in the green technologies field, which, in global terms, is such a key market for the future. The coming years will offer a golden opportunity to take a decisive lead in the technological race – a gap the USA will find difficult to close.

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About the Hamburg Institute of International Economics

The Hamburg Institute of International Economics (HWWI gemeinnützige GmbH) is a privately financed economics research institute. Its main activity is the publication of scientific analyses. Academics and researchers of the HWWI also develop recommendations for action and issue advice based on basic research and the development of models. Besides training young academics, the institute maintains international partnerships and networks, focusing on scientific communication in particular. You can find additional information at www.hwwi.org

RED ALERT FOR GLOBAL PLAYERS

The top 10 global business risks

Over 1,200 risk experts from more than 50 countries identified their “TOP 10” corporate risks for the sixth annual Allianz Risk Barometer:

