THE CHANGING POLITICAL ECONOMY OF PROTECTIONISM

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Agnes Ghibuțiu*

Abstract
The paper aims to identify the peculiarities and some of the implications of global protectionism associated with the financial and economic crisis of 2008-2009, from both a quantitative and a qualitative point of view. The approach is based on a political economy perspective rather than an econometric one, and starts from the assumption that globalization and specifically the global production networks are responsible for a moderate increase of protectionism in correlation with new forms of protectionism (such as financial protectionism or protectionism related to the utilization of natural resources). The analysis brings the authors to the conclusion that due to the continuing process of globalization as well as the more explicit presence of regional and world governance in the short and medium-term perspective, traditional trade protectionism is not going to increase. Nevertheless, other forms of protectionism initiated by transnational corporations might become manifest.

Key words: globalization, protectionism, global production networks

JEL Classification: F01, F02, F23, F59

Political economy and economics – “What’s in a name?”

The current crisis that started in 2008 and may last, at least in the Euro zone, for another decade according to a recent statement by German Chancellor Angela Merkel¹, brings into the forefront not only some long-term overdue structural issues of the post–WWII development paradigm, but also some subtle changes in economic terminology. These changes include an apparent return to the classical notion of “political economy” instead of a more objective one, like “economics” or “economic science”. But we can ask ourselves, in the same way as Shakespeare did: “What’s in a name?”² The answer in our case is that, as George Friedman remarked³, classical economists like Adam Smith and David Ricardo never used the term “economics” but always that of “political economy” for the simple fact that they did not

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¹ Annika Breidthardt, Germany's Angela Merkel: It Will Take a Decade to Turn Around the Euro Zone, November 11, 2011, http://www.huffingtonpost.com/2011/11/05/german-chancellor-angela-
² The whole quotation: "What's in a name? That which we call a rose / By any other name would smell as sweet.", William Shakespeare, Juliet in Romeo and Juliet (II, ii, 1-2).
conceive politics without economics, and economics without politics. In other words, according to the classical approach, the motivations and behaviour of economic agents could not be separated from the political system in which they were embedded, with the political system being permanently modified by the economic realities.

The term economics tends to convey an entirely objective sense, and this term correlated with the heavy use of econometrics made a vast majority of economists to forget that economic science is part of the social sciences, i.e. of “soft sciences”, and not “hard sciences”, such as mathematics and physics.

Why is all this so important in understanding the current crisis and its implications in the field of protectionism?

Our answer is that in order to understand the current state of the world economy and its future trends, we have to take into consideration the non-linear behaviour of human beings, the not always rational character of economic agents (which is usually assumed) and the prevalence of individual and group interests over the abstract interest for the common good of humankind.

This being said, we intend to put into perspective the practical aspects of globalization from the point of view of the above mentioned individual and group interests. Based on this, we are then going to explain why despite the significant dimension of the current economic crisis, it did not lead to an equally significant increase in the level of protectionism.

**Globalization – a pragmatic approach**

Table 1 provides a snapshot of globalization and its implications, including both production and trade.

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Value at current prices in 2010 (billions of US $)</th>
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</thead>
<tbody>
<tr>
<td>Nominal Gross World Product</td>
<td>61,960</td>
</tr>
<tr>
<td>World exports of goods and services</td>
<td>18,902</td>
</tr>
<tr>
<td>World sales of TNCs’ affiliates</td>
<td>33,000</td>
</tr>
<tr>
<td>World exports of TNCs’ affiliates</td>
<td>6,239</td>
</tr>
</tbody>
</table>

**Sources:** Data compiled by the authors from IMF, WTO, and UNCTAD databases.

Data in Table 1 shows that world sales of TNCs’ foreign affiliates (meaning in fact FDI) represent over 50% of the nominal value of gross world product and 1.74 times more than the value of world exports of goods and services.

The interpretation of these figures and proportions is that nowadays over 50% of everything that is produced globally is produced by TNCs (through their foreign affiliates located in another country than the country of origin of the mother company). At the same time, global sales of TNCs’ foreign affiliates represent almost twice the value of world exports of goods and services. This latter observation does
not mean in any way that exports are to disappear any time soon, but points to the fact that increasingly producers are relocating their production capacities in accordance with the presence of their solvable consumers. The economic importance of foreign affiliates of TNCs is further strengthened by the fact that they generate more than 1/3 of world exports of goods and services.

This being the case, it becomes clear that in the present-day world economy we can speak (in a majority of cases) primarily about global or distributed interests of some global players (that is, TNCs), and only secondarily about national or local interests (mostly in the case of states that represent world or regional powers).

And it is just this perspective that puts the question of protectionism in a new light. Because in this context the questions becomes: “Who seeks protection from whom?”

Who is going to raise protectionist requests when, for instance, Volvo from Sweden is owned by the Chinese company Geely, or Land Rover from Great Britain is owned by the Indian company Tata Motors, or the US company Chrysler is owned in proportion of 53.5% by the Italian company Fiat? Who is going to ask for protection in a country like Romania where the production of steel, cement, automobiles, beer or dairy products is owned completely or to a very large extent by foreign investors?

These statements should not be interpreted in an absolute way. Indeed, there are still some local producers in all countries of the globe, and some of them are big enough to raise protectionist claims. But in most instances protectionist claims are either limited or expressed rather by TNCs themselves, in which case the host country government is just a vehicle for defending global corporate interests.

Globalization makes protectionism difficult not only because of foreign ownership. The case of protectionism is also seriously affected by the very intricate web of parts and components made in many corners of the globe that find their place in the final products, be they electronics, vehicles or others. A very good example in this context refers to the US trade deficit in iPhones (Table 2). It is easy to extrapolate this situation to automobiles, computers or electronic devices, in general.

| Table 2: US trade balance in iPhones, in 2009 (million US $) |
|-----------------|--------|----------|---------|---------|---------|--------|
|                 | China  | Japan    | Korea, Rep. of | Germany | Rest of world | World  |
| Traditional measure | -1,901.2 | 0       | 0        | 0       | 0       | -1,901.2 |
| Value added measure    | -73.5  | -684.8   | -259.4   | -340.7  | -542.8  | -1,901.2 |


The table is very suggestive of the fact that international production networks call for a completely new measuring methodology based on value added for a more accurate assessment of trade. Trade in value added is likely to challenge not only traditional statistical concepts (such as, “country of origin” or “resident versus non-resident”), but it will also have a major impact on trade policy issues (e.g. trade
disputes and anti-dumping measures), including trade negotiations. Who produces for whom or who should be protected against whom, judged so far on the basis of trade figures recorded gross, will be put in the right context, in conformity with the sheer realities.

The crisis and protectionism – some facts and figures

The outbreak of an almost global crisis in 2008 raised at that time the fear that the crisis situation will lead to an increase of the number protectionist measures and that such an increase would affect international trade and further aggravate the crisis. However, the reality was far from such a pessimistic scenario even if some increase in the number of protectionist measures took place, indeed. Figure 1 provides a combined presentation of the total number of protectionist measures per country in force between October 2008 and September 2011 and the total of new measures per country for the same period of time.

Figure 1: Potentially trade restrictive measures, by country, since October 2008


According to the graph, higher number of protectionist measures were to be found only with a small number of countries (Argentina, Russian Federation, Indonesia, Brazil and China), and even for these countries there were no great numbers of new protectionist measures (with the exception of Argentina). The distribution of the “potentially trade restrictive measures” by country is of importance, as out of 424 measures in force since October 2008 104 were implemented by only one country (Argentina) and 71 by the Russian Federation,

4 These are the exact words of the European Commission in the source document. We point out the fact that the studies refer to potential and not to real adverse effects on international trade.
while for the same period of time USA enacted 7 measures, Japan 5, Canada 5. A detailed presentation of the number and type of measures is given in Table 3.

Under these circumstances, we may rather speak about individual, specific cases and not about a world-wide phenomenon. We can also note that the majority of the measures were border-barriers initiated by a relatively small number of countries that had circumstantial conditions. At a large distance from border-barrier measures, we can find stimulus and other measures which are specific during a crisis period as the private sector is seeking assistance from governments.

**Table 3: Potentially trade restrictive measures, per country and type of measure, in force since October 2008**

<table>
<thead>
<tr>
<th>Country</th>
<th>Border barriers</th>
<th>Behind-the-border measures</th>
<th>Government procurement</th>
<th>Services and investment barriers</th>
<th>Export restrictions</th>
<th>Measures to stimulate exports</th>
<th>Stimulus and other measures</th>
<th>Total measures per country</th>
</tr>
</thead>
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<td>Algeria</td>
<td>2</td>
<td>3</td>
<td>2</td>
<td>3</td>
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<td>1</td>
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<td>Taiwan</td>
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<td>Ukraine</td>
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<td>1</td>
<td>1</td>
<td>1</td>
<td>2</td>
<td>18</td>
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</tr>
</tbody>
</table>

| Total measures by type | 209 | 35 | 34 | 35 | 29 | 23 | 59 | 424 |

* G20 countries

**Source:** Eighth Report on Potentially Trade Restrictive Measures - October 2010-September 2011, European Commission Trade, Tradoc_148288.pdf
What is clear, is that despite the increase in the number of protectionist measures, the world economy has not been affected in any important way. This assertion can be easily sustained by the following facts:

- World GDP increased in 2010 by 5% over the previous year and it is expected to increase in 2011 and 2012 by 4%.\(^5\)
- World exports recovered in 2010 what they lost in 2009 (an increase by 14.5% in 2010 over 2009, which could offset the 12% decline in 2009)\(^6\); global FDI flows increased in 2010 by 5%, although they are still under the 2007 peak level.\(^7\)

The simple interpretation of the above indicators is the following: if during the same period of time we witness, on the one hand, an increase in the number of protectionist measures (and the key issue here is that we speak about the number of protectionist measures, and not about their impact) and on the other hand, an increase of world GDP, world trade and world FDI, then the only conclusion is that the effect of the said protectionist measures is practically not significant.

Anyway, the fear of a resurgence of protectionist measures made WTO, OECD, the European Commission, G-20 or independent organizations such as Global Trade Alert (GTA) to monitor the phenomenon at global level. The results obtained from monitoring are diverse according to the organization that did the measure and interpreted as a whole (for the period November 2008 – September 2011) they are somehow mixed. The mixed character derives from the fact that while the number of protectionist measures increased, they did not significantly affect trade.

What is clear is that in 2009 (the peak year of the crisis) the protectionist measures affected only 1% of trade in goods and even less in the case of trade in services. At the same time, although the number of new antidumping investigations increased by 15% from mid-2008 to mid-2009, they affected only 0.4% of USA and European Union imports.\(^8\)

More recent data produced jointly by WTO, OECD and UNCTAD indicate that the cumulative share of world trade affected by new trade restrictions since the start of the financial crisis in 2008 was of over 2% by mid October 2011\(^9\) which represent an increase but the level is still marginal and the general trend of the world trade is ascendant.

Moreover, WTO statistics had shown a considerable slowdown in trade defense activities since 2008, with new investigations declining both in 2010 and 2011\(^10\). Therefore, contrary to common sense beliefs the crisis situation has not led to a


\(^{6}\) Idem.


\(^{8}\) Fredrik Erixon, Razeen Sally - Trade, Globalization and Emerging Protectionism since the Crisis, ECIPe Working Paper No. 2/2010.

\(^{9}\) Reports On G20 Trade And Investment Measures (May To Mid-October 2011), WTO, OECD, UNCTAD, October 25, 2011

\(^{10}\) WTO (2011), Report on G-20 Trade Measures (May to mid-October ), 25 October 2011, Geneva
significant increase in the use of trade defense measures such as anti-dumping, countervailing duties and safeguards.

**Protectionism in the world economy of today – what are we talking about?**

As we are going to show below, we have to ask again ourselves, as we did at the very beginning: “What’s in a name”? In this case, the question refers to what we include under the generic name “protectionist measures”.

Traditionally, protectionism referred to “Government actions and policies that restrict or restrain international trade, often done with the intent of protecting local businesses and jobs from foreign competition. Typical methods of protectionism were import tariffs, quotas, subsidies or tax cuts to local businesses and direct state intervention”.

After the onset of the crisis some of the monitoring institutions, for various reasons, decided to broadly extend the scope of protectionist measures, but this extension in correlation with the intrinsic characteristics of globalization made things quite unclear. For instance, researchers from the GTA include bailouts/state aids as well as announced but not yet implemented measures in their data base. Such a broad interpretation led to the count of an impressive number of protectionist measures, that is about 1,100 measures active in September 2011).

**Bailouts as a form of protectionism**

The inclusion of bailouts in the area of financial services, automobile industry and other sectors is highly debatable, in our opinion, because the money provided by various governments to their ailing banks or car makers was not aimed at protecting them from competition, but rather at preventing the respective economies from spiralling out of control. In the case of such large bailouts, attaching certain limitations to the operation of the assisted companies is apparently logical and automatic. A government is putting money into a large bank or a large automotive company in order to prevent a large-scale impact on the respective economy as result of imminent insolvency or bankruptcy. Until the money is paid back by the respective companies following the implementation of some revitalization plans, the respective amounts cannot be used for other activities or transferred abroad. This may sound like protectionism and may look like protectionism, but we may argue it is not.

**Industrial policy related measures**

A salient feature of governments’ responses to the crisis was their primary focus on domestic policy rather then trade policy. Domestic government interventions, particularly in capital and product markets, were related to two key areas: large-scale

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11 http://www.investopedia.com/terms/p/protectionism.asp#axzz1eEoP26BE
bailouts and subsidies, and fiscal-stimulus packages, usually combined with loose and unorthodox monetary policies.\textsuperscript{14}

Such measures have led to a change in the perception of protectionism: from border measures to non-border measures which is somehow equivalent to a change from trade-related measures to economy-wide measures. In this new context, the broad sense of protectionism does not refer to trade protection, but to economy protection, particularly in the case of emerging economies, such as some of the BRICS, or countries like Argentina. In all these circumstances, the broad sense of protectionist measures is related to industrial policies, and can be seen as an adaptation of these emerging economic powers to their new global role.

**Financial protectionism**

A new form of protectionism is emerging, although it is too early to define it properly: financial protectionism or financial mercantilism.\textsuperscript{15} This new form of protectionism was mentioned in a reference contribution issued by the Research Unit of the Bank of England, and was defined as “the preference of banks to lend money at home (that is, in the country of origin of the home bank) at the expense of foreign affiliates of the home banks”.

The confusing aspects refer to the fact that such practices were recorded but they were decided by the banks themselves (due to various vulnerabilities of the mother banks) or by the governments of the countries where the home banks were located in case the respective banks were nationalized or heavily supported in order to avoid bankruptcy. In our opinion, in such cases we cannot treat as similar two very different circumstances: protection from competition in case of classic protectionism and rescue in case of imminent risk of bankruptcy.

An opposite example for the role of home governments can be found in Romania. In March 2009, foreign banks operating in the Romanian banking sector (and which account for 70% of the total banking sector assets), committed under the umbrella of international organizations and representatives of their home country governments to maintain their exposure in the Romanian market.\textsuperscript{16} Hence, this time, the home country governments acted in the sense of preventing the private actors to behave in a protectionist manner, according to the proposed definition mentioned above (although the sense of protectionism here is rather different from the classic one).

**Protectionism related to the activity of state owned TNCs**

The rising role of BRICS in the world economy has been accompanied by the emergence of a new type of transnational corporations – the state owned TNCs. According to UNCTAD, in 2010 there were 650 state owned TNCs with about 8,500

\textsuperscript{14} Fredrik Erixon, Razeen Sally - Trade, Globalization and Emerging Protectionism since the Crisis, ECIPE Working Paper No. 2/2010.


foreign affiliates. While they represented about 1% of the total number of TNCs, they accounted for 11% of global outward investment flows. The presence of state owned TNCs raised some fears and apprehensions in the host countries which enacted some restrictive and defensive regulations in order to protect certain aspects related to their national security.

Again, in this specific area, we have a significant departure from the classic situation in which a state might aim to support companies from the respective country in their competition with foreign firms. Under these new circumstances, we have a state that is trying to limit the influence of other states on its territory manifested by means of state owned companies belonging to the foreign state. It is, indeed, a complicated situation, particularly when the foreign state is based on a centrally planned system (the case of China) or belongs to a distinct cultural system in comparison with the West (the case of Arab countries).

Other protectionist measures

The crisis raised a number of challenges to the governments in developed and developing countries, but these challenges are different. In the developed economies, in certain cases the banks had to be rescued or some private industrial companies. In election years (like 2012), jobs have to be preserved and the citizens have to be reassured that migrant workers will not take their jobs. When state owned TNCs want to buy assets in sensitive sectors (such as energy, transportation, banking or agriculture), the governments may also raise national security issues.

In the developing economies, the possibilities of governments to enact protectionist measures are limited by their financial availabilities. Therefore, in this group of countries we differentiate between emerging economic powers and the rest of countries. The latter countries react as followers. The emerging economic powers, on the other hand, want to assert their position, and therefore consolidate local industries that are large enough to compete internationally, but still not on par with their counterparts from developed countries.

Quite often, another type of protectionist measures may appear: the use of standards (or technical barriers). Here, governments act frequently as a result of lobby activity. Therefore, all countries need a much clearer regulation of lobby activity in order to prevent the “confiscation” of the state by the large corporations that are tempted to use some “monopolistic” position, at least for a period of time.

A particular situation refers to natural resources. In this sector, a new phenomenon is emerging in 2011 (and is expected to continue in 2012), namely resource nationalism. Due to the crisis situation, many governments are looking to control budget deficits and get more revenues. And one available solution seems to be the increase of taxes and royalties related to mining activities, together with enhancing local participation in projects or even nationalization of resources.

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Among the countries that already initiated or are in the process of implementing such measures are: South Africa, Zambia, Ecuador, Australia, Guinea, Zimbabwe. In the long term, the trend towards nationalization of resources represents a bigger risk, given the increase of population in many developing countries and the demands for better living standards in these countries.

Conclusions
The world economy is going through a period that witnesses both a repositioning of world economic powers and the search for a new development paradigm. Since the 1990s, a number of really significant phenomena were recorded:

➢ The world ceased to be bi-polar and moved to a uni-polar structure, with the United States of America as the superpower. Currently the world economy is gradually shifting towards a multi-polar structure.

➢ The emerging economies, with the noted presence among them of the BRICs (Brazil, India, Russia, India and China) which became in 2011 BRICS (through the addition of South Africa) gradually increased their position in world trade and world FDI flows.

➢ China acquired the status of the second largest economy in the world, and passed Germany as the world's top exporter.

➢ The crisis that started initially as a financial crisis turned subsequently into an economic crisis: it is actually a crisis of the postbellum Western development paradigm.

➢ World population reached 7 billion inhabitants in 2011, and is expected to exceed 8 billion in 2030.

If we were to take into account only the above mentioned aspects (and there are much more than that) we could easily conclude that a new world order is an objective necessity.

We do not discuss or propose here a certain world order, we just point out that given the magnitude of the above mentioned changes a new world order that will take into account all these changes is necessary.

Again, given the complexity of the world economy and the level of interdependence induced by globalization, such a new world order can not be designed or implemented in one step. A decade or even more may be necessary for experimenting, negotiating, testing and hopefully reaching a stable new paradigm of development and international relations.

During this interregnum period, some of the old actors are replaced by new ones and the remaining actors are no longer the same (just think about what is going on with the European Union or the changing position and role of the US). Various interests are to be manifested and harmonized and some of the actors even have to discover what their interests really are.

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During such a period, protectionism is obviously present, however not in a mercantilist sense, but rather in a global sense. Protectionism has to be seen at a number of levels:

- Crisis-induced protectionism (when the state is assisting industries in difficulty and takes measures to secure the rebalancing of assisted companies and to prevent government money from going abroad). This is supposed to be temporary and limited. Given the multilateral rules and disciplines of the WTO and the web of preferential (bilateral and regional) trade agreements as well as the intrinsic characteristics of globalization, this type of protectionism cannot extend to a large scale in time and space.

- Protectionism generated by emerging economic powers (BRICS and others). This type of protectionism is also limited in time, and is likely to last just until the new powers negotiate a relatively stable position for themselves within the new world economic order.

- Protectionism related to some rare resources (the case of rare earths, for instance, which include seventeen chemical elements). This is also likely to be limited in time, till the new technologies will allow for a relatively fast replacement of the true rare substances with more abundant ones. A good example is provided by China’s export restrictions imposed on rare earth metals; as the country accounts for 94% of world production, these measures have initially triggered a sharp increase in prices, followed by a major decrease both in demand and prices.

- Protectionism related to securing jobs for local subjects. Such measures can be found at present in some of the member states of the European Union, even in relation to other European citizens, as defined by The Treaty on the Functioning of the European Union.²⁰ But such measures cannot resist, at least in the European Union, for a simple reason: the demographic problem or the so-called aging population problem.

- Protectionism related to measures on public procurement, foreign investment or standards. This again is temporary, because in many countries the presence of foreign investors is so substantial that the functioning of the economy is not anymore conceivable in the long term without foreign capital.

- In contrast to all the types of protectionism mentioned above, protectionism related to resource nationalization is a risk for the longer run. According to an interesting comparison made by Sir Mohammad Jaafar²¹ in 2030 we would need the equivalent of three Earths in resources to guarantee the European living standards for everybody, and the equivalent of five Earths in resources to ensure the US living standards. In order to limit the risk of this type of protectionism, a real time race

should take place between the increase in demand for resources and the results from research and innovation to provide alternatives.

The magnitude of the problems related to the crisis, the demographics, the climate changes and so on, is so huge that it requires more coordination among all participants. The idea of global or regional governance is already manifest and we expects it to grow in the coming years. We already have G-20 (instead of G-7 or G-8) at the global level, and we have the discussions and debates related to a new European Union, more politically integrated.

Under these circumstances, we may expect a lot of temporary protectionist measures, however with a limited impact on the world economy. In the words of some often cited authors, the medium if not the long-term perspective, will be characterized by a “murky”\(^{22}\) and “creeping”\(^{23}\) protectionism. But as long as these forms of protectionism are affecting only 2\% of world trade, we remain optimistic.

We may be less optimistic as far as resources are concerned, but we do hope these are still substantial and that science and technology may lead us all to a real sustainable development.
