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PROTECTIONIST PRACTICES AS A METHOD OF RESTORING THE TRADE BALANCE

Abstract

Objective: This paper is an attempt to examine protectionist practices, illustrated using the example of the United States, as a means of establishing equilibrium in the trade and current account balance, especially under competitive conditions in pursuit of economic and world leadership.
Research Design & Methods: The research offers conclusions based on an analysis of the literature on the effectiveness of protectionist practices in economic relationships between countries and presents the reasons for the widening trade and current account imbalances. It also describes the results of a simulation on the implementation of punitive tariffs (by both parties) achieved using numerical models.
Findings: Protectionist practices are ineffective instruments for handling trade deficits. Moreover, they undermine international trade principles, lead to conflicts between the countries, and instigate symmetric retaliatory actions.
Implications/Recommendations: Apart from the overall ineffectiveness of protectionist practices in terms of optimising the trade and current account balance, there are adverse implications which may be beneficial to certain domestic groups of stakeholders while, on the international level, protectionist practices signify an attempt to weaken the position of other competitors in pursuit of world leadership.
Contribution: The paper shows that protectionist practices pursued by countries are ineffective instruments for handling trade deficits. Their application restricts technology transfer, deflates the efficiency and effectiveness of an economy and reduces

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welfare. Building actual civilisational and economic supremacy requires economic development in the real economy and cannot be achieved by administrative means.

Keywords: free trade, protectionist practices, trade deficit, world currency, rivalry for world leadership.
JEL Classification: F13, F4, F47.

1. Introduction

The scale and dynamics change in the modern world is giving rise to a prevalent sense of plunging into chaos and instability, both geopolitically and economically. The international standing of the US as the only political hegemon and key economic power worldwide is questioned increasingly often, mainly due to the incredibly rapid economic development of China, whose trade and currency practices and military steps are undermining relations between the existing leader and the new pretender. Punitive and retaliatory tariffs, imposed by America's trade partners, are among the instruments employed by the US in this confrontation.

This paper attempts to examine the economic rationale for a customs war as a means of reducing trade imbalance. The conclusions, formulated by specialists and based on economic experience and the effects of protectionist practices simulated by renowned analytical and research firms, make relative the ostensible objectives of non-economic state policies, intended to revise the current arrangement of international global relations, particularly in the long term.

The objective is explained by addressing a range of issues. Presentation of the aims of the study and its topical nature is followed by a discussion of customs and other forms of trade protectionism. Consideration of the consequences of punitive tariffs and trade partners' responses is inspired by current theoretical debate. The causes of persistent trade and current account imbalances are identified, namely, the practice of offshoring and economic policy errors in the face of an escalating economic confrontation between the superpowers. The state of imbalance is illustrated with statistics concerning the US economy. The possible effects of a customs war are shown in a simulation using the GIMP model. The paper ends by offering some conclusions.

2. Trade Protectionism

Trade protectionism encompasses a range of forms of state interference with principles and conditions of international trade in goods and services

intended to bolster the status of domestic at the expense of foreign manufacturers in a given industry by imposing higher import duties, cutting costs of local production or obstructing access of foreign suppliers to an internal market. Such means comprise (Abboushi 2010, p. 387; Anusz 2005):

– additional (punitive) import duties, including anti-dumping duties, in contravention of WTO agreements,

– quantitative quotas on imports of foreign products to restrict their flow into a local market and to raise their prices, including voluntary export reductions,

– subsidies and compensatory instruments for domestic manufacturers in the form of tax reliefs or direct cash transfers,

– administrative barriers, that is, imposed standards, specifications, fees, certificates, obligatory contributions of domestic manufacturers, and other technical and sanitary barriers,

– restrictions on access to foreign currency to make foreign products more expensive and domestic products cheaper.

Advocates of protectionist measures also resort to arguments involving: national defence, trade deficits, employment, reliefs for new industries, and free trade. Those reasons, though apparently attractive, are usually wrong. Their political discourse appeals to populist sensibilities and emotions. Thus, although national defence requirements may substantiate more restrictive policies on the transfer of military technologies, they require subsidies to research and produce more advanced military equipment rather than restrictions on military imports due to the range of links between states and military concerns as part of military blocs.

3. Effects of Punitive Tariffs in Theory, Empirical Studies, and the Practice of International Trade

Economics textbooks (Bowden & Bowden 2002, p. 748) usually illustrate the consequences of customs duties visually with the aid of charts. Within a system of coordinates denoting production volume and prices, for intersecting supply and demand curves for a given commodity, as the price of a product increases depending on the scale of tariff hikes, the volume of the commodity in the market shrinks, manufacturers record greater surpluses, more tax is collected, and consumers experience losses. The latter outweigh the benefits to domestic manufacturers.

Specialist literature also contains a number of empirical technical (statistical and econometric) studies of the effects of tariff impositions

intended to limit trade deficits, which generate similar results. A review of this research, including of their own studies, is provided by Kaempfer, Tower and Willett (2002). It shows that import restrictions reduce exports without bringing permanent and desired changes to the trade balance. Such protectionist policies lead to the ineffective allocation of resources and fail to reduce the deficit. The authors propose policies of budget deficit restriction as the most effective instruments for limiting current account deficits as such policies anticipate reductions in trade deficits. Limiting imports is not recommended as it cuts potential GDP (Lester 2016).

Arguments against trade protectionism other than economic ones are voiced increasingly often as the latter are often inspired by populist political assumptions intended to satisfy particular interest groups and win the approval of the electorate. Research demonstrates that customs duties are a costly negative-sum political game rather than a positive tool that can help maximise welfare owing to interactions, interchangeability and the effective use of capital.

Protectionist tariffs played an especially sinister role in the aftermath of the Smoot-Hawley Tariff Act in 1930, which exacerbated the Great Depression. Under pressure from influential interest groups, duties were levied on more than 20,000 commodities. It was only the repeal of the law in 1934 and the adoption of a new policy of trade agreements based on mutual respect for partners' interests which in time helped to lay the foundations of the global trade system. GATT (the General Agreement on Tariffs and Trade – 1947) and its descendant – the WTO (World Trade Organisation – 1995) were established as a result.

The relations between overall tariff rates and rates of GDP growth in the US between 1990 and 2015 indicate a negative correlation of (–)52% (Penlington 2017). If a 3-year lag of the impact of tariffs on the economy is taken into account, it rises to (–)73% for a 3-year moving average. Figures relating to the European Union in the same period do not affirm a correlation and even exhibit a negative correlation of (–)20% assuming a 3-year moving average.

The impact of trust and confidence in future policies on international trade is corroborated by earlier research into anti-dumping tariffs (Crowley, Song & Meng 2017). It has shown China joining the WTO has largely relieved Chinese fears of anti-dumping tariffs and contributed to the growth of Chinese exports to the US. A study of Chinese business entering external markets under conditions of imminent anti-dumping tariffs, conducted in 17 countries in 2001–2009 and based on Chinese customs transaction

figures, has demonstrated that 1399 manufacturers and 319 trading companies did not decide to enter new markets for that reason.

4. The Debate on the Consequences of Punitive Tariffs for the Trade Balance

A dispute concerning the theses in P. Krugman's brief analysis of the expected effects of a possible general tariff hike by the US (Dorman 2016) has evolved into a debate on the rationale for punitive tariffs. The author points out that increasing a country's current account deficit is balanced by capital inflows (increased debt) in its capital account. Capital flows are affected by returns on investment offered, while real rates of exchange ensure the balancing of both streams: current account deficit and capital transfer. The author proceeds to claim that appreciation of the currency, which helps to restore the earlier equilibrium with lower volumes of imports and exports, is the initial effect of raising import duties given a trade deficit. This is, however, at the expense of the reduced attractiveness of financial assets of the country increasing its tariffs as export receipts in the exporting country diminish. Pressure is generated, therefore, to weaken the rate of exchange and thereby reduce the trade deficit, which can turn into a surplus. This effect arises without recourse to protectionist practices since the attractiveness of a country's capital assets depends on its future exports. Trade deficits (insufficient exports) require persistently weakening currencies in order to attract investment (depreciation of domestic assets), which sooner or later leads to trade surpluses. Krugman believes, meanwhile, that the restoration of the necessary trade equilibrium by protectionist means requires a more thoroughgoing asset depreciation to trigger flow shifts in conditions of a less open economy compared to the option of allowing matters to run their course – he is unequivocally against protectionist practices as a result.

Countering this argument, Dorman points out that Krugman, like many other authors, wrongly treats the expression: "the total of current and financial account balances is zero" as an equation, and not as an identity. This distinction is necessary in order to note this is not a cause-and-effect process: a current account deficit is not equal to an automatic surplus in the capital account, since these are two methods of measuring the same quantity. This is because a buyer's expenditure on a commodity manufactured domestically is income for its manufacturer (supplier) and, domestically, it means an identity, not a process balancing both sides of the transaction.

In the case of a foreign commodity, a domestic buyer's expenditure corresponds to the foreign supplier's income. Savings fall domestically, and a foreign debt arises from the transaction. An identity occurs instantly and is always true. It does not mean, in particular, that a deficit is balanced with a capital transfer later on along the time axis. A country's balance of payments is a result of many microeconomic decisions to purchase domestic or foreign products, trade in portfolio assets or even manipulate rates of exchange. A single factor cannot be distinguished at the level of balance of payments where another results from a certain cause-and-effect process arising from the former factor. In practice, the balance of payments is affected by a number of factors, most commonly operating in a variety of directions; its volume is hard to anticipate in actual conditions. This does not undermine the ever-applicable identity of a current account deficit and capital account surplus. Krugman's other assumption is related to the impact of the reduced openness of an economy on attracting foreign investment. The prospect of repatriating capital income and profits is the pull factor. A continuing deficit/surplus in the balance of payments is unsustainable in the longer term. The equilibrium is restored by depreciation of the national currency. As the depreciation is expected, income denominated in the importer's currency becomes less attractive to the exporter. Shifts in the balance of payments from deficit to surplus, caused by the dynamic cycle of deficit escalation and liquidation, require empirical verification. There are no countries that experience, by turns, deficits and surpluses in their payment balances. Countries tend to maintain chronic surpluses; those are raw material exporters who prefer an export-based model of development: Asian and some European countries. Another group consists of countries maintaining long-term deficits. Heavy international competition at the micro level and mobilisation of savings at the macro level are factors in this differentiation.

5. Mechanism of the US Trade Imbalance. Economic Rivalry of the US and China

5.1. General Remarks

The trade imbalance of the US is a result of that country's de--industrialisation caused by an excessively widespread relocation of manufacturing abroad (offshoring) and defective economic policies that risk loss of intellectual property and undermine the national interest in the name

of short-term economic gains. These policies are bolstered by the dollar's status as the global accounting currency and the practice of maintaining persistent export surpluses by key trade partners of the US.

5.2. Offshoring

America's trade turnover with China has persistently shown very high deficits. It should be remembered, however, that this is largely due to exports of goods made in China by American concerns. The process of locating production abroad, known as offshoring, is motivated by a desire to obtain the benefits (premium) of cheaper labour and compliance costs. Offshoring has generated more profits, more management bonuses, and capital gains for shareholders. Roberts (2018) reports that the US lost 54,621 manufacturing plants in the first decade of the 21st century, only partly due to bankruptcies by their own fault, and industrial employment fell by 5 million. More than 40% involved plants with staff of more than 500. Losses of jobs previously performed by the middle class caused incomes to decline and jeopardised the economic prospects of the middle class, municipal finances, the solvency of pension funds, and the provision of public services. The Fed, chaired by Alan Greenspan at the time, adopted a policy of stimulating consumer credit (debt), due to the stagnant incomes of workers losing their US jobs, in order to generate economic growth. The disappearance of the consumer market, as manufacturing of consumer goods was offshored, mainly to China, caused a loss of competitiveness in these sectors and lowered standards of living.

The policy of credit expansion led to overheating of the real estate market and, as the Glass-Steagall Act was revoked and an extensive market in MBS (mortgage-backed securities) emerged, it became the cause of the credit crunch in 2007–2008. In response, the Fed proceeded to rescue the big banks, rather than let them fail, by redeeming debt instruments (bonds). It offered to purchase them at the real market price, not the notional price set by market players without the regulator's interference. This policy of purchasing, also referred to as quantitative easing (QE), brought interest rates down virtually to zero or, if inflation is taken into account, below zero. This helped to improve the valuation of the assets of banks at risk and assured their solvency. The policies of cheap money and forceful offshoring have made all segments of the economy (consumers, government, and businesses) heavily indebted. The absence of a sufficiently robust consumer market has stifled economic growth, which requires the support of monetary (credit) and fiscal (taxation) policy measures.

It should be added, as an aside, that the defence of the value of dollar as the global reserve currency is key to maintaining the US's status as an economic and military power.

5.3. De-industrialisation of the US in the Case of Steel- and Aluminium-making Industries

The collapse of American metallurgy, which has turned an industrial region into a "rust belt" of earth, reaches as far back as the 1950s (Pozhidaev 2018). In 1950, 88 million tonnes of steel were produced out of the Mesabi Iron Range, relying on cheap labour. Production was based on open hearth furnaces at the time. As the deposits neared depletion and steel-makers went on a long strike in 1959, major imports of steel, chiefly from Japan, were initiated. They soon outweighed domestic output. Foreign, mainly Japanese and European suppliers switched to innovative forms of manufacturing: oxygen convertors and continuous casting. Steel was still made using outdated methods up until the late 1970s. As modernisation was attempted by opening small mills and demand for steel declined owing to the greater use of non-metallic materials and state-of-the-art technologies, particularly in the motor and construction industries, the share of imports fell. More steel was produced in the 1980s as a result of protectionist steps in response to price rises. It reached 88.2 million tonnes following the 2008–2009 crisis (2014), falling back to 81.6 million tonnes in 2017, compared to imports of 34.6 million tonnes, mainly from Canada, Brazil, and Korea. Currently, imports account for approximately one third of the domestic market. Thus, American metallurgy is behind its foreign competitors, who produce cheaper and more innovatively.

The circumstances of the aluminium-making sector are even grimmer. At their peak in the 1980s, the US produced approximately 5 million tonnes of aluminium per annum. In 2017, it made a mere 0.84 million tonnes, with 90% of internal demand being met by imports, chiefly from Canada, Russia, and the UAE. It became unprofitable to produce aluminium in the US.

Thus, the real reason for resorting to protectionist measures is the relative technological gap in steel- and aluminium-making, insufficient and usually late modernisation efforts, and tolerance of national security risks through excessive dependence on foreign supplies. It remains to be seen whether the imposition of duties on steel and aluminium, which has already hiked their prices in the internal market, will significantly increase the share of domestic output in their consumption and cut the trade deficits in these materials.

5.4. Economic Rivalry between the US and China

The US and China have had an intensifying dispute about market access, respect for intellectual property rights, and the size of the trade deficit (Bremner 2018). The dispute is accompanied by military actions, which are beyond the scope of this paper. What we are witnessing is a conflict between superpowers for global influence. China has achieved impressive economic success at a record-breaking rate, matching the US in the manufacture of high-technology products, including robotics, telecommunications, military production, and artificial intelligence (AI). This is a war of civilisations for the choice between the market economy model and the state-controlled market economy model. A tariff war, initiated by the US to impose steel and aluminium import duties of 25% and 10%, respectively, was followed by two-staged 25% tariffs on Chinese goods worth USD 50 billion (34 and 16 billion) and a promise of more measures against Chinese imports worth USD 200 billion, particularly if the new higher American tariffs are met with Chinese counter--tariffs. The US claims the tariffs have been imposed in response to "the theft of American intellectual property". Steel and aluminium tariffs will largely not affect China as these metals contribute little to Chinese exports. China has announced, however, that it will introduce its own retaliatory tariffs "of the same scale and intensity". The duties will be levied on soya, grain, beef, poultry, fish, dairy products, and vegetables. To begin with, China will restrict purchases of American soya, which it largely re-exports, and increase soya imports from other countries, principally Brazil and Argentina. Trade relations may become very tense if both the parties yield to jingoistic rhetoric. Other, predominantly Asian countries may suffer from the punitive tariffs as they supply components for goods China exports to America. As much as USD 20 billion of goods, out of USD 34 billion subject to the higher duties, are estimated to originate from other countries, including the US.

The US accuses China of various protectionist practices: enforced exports as part of maintaining persistent export surpluses, subsidising exports, manipulating rates of exchange, and administrative restrictions on access to its own market. The US believes that China makes access to its market conditional on technology transfer without paying the latter's full price. Many figures from the worlds of business, politics, and science advocate abandoning links with Asian networks and severing supply chains in high technology sectors or even relocating American suppliers who have been

manufacturing in China, such as Intel, Apple and Microsoft, to production parks in the US. The Americans maintain their technological advantage in the fields of space exploration, aviation, chemicals, and biotech. US exports to China mainly comprise means of transport, chiefly air transport, computers, electronics, and chemical products. Trade between the US and China in 2017 was heavily imbalanced. The US regards the expansion of such high technology businesses as Huawei Technologies, ZTE Corporation, and China Mobile in the American market as a threat to national security and considers introducing restrictions on Chinese firms in the aviation, space, and robotics industries.

It has been demonstrated above that tariff wars stifle international trade in goods and services and slow the development of national economies. Other remedies are also proposed to limit China's protectionist policies that breach good business practices. A complaint to the WTO is a possibility. This path is taken by countries affected by punitive American tariffs, although it is time-consuming and usually ineffective.

6. The US Trade Balance, Current Account Balance, and Balance of Payments

6.1. General Remarks

Populist politicians stress the need to reduce current account deficits especially strongly. The rationale for this idea is the mistaken belief that a current account deficit is in itself harmful to an economy. Studies of international trade fail to corroborate this thesis. A deficit in the current account, which obviously comprises trade balances of goods, services, net primary income (net direct investments, other financial assets, income from reserve assets and from wages) and net cash transfers (private transfers, government grants, pensions, insurance transfers), is identical with a positive balance in the financial account of the balance of payments. These balances, adjusted for the capital account balance of the current account, are not equal as a rule. The difference is constituted by a balance of omissions and errors. The balance also encompasses the capital account including transactions in non-production and non-financial assets.

6.2. The Trade Balance of the US in 2017. The Current Account Deficit

The trade deficit in goods and services totalled USD 552.4 billion in 2017, given exports of USD 2,329 billion and imports of USD 2,895 billion

(the numbers are not seasonally adjusted) – Kimberly (2018). Key exports are (in billion USD): investment goods (533.3), production materials and components (464.7), consumer goods (197.7), vehicles and car parts (157.7), and food, animal feed, and beverages (132.7). Investment goods (640.6), consumer goods (clothes and footwear, mobile phones, TV equipment and pharmaceutical products – 601.9), production materials and components (507.3), and food, animal feed and beverages (137.8) prevail among the imports. Thus, cheap imported consumer goods make the greatest contribution to the trade deficit and constitute a substantial part of spending by less well-off American consumers.

As far as commodity trade by countries is concerned, trade with China totalled USD 636 billion with the US deficit of USD 375 billion (below: 636/375), followed by Canada – 582/18, Mexico – 557/71, Japan – 204/69, and Germany – 171/65. Approximately two thirds of the goods deficit is accounted for by China, therefore.

The US can boast a surplus of USD 245.1 billion (below: in billion USD) in service trade, including trade in intellectual property (licence fees) – 77.1, travel services – 75.7, computer and business services – 52.1, and financial and insurance services – 48.1.

The volumes and structure of the initial current account of the US are illustrated in Figure 1, where the numbers are provided distributed (ranged) over quarters of the year.

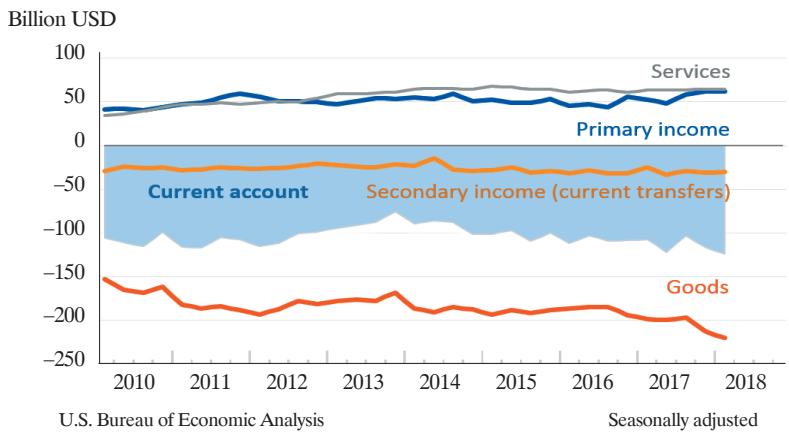

Fig. 1. Quarterly US Current-Account and Component Balances, 2010–2018

Source: SCB (2018).

The systematic increase in the commodity trade deficit, services balance surplus, surplus primary income, and deficit of cash transfers are noteworthy. Substantial current account deficits are also clear during the financial crisis of 2007–2008. The current account deficit in relation to American GDP in 2017 was 2.4%; in 1980–2017, it had averaged 2.64%. It reached a record level of –6.0% in 2006 (*United States…* 2018).

6.3. The US Balance of Payments in 2017

The balance of payments of the US in 2017 (USD billion, revised; the numbers are seasonally adjusted, possible rounding errors) totalled –424.4, including the trade balance (–552.3), the balance of commodity exports (–807.5), and balance of services (+255.2). The current account including the balance of primary income and cash transfers (103.1) totalled –449.2. The capital account's balance totalled 24.8, and the financial account balance was –331.9 given a balance of statistical differences due to errors and omissions equal to 92.5. In Q1 2018, the trade deficit was 155.6, the current account balance –124.1, the capital account 0.0, and the financial account –180.6, with a balance of statistical differences of –56.5.

The escalating customs and trade war between the US and the rest of the world may prove dangerous to the American economy itself. Tariffs and counter-tariffs undermine confidence in international trade, traditional relations, and readiness to make investments, giving rise to uncertainty regarding long-term capital allocation decisions. In the circumstances, customs and trade policies become inconsistent and unpredictable.

The current economic performance of the US is exceptionally good, owing, *inter alia*, to tax cuts. GDP growth in Q2 is estimated at 4.5%, compared with 2.2% in the 1st quarter. Pushing for a trade war is tempting as the initial position of the US appears stronger, since the American economy relies on its internal, highly absorptive market to a larger extent than its competitor economies, particularly China, Japan, and Germany. US exports account for 12% of American GDP, whereas they constitute 20% in China and 43% in the EU (Miller 2018). Countries affected by US tariffs may resort to a number of countermeasures, including: retaliatory duties at symmetrical levels, delayed customs clearance, tax auditing and more stringent administrative regulations, disputes at the WTO, devaluation of national currencies, and reduction of dollar denominated currency reserves. The depletion of China's extraordinarily high surpluses in its trade with the US, given high liabilities in the American currency, may force financial authorities to cut Chinese strategic reserves by selling out American

bonds. This would in turn force the FED to offer higher rates of interest when issuing new bond tranches. Most measures and countermeasures are obviously double-edged.

As a result of a tariff war, multinationals will produce locally, relocate their manufacturing to their native countries that provide great sales markets or to countries of local fiscal jurisdictions.

7. Simulated Effects of Punitive Tariffs Levied on Imports into the US

The impact of customs duties on overall demand is unequivocal. Raising tariffs means higher domestic prices, thus improving the position and revenue of domestic manufacturers, while consumers (households) and other manufacturers using imported goods as raw materials for their own products lose. Budget revenue grows as well, although dispersed across an entire economy. Thus, profits and losses evolve in a variety of ways and their influence on overall demand seems to be determined by the scale and extent of tariff hikes. Analysis of the impact on aggregated demand is not applicable to the Keynesian approach, which assumes fixed pricing and rates of exchange (Davies 2018). It should be also remembered that growing tariffs mean losses for exporters. Robert Mundell (after Obstfeld 2016) has demonstrated that new commodity import tariffs in conditions of variable exchange rates tend to improve the trade balance yet also strengthen the real rate of the dollar. The growth of the dollar's real value will prove to be the key influence on the US economy, causing a general decline in production and employment in spite of the relatively weaker positive effect of a reduced trade deficit. The overall decline of GDP and employment (*ceteris paribus*) will ultimately exacerbate the trade deficit. The effect will be greater at zero rates of interest as the issuing bank is unable to effectively counteract the adverse impact of tariff rises by means of fiscal policy. The effects of increasing tariffs are illustrated in the following figures. They show the response of real economic quantities (GDP, rate of exchange – Figure 2; import and export – Figure 3) in the US after duties on imports from the emerging East Asian countries are raised by 20%. It is also assumed that the Fed's rate of interest is zero and the rate of interest of the exporting countries is other than zero. Were the Fed's rate positive, the effect of the tariffs would be more limited. The figures present the consequences for two assumptions: a) exporters fail to impose counter-tariffs (fail to respond), b) exporters apply retaliatory measures. The figures were prepared using a forecasting and research tool employed by the IMF – the Global Integrated

Monetary and Fiscal Model. Figure 2 shows that US GDP falls by between 0.5% and approx. 1.2% under both scenarios within 5 years, that is, as the full impact of the tariff manoeuvring is felt. The dollar's rate of exchange increases by 2% to more than 5%.

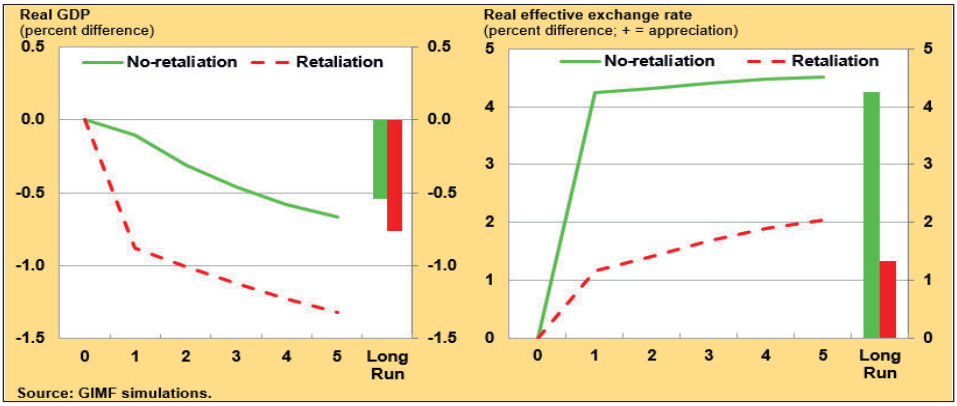

Fig. 2. Macroeconomic Impact in the United States from Imposing Tariffs on Imported Goods

Source: simulations using the Global Integrated Monetary and Fiscal Model (Obstfeld 2016).

Figure 3 shows that tariffs depress imports by more than 6%; exports fall faster (up to –6% in the first year and more, up to –8%, later. The dollar, stronger owing to the tariffs, makes imports from alternative sources more attractive (subsidises greater imports) while charging (taxing) US exports. This affects the trade balance, since exports diminish relatively faster than imports, and GDP and employment decline as well. Consumers may derive certain benefits then, as real consumption climbs owing to imports made cheaper by the dollar's higher exchange rate; these are rather broadly dispersed and insignificant, however, without recompensing the job losses. It should also be pointed out that domestic jobs do enjoy protection in the initial period of higher tariffs, to be eroded, though, due to the market's response (falling exports).

There is an entrenched conviction in economic theory that raising tariffs leads to reduced volumes of international trade, restricted technology transfers, and consequently to lower (increasing more slowly) work efficiency and welfare.

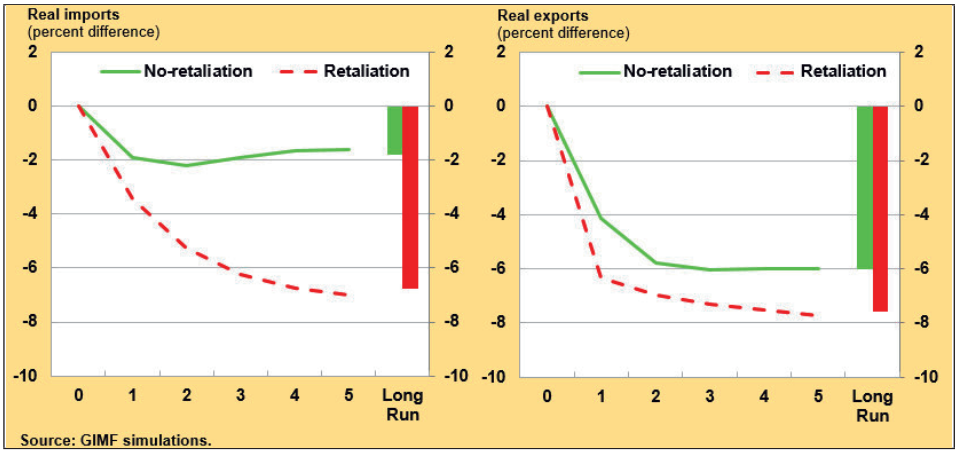

Fig. 3. Impact on United States' Trade from Imposing Tariffs on Imported Goods
Source: simulations using the Global Integrated Monetary and Fiscal Model (Obstfeld 2016).

Both economic theory grounded in Ricardo's concept of comparative advantage and extensive economic practice point to benefits of international trade. This is because expanding trade reduces costs per unit of production, forcing manufacturers to keep making their products more attractive in cost and functional terms and boosting consumption. These benefits are reaffirmed by a range of technical research. For instance, a World Bank study of 1963–1973 (Abboushi 2010, p. 386) shows that the growth of economies with the most liberal principles of trade averaged 6.9%, compared to 1.6% in countries applying restrictive policies. The price of restrictions is high. Hufbauer (after Abboushi 2010, p. 389) examined 31 cases of domestic industry protection and found that the price was more than USD 100 million in 25 cases and USD 27 billion a year in the textile and clothing industries. What is more, maintaining a single workplace cost more than USD 100,000 in the majority of cases.

The current US administration's use of punitive tariffs, mainly in trade with China, is an attempt to exert economic pressure in their multidimensional dispute over world leadership. The economic and geopolitical status of the US has been gradually eroded by the unprecedented, rapid economic rise of China and other countries. This process is well illustrated by the fact that the US economy produced a half of global GDP in 1950 compared with a little more than 20% at present. There is a clear and sharp conflict of interest among world leaders.

Protectionist measures will encounter resolute resistance, though. Opponents of the US are interested in maintaining free trade principles. China, like India, Germany and other countries, cannot develop only by forcing internal consumption; they would in effect be developing at the expense of exports. International financial institutions are against protectionism as well.

Retaliatory tariffs have introduced uncertainty to global politics. A genuine threat has emerged that chains of cooperation (added value creation), extended over decades, will be severed. Protectionism will break those chains, and the growth rates of countries engaging in the tariff war will decline. Protectionism is always a zero-sum game: no one wins (Raghuram 2018). A trade war is a relatively straightforward way of abolishing contradictions (conflict) if it is limited to a customs war only. Its consequences may be far graver if it is followed by manipulation of exchange rates, the most powerful weapon of protectionism.

The steps taken by the US are calculated to win approval of the electorate, workers of factories that have moved abroad, engineering staff, and the impoverished middle class. The earlier fall in employment was caused by uncontrolled offshoring that has resulted in the US losing its position in the competitive war; large swathes of the US economy have been de-industrialised, and investment in IT technologies, the digital economy, and artificial intelligence is insufficient (Gajva 2018). A return to full industrialisation of the US is impossible without conflict, whereas continued de-industrialisation is unacceptable.

8. Conclusion

Both economic theory and the practice of international economic relations are quite clear about treating tariff increases as ineffective instruments for handling trade deficits. Their application restricts technology transfer, deflates the efficiency and effectiveness of an economy, and reduces welfare (GDP). Research into the rationale for applying tariffs should be considered in their broader connection with recommendations implied by strategies for renegotiating trade agreements and with game theory.

The relative attractiveness of customs duties as import restrictions is prone to the temptation of populist appeals to protect domestic industry and local workplaces and does not serve the needs of an economy as a whole. It usually serves the temporary purpose of winning political support and

mobilising public opinion in defence of slogans such as "Make America Great Again". In the international dimension, it enhances an economic and military power's standing in its rivalry for global leadership by (briefly) weakening its opponents.

National economies develop vigorously owing to free trade. They grow rapidly after spot-on investments in areas of maximum added value, which require adequate institutional support and substantial investment in fixed assets.

The US dollar is the leading global currency of accounting. Reserves are saved predominantly in this currency. This builds excessive pressure to obtain the American currency by means of export surpluses, to be invested in the American treasuries, which helps the US balance its profound current account deficits. This pushes up domestic consumption at the expense of rocketing foreign (external) debt. This process is unlikely to continue *ad infinitum* and will probably end by undermining the role of dollar as the underlying world currency and, in time, the status of the US as a world power.

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