A negative railway

A beautiful reminder of the benefits of free trade at a time of nationalist pride

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Whatever the highs and lows of the World Cup, it provides a stark reminder of the passion tied up in the feeling of belonging to a country. But this time around, is the stirring purely temporary? Because when you factor in the recent European parliamentary election results, which exposed a distinctly nationalistic zeitgeist, and the increasing number of territorial disputes occurring globally – think the bitter Japan-China row over East China Sea islands – it is hard for the more imaginative mind not to get carried away and draw quite sinister conclusions.

Given the current economic milieu, this sentiment is completely understandable. When times are hard, becoming defensive and protecting 'your own' are natural reactions. Indeed, the World Trade Organisation (WTO) warned in a report released on 18 June that "protectionist pressures are bound to remain in a context of slow uneven recovery [in the global economy] and persistent high levels of unemployment".

Students of economics or finance will likely find this trend somewhat alarming. To jog our minds as to why, it is worth consulting the little-known 19th Century French economist, Frederic Bastiat. Over 150 years ago Bastiat put forward a ruthless attack on tariffs, and it still stands out as a fabulously clear defence of free trade/markets.

He attacked the logic of a Mr Simiot in a Bordeaux newspaper, who promoted the protectionists' cause by suggesting that the proposed railway between Paris and Madrid, aimed at improving the flow of goods, should have a break in the tracks at Bordeaux. Simiot argues that if goods and passengers are forced to stop at that town, profits will accrue to bargemen, porters, commissionaires, hotel-keepers, etc.

Bastiat cleverly and playfully exploits a fatal flaw in Simiot's stance by exaggerating the point and taking it to its extreme:

"If Bordeaux has a right to profit from a break in the tracks, and if this profit is consistent with the public interest, then Angouleme, Poitiers, Tours, Orleans, and in fact, all the intermediate points, including Ruffec, Chatellerault, etc, etc, ought also to demand breaks in the tracks, on the grounds of the general interest — in the interest, that is, of domestic industry — for the more there are of these breaks in the line, the greater will be the amount paid for storage, porters, and cartage at every point along the way.

"By this means, we shall end by having a railroad composed of a whole series of breaks in the tracks, i.e. a negative railroad."

"Whatever the protectionists may say, it is no less certain that the basic principle of restrictions is the same as the basic principle of breaks in the tracks: the sacrifice of the consumer to the producer, of the ends to the means."

It's not all one-way though, as the above train of thought ignores such worthy projects as the Trans-Pacific Partnership (TPP), the Trans-Atlantic Trade and Investment Partnership (TTIP), as well as on-going progress being forged out at WTO meetings.

It also washes over some of the key motivations behind protectionism. While in aggregate the net effects of global trade are positive, it does produce losers as well as winners. Economics textbooks brush this reality off by suggesting that the winners compensate the losers, at least to some degree. In practice, however, this rarely happens – hence the protective instinct of governments. This instinct takes on a parental form when it comes to 'infant industry', protecting them while they develop and grow before releasing them into the big bad world.

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Unfortunately, in many cases it can prove hard to let go and once these barriers are established, it can be very tempting not to remove them. Similar arguments are often put forward and implemented for more developed industries that carry strategic importance. Certain European countries (with, let's face it, more impressive World Cup credentials) are renowned for this, not only in defence, of course, but also in utilities and agriculture.

Perhaps this helps explain why, in their recent report, the WTO warned that protectionist policies have been on the increase. A number of G20 members, including US, China and the EU, have taken policy measures such as instigating anti-dumping investigations and introduced special licensing agreements that favour domestic businesses over foreign ones. In the report, the WTO said it had identified 112 trade restrictive measures introduced by members of the grouping of leading advanced and developing economies between mid-November 2013 and mid-May 2014.

The idea that trade should be free to permeate borders, while of overall economic benefit, poses interesting challenges, in particular to the notion of sovereignty. Europe provides a perfect entry point to examining this point of what sovereignty truly means in an interconnected world. As the monetary union lurches toward greater political and fiscal union, the need to set up mechanisms for managing interdependencies is clear as national economic policies have natural and sizeable repercussions for neighbouring economies. And yet, despite progress being made on important issues such as banking supervision, the reluctance of the currency bloc to arrange and implement supra-national entities is a function of a 'fetish with national sovereignty' and appears to overlook reality. However, elements of this reluctance are understandable given the construct of the current system – cross border lending was inevitably going to contract when the music stopped and revealed that national governments were largely on the hook. Knowing what is good for you is one thing. Doing it is quite something else.

As ever, the solution to the problem lies in compromise. The competing forces can co-exist but the harmony is delicate. An international decision-making approach is required, with political and economic institutions that are global in nature and in thinking. Encouraging free trade should be paramount to the overall agenda as the benefits are undisputed. But to address the distribution of those benefits, national interests must be factored in.

To conclude, the confusing interplay of the tug of war between tribalism and globalisation cannot be ignored. On the one hand, the idea of rigid national borders looks increasing archaic, after all many of them have been drawn somewhat arbitrarily – Africa and the Middle East spring to mind here. But on the other, the notion that we will all become global citizens and shed our tribal instincts is uncomfortable. Unfortunately we are still living in a world of parochial railway lines, to some degree at least, but it does make the quandary of who to support in the World Cup a little easier.

Lucy O'Carroll, Chief Economist for Aberdeen Solutions

Trade restrictive measures

Type of measure	Mid-Oct 10 to Apr 11 (6 months)	May to mid-Oct 11 (6 months)	Mid-Oct 11 to mid-May 12 (7 months)	Mid-May to mid-Oct 12 (5 months)	Mid-Oct 12 to mid-May 13 (7 months)	Mid-May to mid-Nov 13 (6 months)	Mid-Nov 13 to mid-May 14 (6 months)
Trade remedy	53	44	66	46	67	70	66
Import	52	36	39	20	29	36	25
Export	11	19	11	4	7	8	17
Other	6	9	8	1	6	2	4
Total	**122**	**108**	**124**	**71**	**109**	**116**	**112**
Average per month	230.3	18.0	17.7	14.2	15.6	19.3	18.7

Source: WTO Report on G-20 Trade Measures (Mid-November 2013 to mid-May 2014), 18 June 2014

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