Free Trade

Meaning

- Free trade promotes unhindered exchange of goods and services across international borders.
- Under free trade policies, goods and services can be bought and sold across international borders with no government tariffs, quotas, subsidies, or prohibitions to inhibit their exchange.
- Free trade policy is also known as laissez fair policy, in which the government does not have any role in the transection of goods and services across borders.

History

- Mercantilism (16th to 18th centuries): accumulating precious metals (especially gold and silver) through a favourable balance of trade like import restriction and export expansion policy.
- Physiocrats (18th century): A group of French economists known as the physiocrats challenged mercantilist policies and advocated for laissez-faire economics and free trade.
- Corn Laws and British Free Trade Movement (19th century): In the early 19th century, Britain faced protectionist policies like the Corn Laws, which imposed tariffs on grain imports.
- Cobden-Chevalier Treaty (1860): This treaty between Britain and France to reduce tariffs and trade restrictions between the two countries, setting a precedent for future free trade agreements.
- Interwar Period and Protectionism (1919-1939): The aftermath of World War I saw a resurgence of protectionist measures as countries tried to shield their economies from the effects of the Great Depression. The collapse of international trade.
- Post-World War II Era: Institutions like the General Agreement on Tariffs and Trade (GATT), which later became the World Trade Organization (WTO), were established to facilitate free trade and reduce trade barriers.
- Modern Free Trade Agreements (post 1990): numerous regional and bilateral trade agreements have been negotiated to further liberalize trade. Like the North American Free Trade Agreement (NAFTA), the European Union's single market, and the Trans-Pacific Partnership (TPP), G-20.

The argument in favour of free trade

- **Comparative Advantage**
  - Comparative advantage holds that all countries will always benefit from cooperation and participation in free trade.
  - The law of comparative advantage refers to a country's comparative ability to produce goods and services at a lower cost than other countries. The country can export goods and services in which it has a comparative advantage and import goods and services in which it has a comparative disadvantage.
  - World output will increase and production level will be more efficient
  - Each country will gain from trade compared to no trade
- Optimum allocation of resources
  - By promoting competition and specialization, free trade can lead to more efficient allocation of resources, lower production costs, and increased economic growth. Most efficient use of productive resources in the world.

Consumer Benefits:

- Free trade can lead to lower prices.
- When trade restrictions are removed, consumers tend to see lower prices because more products imported from countries with lower labour costs become available at the local level.
- This can improve the standard of living for people in importing countries.

Other Benefits to Consumer:

- The consumer have a wider variety of goods and services because it opens up access to products from around the world at competitive prices.

- Widen the size of the Market:
  - Free International trade widens the size of the market which increases the scope of production, specialization and division of labour.
  - All this leads to the minimization of cost and optimization world's material welfare.
- Equalization of Prices:
  - Free international trade tends to equalize both commodity and factor prices in all regions.
- Larger factor Income:
  - Under free international trade, the income of abundance factors of production will also increase as the country will use more abundance factors.

- **Check on Monopolies:**
  - Free trade promotes competition and prevents monopolistic tendencies
  - The fear of foreign competition does not permit producers at home to form monopolies and exploit the consumer by raising the price of the product.

- **Innovation and Entrepreneurship:**
  - Open markets foster competition, which can lead to increased innovation, higher product quality, and lower prices.
  - Businesses must continuously improve to stay competitive in a global market, benefiting consumers. (Example in the Movie industry, automobile industry)

Economic Development:

- Free trade can contribute to poverty reduction by creating economic opportunities, both within countries and between countries.
- It can provide access to global markets for businesses in developing nations, helping them grow and create jobs.
- Export is a major source of development for many Asian countries (China, South Korea, Singapore) (Bangladesh joining the path)
- Why does India fail to create export-oriented growth model?

Global Cooperation:

- In an interconnected world, addressing global challenges such as climate change, pandemics, and terrorism often requires international cooperation.
- Free trade can facilitate this cooperation by creating economic incentives for countries to work together on these issues.

Environmental Considerations:

- When countries trade, they may adopt each other's environmental standards and technologies, which can lead to the spread of cleaner and more sustainable practices. (Indian agricultural export and organic farming)

Reducing Corruption:

- Free trade can reduce opportunities for corruption by streamlining trade processes and reducing the need for excessive regulations and bureaucracies.
- Promote laissez fair economy.
- Interlink relationship between international trade and Corruption in India.

Global Peace and Cooperation:

- Proponents argue that free trade can foster international cooperation and reduce the likelihood of conflicts.
- When nations are economically interdependent, they have a vested interest in maintaining peaceful relations to ensure the smooth flow of goods and services across borders.

The argument against the free trade

- Full free trade policy has never been implemented by any country in the world.
- Unrealistic Policy:
  - The free trade policy is based on the assumption of laissez-faire policy.
  - Its success also requires the pre-condition of perfect competition.
  - But such a condition is unrealistic and does not exist in the real world.
- Non-Cooperation of Countries: (prisoners dilemma)
  - Free trade works smoothly if all countries cooperate with each other.
  - If some countries decide to gain more and impose import restrictions the system of free trade can not work.

- **Danger of Overdependence**
  - Overreliance on imports for essential goods such as food, energy, or pharmaceuticals can be viewed as a national security risk.
  - In times of crisis or conflict, disruptions in the global supply chain could leave a nation vulnerable.
- Political Slavery:
  - Economic Dependence leads to political slavery
  - For political freedom, economic independence is necessary. This requires to abandonment free trade
- The danger of risk pooling:
  - Free trade brings in the danger of risk pooling to other countries. A country may face economic depression if its international trading partner suffers from it.
  - The Great Depression that arose in 1929-30 in the US economy swept all over the world and all countries suffered badly even if their economies were not caught in the grip of the Depression.
  - Recent Economic Depression 2007-08, The failure of the banking sector of the US seriously affected every part of the world.

- Unbalanced Development:
    - The comparative advantage sector will only develop due to free trade but other sectors remain undeveloped
    - inefficient industries remain neglected.
- Dumping:
    - It refers to the practice of exporting goods to a foreign market at a price lower than the cost of production or below the price charged in the home market in order to capture the foreign market.
    - Free trade policy can not control the Dumping
- Harmful Product:
    - Under free trade injurious and harmful products may be produced and traded. Trade restrictions require to check the import of such products.

- International Monopoly :
  - It encourage the establishment of multi-national corporation.
  - These corporation tend to acquire monopoly position and harm the interest of local people (through price controlling)
  - Concerns exist that unfettered free trade can lead to the decline or even the extinction of entire domestic industries.
- **Job Displacement:**
  - Free trade can lead to job losses in certain industries, particularly those that cannot compete with lower-cost foreign producers.
  - This can result in unemployment and economic hardship for affected workers and communities.
- **Income Inequality:**
  - Critics argue that free trade can exacerbate income inequality within countries.
  - While it may benefit consumers with lower prices, it can lead to wage stagnation or decline in certain industries, while corporate profits rise. This can contribute to a growing wealth gap.

Exploitation of Labor:

- In pursuit of lower production costs, companies may outsource production to countries with lax labor standards.
- Critics argue that this can result in poor working conditions, low wages, and exploitation of workers in developing countries.

Trade Imbalances:

- Free trade can lead to trade imbalances, where one country consistently runs a trade deficit (imports more than it exports).
- Persistent trade deficits can lead to economic instability and dependence on foreign creditors.

Globalization's Negative Consequences:

- Free trade as a driving force behind broader negative consequences of globalization, including cultural homogenization, loss of cultural diversity, and the dominance of multinational corporations over local businesses.