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## What Can Be Learned From Crisis-Era Protectionism? An Initial Assessment

**Simon J. Evenett**, *University of St. Gallen and CEPR*

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# What Can Be Learned From Crisis-Era Protectionism? An Initial Assessment

Simon J. Evenett

## Abstract

Drawing upon a comprehensive database of contemporary protectionism, this paper offers an initial assessment of the extent to which our understanding of protectionism may have to evolve. While some long-standing features of protectionism appear to have endured (such as the distribution of discriminatory measures across economic sectors), specific corporate needs arising from the global financial crisis and particular national attributes are more likely to have influenced the choice of beggar-thy-neighbor policy instruments than binding trade rules and other international accords.

**KEYWORDS:** protectionism, economic crisis, discrimination

**Author Notes:** Simon J. Evenett is a Professor of International Trade and Economic Development, Department of Economics, University of St. Gallen, Switzerland, and Co-Director of the International Trade and Regional Economics Programme, Centre for Economic Policy Research (CEPR). The author coordinates the Global Trade Alert, an independent initiative to monitor the implications for international commerce of state measures taken during the recent global economic downturn, see [www.globaltradealert.org](http://www.globaltradealert.org) for details. Much of the evidence presented in this paper is drawn from this monitoring initiative. Thanks to the editor and two anonymous referees for comments received on an earlier version of the paper. Messages to Simon Evenett can be sent to [simon.evenett@unisg.ch](mailto:simon.evenett@unisg.ch).

## 1. Introduction.

The recent global economic crisis has posed a profound challenge to national policymakers, but does our understanding of protectionism need to be revised as well? Even though no definitive answer to this question can be given yet, enough information about contemporary crisis-era protectionism is now available to start sifting through the facts and identifying potentially fruitful lines of inquiry. The purpose of this paper is to do just that, drawing upon a comprehensive database of investigations into over 425 state initiatives announced by governments around the globe since the first Group of Twenty (G-20) crisis-related summit in November 2008.

Since the information presented in this paper is current through to mid-September 2009, the findings contained herein are potentially of interest to decision-makers as well as to analysts. Government officials, for example, will need to determine commercial policy priorities in the coming months and years, not least concerning the possible unwinding of discriminatory measures imposed since November 2008. They may also be interested in information reported here about the announced, but not yet implemented measures that are likely to entail discrimination against foreign commercial interests.<sup>1</sup> Scholars and other analysts may be interested in the choice of policy instruments and the extent to which international accords and initiatives influenced the patterns of state intervention. Turning from the positive to the prescriptive, such findings may influence assessment for proposals for further international trade obligations in what is often referred to as a rules-based multilateral trading system.

The remainder of this paper is organized as follows. In the second section the construction by the Global Trade Alert (GTA) team of a database on contemporary protectionism, that provides the evidential base for this paper, is described. An account of the emerging contours of crisis-era protectionism is provided in section three. Some observations are made there concerning what, if any, novel features are contained in contemporary crisis-era protectionism. Drawing upon elements of the extant literature, section four includes an evaluation of four hypotheses concerning the choice of beggar-thy-neighbor policy instruments during the current crisis. An evidence-based evaluation of the effectiveness of binding trade rules and the G-20 countries' no-protectionism pledge is presented in section five. Concluding remarks are offered in section six.

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<sup>1</sup> In this paper such measures are referred to as the protectionist pipeline or the protectionist measures in the pipeline.

## **2. The Global Trade Alert's database on contemporary protectionism.**

During the first half of 2009 many nations experienced substantial year-on-year reductions in their exports. Japanese exports, for example, fell by half. Concerns that such export contractions would be exacerbated by the widespread resort to protectionism lead a group of trade policy analysts, independent from government and international organizations, to establish an initiative to monitor whether state initiatives were being introduced that tilted the playing field against foreign commercial interests. The Global Trade Alert was organized and officially launched on 8 June 2009.

By the middle of September 2009 the GTA team had investigated over 425 state measures and posted reports on each of them on its dedicated website, [www.globaltradealert.org](http://www.globaltradealert.org). Two written reports have also been published, the second of which has been referred to as "authoritative."<sup>2</sup> Usage of the website, which includes a summary statistics page whereby country-specific, sector-specific, and policy instrument-specific information can be readily downloaded, has been extensive. By the end of September 2009, less than four months into the initiative's existence, over 3000 distinct users have consulted the GTA database nine or more times, suggesting frequent usage by a not inconsiderable portion of the community of trade policy analysts.<sup>3</sup> Several governments have sought memoranda and presentations from the GTA team.

The unit of observation in the GTA database is a (typically unilateral<sup>4</sup>) state initiative that at the time of its announcement might have implications for foreign commercial interests, the latter broadly conceived to include migrant workers, intellectual property deployed abroad, foreign investments as well as imports and exports. The GTA takes as a starting point state initiatives announced during or after November 2008 because in that month many heads of government committed themselves in international meetings (including the first crisis-related G-20 summit in Washington, D.C.) to eschew protectionism during this global

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<sup>2</sup> The second report of the Global Trade Alert can be downloaded at the following URL: <http://www.globaltradealert.org/gta-analysis/broken-promises-g20-summit-report-global-trade-alert>

<sup>3</sup> The size of this community has not been estimated with any precision. The author has consulted a number of trade analysts about this matter and estimates of the total number of persons worldwide likely to find the GTA database of regular interest vary from 5,000 to 20,000.

<sup>4</sup> The negotiation and conclusion of free trade agreements, bilateral investment treaties, and double taxation treaties are therefore outside of the scope of the GTA database. This design choice was made deliberately so that the focus would be on the unilateral state acts that governments undertake during the current global economic crisis. Having said that, there are a few instances where two or more governments have agreed to "manage trade" in a sector that are recorded in the GTA database.

economic downturn.<sup>5</sup> Had available resources permitted, it would be desirable to extend the database back to the onset of the subprime crisis in the third quarter of 2007 and possibly before (to provide a pre-crisis benchmark).

A state initiative could be as broad in scope as a state budget (so containing changes to many trade-related policy instruments) or as narrow as a tariff increase on a single product. The total number of policy instruments altered, therefore, exceeds the number of state initiatives reported in the GTA database, so the latter should not be taken as an indication of the former. No assumption is made that each initiative is comparable to every other initiative, although it is possible to sensibly group together initiatives involving the same policy instrument (such as anti-dumping investigations) and to distinguish some sets of initiatives from others (such as tariff increases from public procurement-related measures). Indeed, as described below, there is no presumption that the harm done by state initiatives, including those comprising the same types of policy instrument, is the same.

The GTA team comprises independent trade policy analysts from across the globe. When a team member spots an announcement of a potentially relevant state initiative (on a website, in newspapers and periodicals, and in the reports of national governments and international organizations), the first step taken is to verify the facts contained therein are consistent with information available from official sources. Occasionally, when verification from official sources is not possible, private sector traders are consulted to determine if there has been, or is planned, a change in state policy. The facts uncovered are used to ascertain whether the implementation of the state initiative in question would alter the relative treatment of the domestic and foreign commercial interests operating in the markets where the initiative's effects will be felt. In common parlance the GTA checks whether the state initiative tilts the "playing field" against foreign commercial interests.

A traffic light system was developed so that each initiative can be categorized in terms of its effects on foreign commercial interests: a red evaluation indicates that the initiative has been implemented and is almost certainly discriminatory; amber that either the initiative has yet to be implemented and once in force will almost certainly discriminate against foreign commercial interests, or the initiative has been implemented and is likely to be discriminatory, or the initiative contains a mix of policy interventions some that are discriminatory and some that are not. A green evaluation is given to an initiative that is either non-discriminatory, involves liberalization on a non-discriminatory

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<sup>5</sup> The November 2008 start date almost certainly implies that there are some financial sector bailouts that are not contained in the GTA database. Even so, the number of state aids, bailouts, and financial assistance in the GTA database exceeds the number of every other policy instrument reported therein.

(Most Favored Nation basis), or improves the transparency of aspects of the national trade regime.<sup>6</sup>

It should be borne in mind that the metric used to evaluate a state initiative relates to its potential for discrimination against foreign commercial interests. That is, a GTA investigation examines whether there is any change in the relative treatment between domestic and foreign commercial interests or between foreign commercial interests. Reported investigations take no position on whether a state initiative is WTO-legal, "crisis-related," "appropriate," "effective," or "reasonable," other metrics that some may prefer (and care to define.) It is possible that a state initiative is discriminatory and yet motivated by a benign non-protectionist goal. The GTA takes no position on the motives of a government. However, when a government states a benign rationale for an initiative that claim is recorded in the description of the initiative found on the GTA website.<sup>7</sup>

GTA investigations also report what is known publicly about the process of deliberation pursued by a government as it takes decisions with respect to a specific state initiative. This helps users assess whether a government consulted scientific evidence when making its determinations, whether it offered a rationale for the policy instruments chosen, and whether the impact of different instruments on foreign commercial interests was taken into account. In this manner users can judge whether a government used available scientific evidence to choose policy instruments that minimized the harm done to trading partners and were transparent in doing so.

With respect to the potential effects of a state initiative, the GTA takes a cautious, multi-faceted approach.<sup>8</sup> In a perfect world it would have been desirable

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<sup>6</sup> Each evaluation of a state measure must be approved by the GTA's Evaluation Group, comprising all of the senior analysts associated with the initiative.

<sup>7</sup> Sometimes a member of the trade policy community asserts that a given measure is legitimate or different or justified and should not be included among a list of discriminatory state measures. The GTA team takes no position on the validity of these assertions. Having said that, the "advanced search" page of the GTA website has been deliberately designed so that a user can extract information from the database excluding a given type of state measure. Moreover, most of the tables that the "statistics" page of the GTA website generates reports the total number of measures meeting whatever criteria is sought and the total number of measures other than trade remedies. The latter distinction is made because some assert that trade remedies (anti-dumping, countervailing duties, and safeguards measures) are somehow legitimate or different. As will become clear, removing trade remedies from the summary statistics for discriminatory measures imposed in the year November 2008-September 2009 does not make much difference at all, precisely because there were so few of the former. It will also become apparent that for the 6-12 months from September 2009, if the already announced trade remedy investigated are completed then the imposition of discriminatory trade remedy measures will become much more prevalent.

<sup>8</sup> In the GTA database a measure undertaken by the European Commission on behalf of the 27 member states is attributed to each one of the latter. When other jurisdictions take measures

to conduct a full-blown economic analysis of the effects of each state initiative. Leaving aside the matter of available data and resources, the time taken to conduct economic analyses is such that a comprehensive set of results on the effects of contemporary protectionism is unlikely to be available in time to inform policymaking during the global economic downturn and any subsequent recovery.<sup>9</sup> Recognizing this, the GTA provides information on a number of dimensions of the likely impact of a state initiative. Each state initiative is examined carefully to identify which tariff lines, trading partners, and economic sectors would be affected by its implementation. Available data on trade and investment flows, on foreign affiliates of multinational corporations, and on stocks of migrants are used to identify those trading partners that currently have a commercial interest in the sectors or tariff lines likely to be affected by a given state initiative.<sup>10</sup> The identities of those trading partners are recorded in the GTA

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against the European Union (EU) the identities of the affected member states are sought and the latter are listed as the affected trading partners in the GTA database rather than the European Communities (as the EU is referred to still in trade circles). In the rare cases where such identities cannot be established, the European Communities is listed as the affected trading partner. It being the case that individual member states may take their own crisis-related measures that affect foreign commercial interests (such as buy national public procurement policies), a deliberate choice was made to list each member state in the GTA database as both a potential implementing jurisdiction and an affected trading partner. At the request of several users, the summary statistics and advanced search pages of the GTA website have been configured to allow for searches involving the 27 members of the EU member states.

<sup>9</sup> This is not an argument against economic evaluations *per se*. It is an argument, though, to counter the tendency of some analysts who downplay the impact of contemporary protectionism just because many economic studies of potentially discriminatory state initiatives have not been conducted. There is plenty of evidence, short of detailed empirical studies, that can be carefully collected by trade policy analysts which can usefully inform policymakers during a systemic crisis. Researchers should not fall into the trap of making the perfect the enemy of the very good.

<sup>10</sup> Some have argued that the GTA team should go further and report the amount of commerce affected or potentially affected by each state measure. Adding up across the different measures, so the argument does, might provide another summary indicator of the reach of contemporary protectionism. There are a number of reasons (a few of which are presented below) why this apparently appealing idea is either likely to be implemented and interpreted in a misleading manner or very hard to implement at all. One concern is that the measures do not just affect imports and exports. So how would one add the trade impact to the impact on foreign investors and owners of intellectual property to the impact on migrants, bearing in mind that many of the latter variables are not measured in the same flow terms as trade? Once the foolishness of adding apples to oranges becomes apparent, there is a risk that only the totals for the apples or the oranges are reported, so understating the amount of international commerce affected by contemporary protectionism. Another concern, even in trade in goods, is how to value the amount of global commerce that might be affected by export-promoting policy instruments. Surely the correct number is not the total value of exports from the jurisdiction implementing the policy instrument in question of the goods that might benefit from that instrument? If not, which foreign trading partners are taken to be competitors and in which markets? Many--and in some cases no doubt arbitrary--choices would have to be made here. Worse, many of the export-promoting policy

database. Notice that those trading partners potentially affected by a measure are not identified. This fact, plus the use of *de minimus* thresholds for trade, investment, and migration levels, further reduce the number of recorded trading partners affected.

How representative is the GTA database of contemporary crisis-era protectionism? While at present no definite answer can be given to this question, readers may find the following observations useful in making their assessment of this important matter. First, to the extent that any state initiatives are not discovered by the GTA team then the database will under-report the number of discriminatory state measures and tariff lines, sectors, and trading partners affected. Likewise, a state initiative may exist, be investigated, and its contents not verified, in which case it will not be recorded in the GTA database. If anything these considerations imply that the GTA database will understate the scale of contemporary protectionism, a point worth bearing in mind when interpreting the findings in section 3. Second, any variation across the GTA team in the vigor with which they identify and investigate state initiatives may affect the composition of the database. Third, nations differ in the extent to which they make public (through statements, website postings, etc) state initiatives. Likewise, WTO members may vary in their propensity and speed to meet their notification obligations to that organization. The GTA team has begun an analysis of the representativeness of its database.

The purpose of this section has been to describe the manner by which the GTA team has assembled an extensive evidential base on crisis-era protectionism. Inevitably such an endeavor involves making numerous design choices, the most important of which have been described here.<sup>11</sup> The entries in that database have been carefully categorized so as to facilitate comparison and assessment of the prevalence and consequences of different forms of crisis-era protectionism.

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instruments reported in the GTA database cover lots of sectors of the implementing jurisdiction, further complicating these calculations. Finally, just because the total value of imports potentially affected by an anti-dumping investigation into one product line from one trading partner seems easy to identify does not imply that calculating the amount of trade affected by the wide set of GTA measures is as simple. The last observation is particularly pertinent given the small proportion of trade remedy measures implemented during the period November 2008-September 2009. Put another way, a serious attempt to calculate the total amount of commerce affected in the past year by contemporary discriminatory measures is going to require some difficult, and perhaps hard to defend, design choices.

<sup>11</sup> Not every user may concur with the design choices of the GTA team or, for other reasons, may want to focus on a subset of the GTA database. The advanced search function of the GTA database has been deliberately designed to accommodate many such preferences, allowing certain types of policy instruments, sectors, and jurisdictions to be excluded from any of the reports generated.



### **3. The emerging contours of crisis-era protectionism.**

With 428 state initiatives investigated it should be possible to discern some of the principal features of crisis-era protectionism. Having said that, the picture that emerges may be modified over time as more state interventions are investigated by the GTA team and so what follows is best thought of as a summary of the state initiatives announced between November 2008 and September 2009. During this period the avoidance of risk in financial markets resulted in far less credit being made available to other sectors of the economy, dire expectations of future economic performance resulted in reduced investment and consumer outlays, and there was a sharp reduction in world trade in the first half of 2009.

Of the 428 investigated initiatives, 280 have been implemented implying that there were 148 measures in the pipeline, that is announced but, as of 15 September 2009, not yet implemented. Of the 280 investigated state measures, 40 were color-coded green, that is, the measures involved liberalization on a Most Favored Nation basis, improved transparency of a national trade regime, or no change in the discrimination against foreign commercial interests. It would be incorrect to assert, therefore, that the every reaction to the global economic downturn has been to close markets and engage in beggar-thy-neighbor behavior. Tariff reductions (in particular for parts, components, and raw materials) and reforms to foreign direct investment regimes were the most prevalent forms of liberalization observed.<sup>12</sup> A number of reports of the national budgets in Sub-Saharan Africa show the steps being taken to integrate the economies in question further into world markets.

The ratio of the total number of discriminatory measures (color-coded red) to the total number of measures that might benefit trading partners (color-coded green) is approximately five to one. Furthermore, when one adds to the 192 of the former the 48 implemented measures that are likely to harm foreign commercial interests (color-coded amber), the overwhelming tendency during this crisis to reduce cross-border commercial opportunities becomes apparent (see Table 1).

The data summarized in Table 1 also implies that of the measures implemented to date, trade remedies represent a relatively small share (14 percent). Moreover, the G-20 countries together account for two-thirds of discriminatory measures implemented. Very few tariff lines, economic sectors, and trading partners have not been affected by some form of discriminatory policy instrument since November 2008, indicating the worldwide reach of current protectionist dynamics.

In addition to the announced and implemented discriminatory state initiatives, 134 of the 148 pending measures are likely to harm foreign

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<sup>12</sup> It being understood that reductions in tariffs on raw materials and intermediate goods could, in fact, increase the effective rate of protection enjoyed by final goods producers.

commercial interests when implemented. Given that approximately 70 harmful measures have been implemented per quarter during 2009, the potentially harmful measures in the pipeline represent up to another half a year of protectionism. These measures will start to influence global commerce even if governments were able to resist announcing any more initiatives that discriminated against foreign commercial interests (see Figure 1).

In terms of policy instruments used to discriminate against foreign commercial interests, Table 2 demonstrates that a variety of methods have been employed since November 2008. Focusing on a few policy instruments (such as anti-dumping investigations or tariff rises), therefore, is likely to provide an inaccurate impression of the prevalence of, and probably the harm done by, contemporary protectionism. A cumulative picture ought to be developed.

Of those implemented to date, bailouts, state aids, and other forms of financial assistance were the most popular discriminatory policy instrument<sup>13</sup>, followed by tariff measures and then trade remedies. Two of the top three most used policy instruments often involve the use of discretion on the part of implementing agencies. The associated lack of transparency and predictability that typically arises from the exercise of such discretion has led some observers<sup>14</sup> to worry about the prevalence of "murky protectionism" during the recent crisis, and arguably the evidence in Table 2 accords with this concern.

Seven different policy instruments are expected to have harmed over 100 trading partners, two of them by promoting national exports rather than curtailing imports. Moreover, there are far from perfect correlations between the number of times a policy instrument has been used in a discriminatory manner, and the number of trading partners, tariff lines, and economic sectors affected. This reflects the fact that some of less frequently used policy instruments have distorted commerce in substantial numbers of products and sectors (see the lower part of Table 2). Once again this points to the perils of focusing on a limited subset of policy instruments--perhaps because they are easier to measure or easier to think through than others--when assessing the scale of contemporary protectionism.

There appears to be a difference between the beggar-thy-neighbor policy instruments that governments have resorted to when the credit markets had dried up and the measures in the pipeline. Contrasting Figures 2 and 3 it becomes evident that trade remedies will almost surely play a more prominent role in the coming year than in the previous one. Perhaps the "scramble for cash" (that arises because many corporate outlays are made before revenues are received) is being

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<sup>13</sup> Of the 62 state initiatives offering some form of public financial assistance, 34 do not target the financial sector. There may also be state initiatives whose beneficiaries are in the financial and non-financial sectors.

<sup>14</sup> See, for example, Baldwin and Evenett (2009) and several of the contributions therein.

replaced by the more traditional "scramble for rents". As argued later, traditional barriers may be more effective at delivering the latter rather than the former. The more general point is that there is likely to be a change in the overall composition of cross-border commercial discrimination which cautions against accepting any explanation that cannot account for changes in this composition over time.

In terms of the sectoral impact of protectionism, Table 3 is revealing. Apart from the financial sector, which has received plenty of state aid during the crisis, six of the top 10 affected sectors are traditionally associated with high levels of protection from foreign competition. The same is true for six of the next 10 sectors to be most affected by discriminatory measures. As Aggarwal and Evenett (2009) have argued, this finding casts doubt on overall relevance of defenses of the use of discriminatory state measures on the grounds of nurturing "growth poles" or the "green economy." Most of the beneficiaries of crisis-era protectionism are the very smokestack manufacturing, textiles and apparel, and agricultural sectors that for decades have received above average levels of protection.

With respect to the targets of discriminatory state measures, China stands out (see Table 4). Just under 100 foreign state initiatives target Chinese commercial interests, with another 77 in the pipeline. Fifty-six countries have taken measures that have harmed China's trading interests. Only the United States comes close in terms of being targeted by so many trading partners (49 in this case). Still, several economies in the European Union and Japan have seen their commercial interests harmed over 70 times since November 2008.

Four indicators of the harm done by a nation to its trading partners' commercial interests are recorded in the GTA database (see Table 5). From these indicators four rankings can be generated of the countries that have implemented the most almost-discriminatory measures and affected the most tariff lines, economic sectors, and trading partners with such discriminatory measures. Depending on the matter at hand, readers may wish to place different weights on each of these four rankings. Comparing across them, it is noteworthy that Indonesia is always in the top 5 worst offenders. China and Russia are always in the top 10 of each ranking; Germany and India are in the top 10 of three of the four rankings. Of the 18 nations mentioned in these rankings of worst offenders, 12 took the G-20's no protectionism pledge.

To summarize, the purpose of this section has been to describe the main findings of the GTA's database on contemporary crisis-era protectionism. In short, this establishes the facts that any proposed explanation ought to account for. The following section examines whether our understanding of protectionism needs to evolve in the light of these facts.

#### **4. Four hypotheses concerning the resort to beggar-thy-neighbor policy instruments.**

The facts reported above are now employed to assess the possible underlying casual processes responsible for the resort by governments to discriminatory policy instruments since November 2008. To what extent, if at all, does our understanding of protectionism need to be modified in the light of the state intervention taken in response to the recent sharp global economic downturn? Are the factors that determine the resort to protectionism in a systemic economic crisis different from those at work during a "typical" business downturn? To date, it appears that governments have not resorted to the sort of across-the-board tariff increases witnessed during the 1930s, why is this so? Analysts will no doubt be reflecting on these questions, and others, for years to come. To focus the following discussion, four hypotheses concerning the resort to protectionism are evaluated in the light of the evidence contained in the GTA database.

The first hypothesis, ably advanced by Eichengreen and Irwin (2009), contends that resort to widespread protectionism in the 1930s was greater in those nations where exchange rate, fiscal, and monetary policies were more constrained.<sup>15</sup> On this view, protectionism was used in the 1930s as a macroeconomic tool to stimulate aggregate demand by switching expenditure from imports to the produce of domestic firms. Macroeconomic management, then, is privileged over special interest explanations for the outbreak of 1930s protectionism. Since the policy constraints of the 1930s rarely find counterparts in jurisdictions today, so the argument goes, there has been little need to resort to across-the-board protectionism.

On the face of it, some contemporary experience bears out this hypothesis.<sup>16</sup> With the possible exception of Ukraine, no other country has resorted during the current crisis to across-the-board tariff increases on a scale witnessed in the 1930s; the Smoot-Hawley tariff increases being an example of the latter and involving an average tariff increase of six percent.

Can this hypothesis also account for the cross-country variation in the propensity of governments to resort to discriminatory policy instruments? The first hypothesis implies that, the greater is the capacity of governments to implement aggressive monetary and fiscal policies<sup>17</sup> then resort to expenditure-

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<sup>15</sup> Recall that in the early 1930s the prevailing macroeconomic orthodoxy called for membership of the Gold Standard and for balanced government budgets.

<sup>16</sup> See also the footnote at the end of the next paragraph.

<sup>17</sup> Unless one is prepared to argue that the decision to stop the gradual appreciation of the Chinese renminbi is an example of crisis-driven exchange rate manipulation, it would be difficult to argue that flexibility in exchange rates is the reason why governments have not resorted to widespread

switching discriminatory policy instruments ought be less. Bearing in mind the different types of protectionist measures imposed since November 2008, assume that greater reliance overall on expenditure-switching discriminatory policies is associated with more discriminatory measures being imposed, with more tariff lines being affected by such measures, with more economic sectors so affected, and with a greater number of trading partners' commercial interests being harmed. With this assumption, if this hypothesis is correct then those countries that could not pursue aggressive monetary and fiscal policies during the recent crisis should be better represented in the rankings reported in Table 5 of countries inflicting the most harm through discriminatory policy instruments. Consulting this table, however, reveals many highly ranked countries that have clearly been able to relax their monetary and fiscal policies, namely, Germany, Italy, Spain, the UK, China, Japan, Russia, the USA, and France. Something else must be going on, beyond the noble goal of macroeconomic management.<sup>18</sup>

The second hypothesis concerning contemporary protectionism hinges on changes in the organization of firms that have taken place over the past 20 or so years with the rise of both international outsourcing and supply chain management. Baldwin and Evenett (2009), amongst others, have argued that the cost levels of contemporary manufacturers are significantly influenced by the costs of parts and components, many of which happen to be sourced from abroad. Firms supplying parts and components have a strong interest in keeping costs down and outsourcing has become a pervasive corporate strategy, so opposition to any proposals to raise tariffs on intermediate goods and raw materials has grown. Cross-border corporate reorganization, itself a consequence of pre-crisis trade reforms, accounts on this view for the reluctance of "Factory Asia" and the industrialized countries to raise tariffs during this crisis.

To what extent does this explanation provide a satisfactory explanation for contemporary protectionist dynamics? In favor of the second hypothesis is the continuing reluctance of governments to raise tariffs on intermediate goods. Moreover, as noted earlier, the GTA database contains a number of instances when governments have lowered tariffs and charges on intermediate goods and

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protectionism since November 2008. (This statement should not be read as meaning that the nominal exchange rates of every major trading nation have been stable throughout the past year. The US dollar and British pound have fluctuated considerably and while concerns were expressed for a short while that the British were devaluing their currency such fears did not persist.) Monetary and fiscal policy must, therefore, carry the argument in this current crisis.

<sup>18</sup> Defenders of the first hypothesis may well take the inclusion of Indonesia, Argentina, Ukraine, Ecuador, Belarus and possibly Mexico as evidence in favor of their proposition if it were the case that these countries' governments were either less able to borrow on open markets than most and where aggressive monetary policies would be more likely to lead to nominal exchange rate collapses than most. The arguments made here and in the main text are suggestive of a more formal econometric evaluation of the first hypothesis.

raw materials. However, this argument is silent on the largest form of discriminatory measures implemented, namely, financial assistance measures and a review of the stated rationales for advancing such assistance does not provide much support for this hypothesis (recall Table 2).<sup>19</sup> Worse, this explanation is hard to square with the 12 discriminatory measures taken by governments since November 2008 to increase the use of locally-sourced parts, components, and raw materials (Table 2 again). In fact, the combination of the additional spending as part of stimulus packages with Buy National provisions and tighter rules on local content, as seen in the United States amongst others, provides stronger incentives to unravel international supply chains and to repatriate production. Again, something is missing; at best, the second hypothesis is incomplete. Instead of taking corporate reorganization as a determinant of contemporary protectionism, future analyses might consider the extent to which influencing corporate reorganization has itself become a motive underlying policy choices during the global economic downturn.

A third hypothesis is that the choice of protectionist policy instruments have been influenced by entrenched corporate interests using the circumstances of the crisis to target rival foreign firms from export powerhouses and to shift the burden of capacity reduction on to others. Central to this argument is that the measures sought by corporate interests are selective; targeting imports from selected foreign sources or acquiring enough financial assistance to resist adjustment while others (including domestic rivals) succumb. On this view, discrimination need not be across-the-board or widespread, but could become or appear so if the aggregate effect of numerous selective interventions was sizeable. Moreover, such corporate interests might be opposed to governments resorting to across-the-board discrimination with transparent policy instruments (such as tariffs) for fear of inducing retaliation from abroad. Better, then, to seek selective and murky forms of discrimination.

On the face of it, this hypothesis might have a lot going for it. The targeting of China, the United States, and Germany (home to some of the world's most successful exporting firms) accords with the third hypothesis (recall Table 4). Selective financial packages to manufacturing firms, often discriminating between firms located in a jurisdiction as well as between jurisdictions, have played a prominent role after November 2008 (recall Figure 2).

The problem with the third hypothesis is timing. The principal measures to selectively target specific trading partners--anti-dumping duties, countervailing duties, and China-specific safeguards--represent only a small fraction of the discriminatory measures implemented during the period November 2008 to

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<sup>19</sup> However, there is one Japanese state initiative listed in the GTA database that was deliberately designed to offer funds to Malaysian firms that are integrated into the supply chains of Japanese multinationals.

September 2009 (Figure 2 again). To the extent that these selective measures require a demonstration of injury to a domestic industry that is attributed to imports, it is difficult to make such a case when imports are falling, as they were for many products in many jurisdictions during the first half of 2009. In contrast, with the stabilization (and in some cases increases) in trade in the third quarter of 2009, such demonstrations may become easier to make. In fact, it is interesting to note that over half of the pending state initiatives likely to harm foreign commercial interests in the GTA database are trade remedies, many of which allow for the selective targeting of foreign trading partners (recall Figure 3). The third hypothesis, then, may perform better in the next twelve months than in the past year.

The fourth hypothesis puts at the center stage certain consequences of the financial crisis, arguing that they influenced the choice of discriminatory policy instruments. When the financial markets froze in late 2008 the amount of credit, including working capital and trade finance needed by firms to cover their expenses before revenues were received, advanced to the private sector fell considerably. Without such credit and other sources of funds, the non-financial private sector would begin laying off employees, delaying (and possibly defaulting on) payments to other firms, and cutting back on investment outlays. Seeking to limit the harm to the "real economy" and bearing in mind that firms' needs varied within sectors as well across sectors, governments undertook direct interventions that selectively delivered "cash" to the non-financial private sector. For those governments with the means to do so, or those nations with banking systems where credit could be directed without inducing a widespread withdrawal of deposits, direct payments, loans, and credit guarantees were the fastest means to deliver cash to those firms in need of it. Selective financial interventions become prominent precisely because "All you need is cash" during the depths of the recent financial crisis (as the cover of *The Economist* magazine put in its 1 November 2008 edition) and other forms of state intervention would have been slower and less targeted in delivering funds to tide firms over.

At best this hypothesis accounts for the widespread resort to financial assistance packages in the industrialized countries and in China (were the banking system meets the conditions described above). As means of delivering cash quickly the alternatives to financial assistance are found wanting. Trade remedies take time to investigate and often require a period of rising imports to justify the imposition of measures. Tariff increases shift sales to domestic firms, but the same financial crisis may discourage domestic and foreign customers from purchasing, so the overall impact on the revenues of domestic firms is uncertain. Worse, the amount of extra sales and profits that tariffs can deliver is bounded (at that levels associated with the elimination of tariffs with a prohibitive tariff.) Stimulus packages take time to legislate and time to implement, especially if state

funds are transferred between levels of government. In the light of these practical considerations, financial assistance is the preferred means to attain a specific, crisis-related end, namely, cash. Other than the European Union's state aid rules, which were soon overwhelmed and scaled back in late 2008, the weaknesses of extant multilateral rules on subsidies reinforced the attractiveness of this option.<sup>20</sup>

It may be fruitful to combine the third and fourth hypotheses and to posit that when national output began to fall sharply then the objectives of firms seeking state intervention changed from cash to rents (from selectively targeting rivals).<sup>21</sup> On this view the purpose of the financial assistance was initially to provide needed cash and subsequently to encourage rival firms to undertake more of the capacity reduction that became necessary in many sectors as the global economy contracted. This was coupled with the selective targeting of imports to reallocate market shares in home markets. For presentational purposes these interventions could be wrapped up in packages--sometimes referred to as industrial policy--but in many cases they amount to the resort to selective, discriminatory intervention in support of influential corporate groups and associated trade unions. Should the pending state initiatives identified by GTA be implemented, then such a combined hypothesis might account for the implied change in the composition of discriminatory measures that is likely to be observed over the next 12 months or so.

The purpose of this section has been to examine how our understanding of protectionist dynamics might have to evolve in the light of state interventions taken during the recent global economic crisis. To sharpen the arguments the discussion here was organized around four hypotheses, that are not necessarily mutually exclusive. The fact that governments have used a range of policy instruments since November 2008 was useful in highlighting the strengths and weaknesses of several hypotheses. Moreover, the specific and acute circumstances of the recent global financial crisis were an important reminder that the problems that governments seek to address during systemic crises may be different from typical business cycle downturns, with direct implications for the likelihood of choosing one discriminatory policy instrument over another.

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<sup>20</sup> Nothing in this paragraph should be taken to imply that selective financial assistance does not distort the allocation of resources or is the least damaging policy option from the perspective of resource allocation. The arguments concerning the attractiveness of selective financial assistance packages to policymakers were made on other grounds.

<sup>21</sup> Notice the formulation is not "cash plus customers" as the maximum amount of customer switching would occur if MFN trade restrictions were applied. To the extent that an industry's firms encourage a government to resort to traditional safeguards or other MFN trade restrictions then the "cash plus customers" formulation might have some explanatory power.



## **5. Assessing international trade rules and accords in the light of contemporary protectionism.**

During the recent sharp economic downturn to what extent, if at all, have national policy choices been influenced by binding multilateral trade rules and other international accords on commercial policy? To what extent has contemporary protectionism been influenced by the binding rules of the World Trade Organization (WTO) and the more informal no-protectionism pledge of the G-20 countries? The answers to these questions may alter our understand the "bite" of existing international accords and influence our assessment of the merits and viability of potential future trade-related initiatives. Drawing upon the evidence presented earlier, the purpose of this section is to offer some observations on these matters.

With respect to the bindings on tariffs on non-agricultural goods made by members of the WTO, a number of remarks are in order. The first is that, in the past year, to the best of our knowledge no government has raised its tariffs above the bindings that it had previously committed to. On the face of it this is good news, until one realizes the significant latitude the great majority of WTO members have to raise tariffs without exceeding their bindings. In recent times many comparisons have been made to the 1930s, presumably to provide some perspective. In this spirit it is worth noting that the Smoot Hawley tariff increases of 1930 raised US tariffs by on average six percentage points. How many WTO members could implement a Smoot Hawley-sized tariff increase now and not exceed their tariff bindings? According to the *World Tariff Profiles 2008*, available on the WTO website, of the 124 trading jurisdictions<sup>22</sup> for which data is available, only 21 have average bound tariff rates that are less than six percent higher than their average applied tariff rates. Put another way, there is so much latitude to raise tariffs in current tariff bindings that 103 jurisdictions could copy Messrs. Smoot and Hawley and not break their WTO obligations. If the Smoot Hawley tariff is the standard, then for these 103 jurisdictions it is very doubtful that current tariff bindings are much of a constraint on national policymaking.

Some might be tempted to salvage part of the argument concerning the bite of tariff bindings by contending that the policy choices of the other 18 jurisdictions, which include six industrialized country jurisdictions (including the European Union) and many of the recently acceding countries (including China), have been influenced by these multilateral trade commitments. This claim is not very persuasive for the industrialized countries in question and China because, as argued earlier, another policy instrument (financial assistance) had clear advantages over tariffs in terms of meeting the specific challenges facing non-financial companies during the past year. There was no risk of these countries

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<sup>22</sup> In this publication the members of the European Union are treated as a single trading entity.

breaking their tariff bindings so long as the challenge of providing cash to firms was better accomplished by another available policy instrument. At most, then, the tariff bindings can be said to have constrained the behavior of some of the recently acceded members. Even there, as the case of Ukraine demonstrates, these countries can resort to other WTO-legal policy instruments that enable them to raise tariffs substantially. In sum, the patterns of contemporary protectionism and available legal loopholes cast doubt on any claims that the WTO tariff bindings have constrained policy choices during the recent global economic downturn.

The incomplete nature of the corpus of many WTO agreements is another feature that must be taken into account when assessing the bite of existing multilateral trade rules. The fact that the WTO's rules on subsidies are limited in reach and that the plurilateral disciplines on government procurement extend only partially to sub-national governments suggest that it would be more accurate to contend that, since November 2008, governments have chosen policy instruments that evade WTO rules rather test them. Moreover, without an expansion of the WTO rules into these areas, it is difficult to see why governments would not resort to bailouts and discriminatory fiscal stimulus packages (including buy national policies) again in a comparable future financial crisis. Overall, expectations of the impact of current multilateral trade rules on government choices made during systemic economic crises should be tempered accordingly.

One reaction to the last paragraph's conclusion is to argue that the world economy would benefit from more far-reaching, binding multilateral trade rules. Despite being sympathetic to this position for a long time, one prominent episode from the past year casts doubt on political viability of strengthening WTO rules on those policy instruments where discrimination has been rife. The emasculation, during the straightened days of late 2008, of the stringent state aids regime of the European Union requires careful examination. The challenge to those seeking further binding trade rules to prevent future governments from repeating their recent choices of discriminatory policy instruments is to show that their proposals will prevail when confronted with the extraordinary pressure that governmental leaders *simultaneously* face to intervene selectively during systemic economic crises. Ostracizing individual rule-breakers is one thing, confronting group violations risks repudiation of the binding rule in question.

More generally in an acute financial crisis, when the fate of banks and other firms may be decided over weekends between the close of the financial markets in New York and their subsequent opening in Tokyo, is it realistic to expect that associated rushed decision-making will respect the WTO principles of transparency and non-discrimination? Furthermore, if any binding rules were violated during a systemic economic crisis, and the consequences of such violations were economically significant and potentially hard to reverse (such as if some firms exit a sector as a result), what value would policymakers attach to

dispute settlement findings rendered 18 months or so later? In short, there is probably a significant mismatch between the current negotiating, deliberative, and dispute settlement practices of the WTO and the imperatives of government decision-making during a crisis. Positive answers to the questions posed above are needed before expansions in the scope of the WTO's binding rules could realistically be expected to influence government choices during a systemic economic crisis.

Another reaction is to argue that the solution is not more binding rules, but rather more informal understandings between governments (or at least between the governments of the largest trading nations) to eschew protectionism in times of economic crisis or to limit resort to discriminatory policy instruments. Supporters of this view might point to the non-binding G-20 pledge to avoid protectionism for the duration of the current crisis<sup>23</sup>; a commitment reiterated often since it was first articulated at the G-20 summit in Washington D.C. in November 2008. Some assert that resort to protectionism by G-20 governments would have been higher in the absence of this no-protectionism pledge. Had the GTA database contained observations before November 2008 it might have been possible to examine whether there were any breaks in state decision-making after the pledge was taken; for example, by considering whether the propensity to implement discriminatory policy instruments became less sensitive to economic conditions after the pledge.

The absence of a compelling counterfactual is, however, not the end of the matter. Other features of contemporary protectionism reported in the GTA database cast doubt on whether the pledge by G-20 heads of government could ever work. The starting point is to recall the variety of discriminatory policy instruments employed since November 2008. Many of the key decisions concerning these policy instruments were not taken state agencies controlled by the head of government. In fact, some of those agencies are formally independent of central government and, absent a change in legislation, would be under no obligation to comply with the G-20 no-protectionism pledge. For example, in many nations the agency responsible for deciding whether to impose trade remedies is independent of government and, therefore, what reason is there to believe such agencies' propensities to discriminate against foreign commercial interests would change after November 2008? Similar considerations apply to the discrimination against foreign commercial interests implemented by sub-national governments (through, for example, buy local policies and financial assistance to local firms) and by independent central banks and financial regulators (through discriminatory bailouts of financial institutions).

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<sup>23</sup> G-20 members have never made it clear what was meant by this pledge. In fact, it may be the case that the pledge was articulated without any common meaning being agreed. Analysts may therefore make the mistake of inferring what they think G-20 members meant by this pledge!

In other cases the head of government must decide which policy instruments to implement in collaboration with other independent decision-makers. Decisions made with national legislatures in presidential systems of government are cases in point; here head of governments may find themselves reluctantly accepting the inclusion of discriminatory provisions in legislation, such as fiscal stimulus packages. In the case of the European Union, the majority of member states are not even part of the G-20 and may not feel bound by the no-protectionism pledge. Once again, commitments by heads of government to eschew protectionism lack credibility when the party making the pledge is not in control of the relevant decision-making processes. The critique here is not that the G-20 pledge did not work rather to question whether many heads of governments had the power to ever make it work.

The murkiness of much contemporary protectionism exposes another weakness in the G-20 pledge, namely, verification. The fact that so little of contemporary protectionism is transparent (such as tariff increases) makes it more difficult to ascertain whether a G-20 member has violated the pledge. With limited verification one is entitled to ask how the anyone, including a party to the pledge, could know if the pledge has worked? Like its binding counterpart, the degree of influence over national decision-making of the G-20 pledge is limited by its incompleteness.

To summarize, on the basis of the available evidence on crisis-era protectionism, there are reasons for doubting that nation states were meaningfully restrained by international trade rules and accords over the past year. Consequently our understanding of contemporary protectionism should give greater weight to domestic factors and imperatives.

## **6. Concluding remarks.**

Profound economic and political shocks in an era of considerable international interdependence ought to provide an opportunity to evaluate and, where necessary, revise our understanding of protectionism. Using a substantial database of state initiatives announced since the first crisis-related G-20 summit in November 2008, this paper has sought to add to our understanding of the characteristics of contemporary protectionism and to start assessing its likely determinants. The world economy has yet to be restored to full health, and in the coming months and years fresh evidence may call for the propositions advanced here to be revisited.

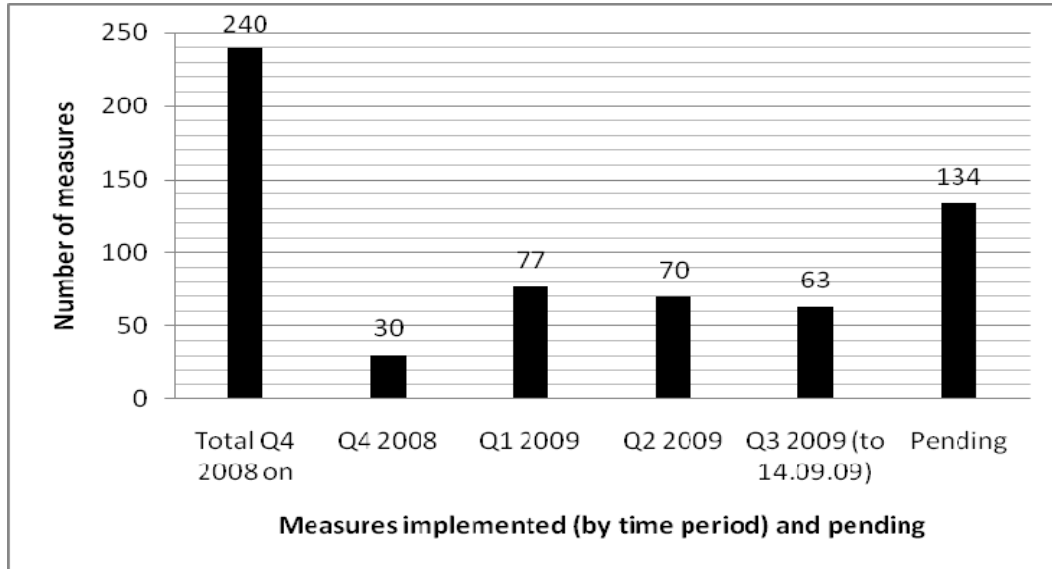
The multi-faceted nature of contemporary protectionism, the specific needs of companies that arise during a systemic financial crisis (as opposed to during a traditional business cycle downturn), and the relative importance of domestic imperatives as compared to international rules and other accords are central to an

understanding contemporary protectionist dynamics and the pervasive abandonment of the level playing field as a guiding principle for state intervention.

**Table 1. Measures implemented since first crisis-related G20 summit in November 2008, totals for all jurisdictions and for the G20 members.**

| Statistic   | All jurisdictions |   | G20 nations |   |
|---|-------------------|---|-------------|---|
|   | Total             | Total except unfair trade and safeguards investigations | Total       | Total except unfair trade and safeguards investigations |
| Total number of measures in GTA database  | 280               | 231   | 172         | 133   |
| Total number of measures coded green  | 40                | 36  | 27          | 24  |
| Total number of measures coded amber  | 48                | 30  | 24          | 11  |
| Total number of measures coded red  | 192               | 165   | 121         | 98  |
| Total number (%) of 4-digit tariff lines affected by almost certainly discriminatory measures | 1157 (95%)        | 1141 (94%)  | 926 (76%)   | 921 (76%)   |
| Total number (%) of 2-digit sectors affected by almost certainly discriminatory measures      | 63 (80%)          | 63 (80%)  | 58 (73%)    | 58 (73%)  |
| Total number of trading partners affected by almost certainly discriminatory measures         | 217               | 203   | 206         | 193   |

**Figure 1. If the measures in the pipeline are implemented, the number of harmful measures will rise by more than half.**



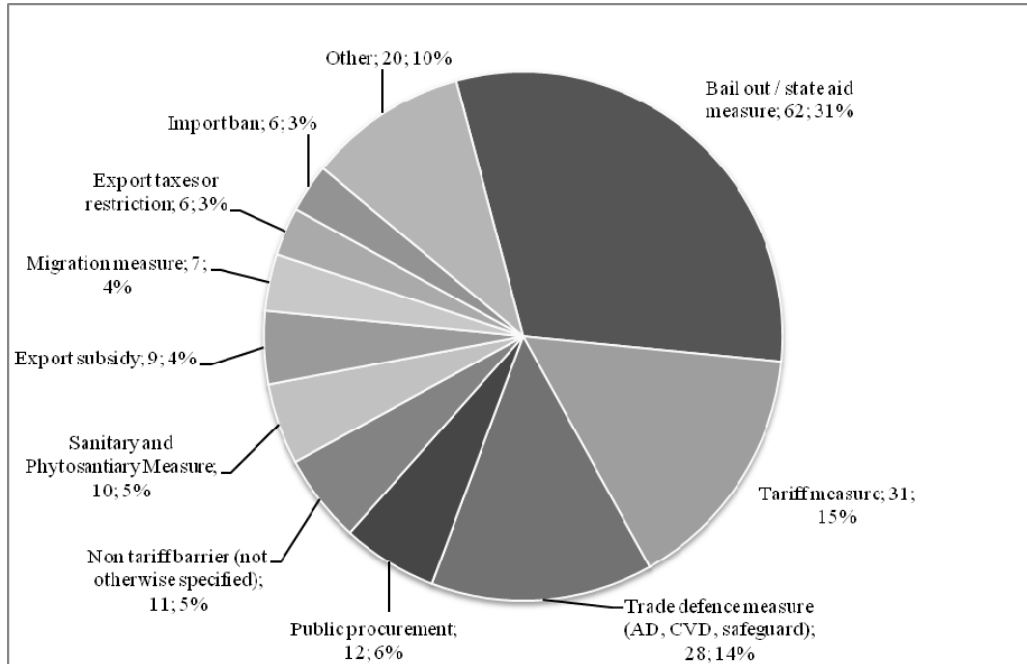
In Figure 1 a harmful measure is taken to be one which has been implemented since November 2008 and is almost certainly discriminatory (coded red) or likely to be discriminatory (coded amber).

**Table 2. Ten most used state measures to discriminate against foreign commercial interests since the first G20 crisis meeting.**

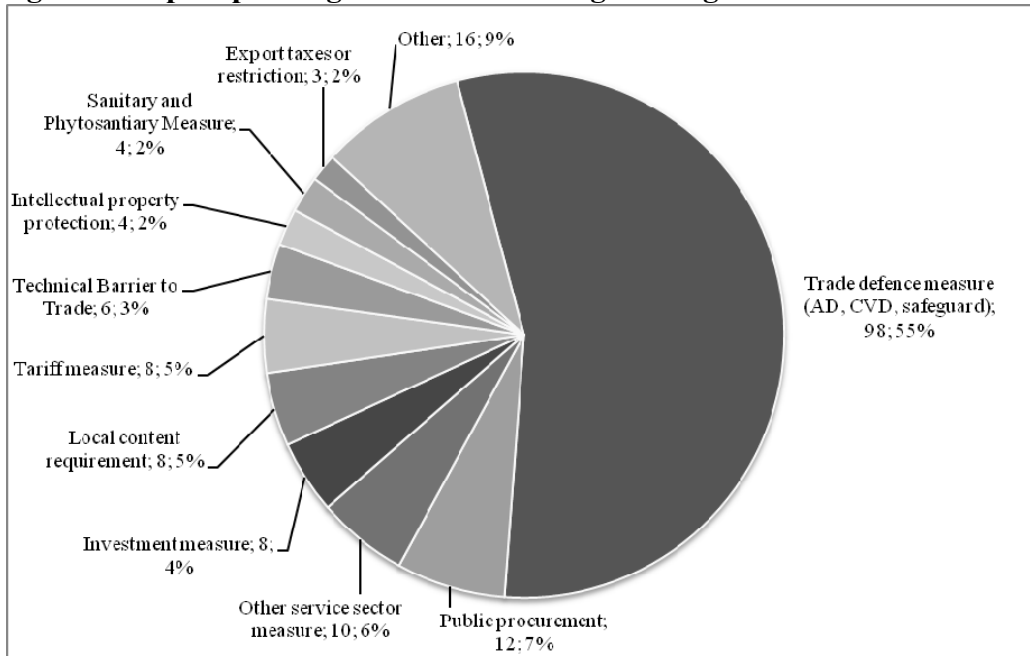
*Ranked by number of discriminatory measures imposed.*

| Rank and measure                                | Number of measures implemented by type. | Number of discriminatory measures (classified red) | Number of countries that <u>imposed</u> these discriminatory measures | Number of countries <u>harmed</u> by these discriminatory measures | Percentage of tariff lines (product categories) affected by these discriminatory measures | Percentage of sectors affected by these discriminatory measures |
|---|---|--|---|--|---|---|
| 1. Bail out/state aid measure                   | 66                                      | 62   | 35  | 150  | 12  | 25  |
| 2. Tariff measure                               | 60                                      | 31   | 15  | 113  | 38  | 43  |
| 3. Trade defense measure (AD, CVD, safeguard)   | 50                                      | 28   | 40  | 101  | 24  | 39  |
| 4. Public procurement/ Buy National policy      | 16                                      | 12   | 11  | 133  | 30  | 34  |
| 5. Non tariff barrier (not otherwise specified) | 17                                      | 11   | 7   | 109  | 22  | 36  |
| 6. Sanitary and Phytosanitary measures          | 11                                      | 10   | 8   | 17   | 1   | 8   |
| 7. Export subsidy                               | 11                                      | 9  | 31  | 144  | 17  | 21  |
| 8. Migration measure                            | 10                                      | 7  | 7   | 31   | 0   | 0   |
| 9. Export taxes or restriction                  | 14                                      | 6  | 9   | 146  | 22  | 22  |
| 10. Import ban                                  | 6                                       | 6  | 5   | 34   | 10  | 27  |

**Figure 2. Top 10 implemented measures used to discriminate against foreign commercial interests since the first G20 crisis meeting.**



**Figure 3. Top 10 pending measures that target foreign commercial interests.**





**Table 3: Sectors most affected by discriminatory measures.**

| Rank, CPC code, and sector description                                   | Number of implemen-<br>ted measures<br>affecting<br>specified sector | Number of discrimin-<br>atory<br>measures<br>harming<br>comer-<br>cial interest<br>in this sector | Number of<br>countries<br>responsible<br>for discrimin-<br>atory<br>measures<br>taken in this<br>sector | Number of<br>pending<br>measures<br>affecting<br>specified<br>sector |
|--|--|---|---|--|
| 1. 81 (Financial intermediation services and auxiliary services thereof) | 31   | 29  | 13  | 1  |
| 2. 21 (Meat, fish, fruit, veg. etc)                                      | 40   | 25  | 16  | 5  |
| 3. 44 (Special purpose machinery)  | 52   | 25  | 16  | 11   |
| 4. 01 (Products of agriculture)  | 40   | 22  | 17  | 7  |
| 5. 23 (Grain mill products)  | 39   | 22  | 40  | 7  |
| 6. 41 (Basic metals)   | 65   | 22  | 38  | 27   |
| 7. 27 (Textile articles other than apparel)                              | 36   | 19  | 13  | 7  |
| 8. 34 (Basic chemicals)  | 54   | 19  | 12  | 20   |
| 9. 42 (Fabricated metal products)  | 49   | 19  | 13  | 18   |
| 10. 49 (Transport equipment)   | 50   | 19  | 13  | 16   |
| 11. 38 (Furniture; other transportable goods n.e.c.)                     | 30   | 18  | 13  | 5  |
| 12. 47 (Radio television and communication equipment and apparatus)      | 29   | 18  | 10  | 6  |
| 13. 22 (Dairy products)  | 27   | 17  | 40  | 5  |
| 14. 28 (Knitted or crocheted fabrics; wearing apparel)                   | 28   | 17  | 12  | 4  |
| 15. 43 (General purpose machinery)                                       | 33   | 17  | 11  | 7  |
| 16. 02 (Live animals and animal products)                                | 25   | 16  | 41  | 4  |
| 17. 29 (Leather and leather products; footwear)                          | 24   | 15  | 11  | 2  |
| 18. 36 (Rubber and plastics products)                                    | 28   | 15  | 13  | 7  |
| 19. 46 (Electrical machinery and apparatus)                              | 23   | 14  | 10  | 4  |
| 20. 26 (Yarn and thread; woven and tufted textile fabrics)               | 33   | 12  | 9   | 10   |

**Table 4. Top 10 biggest targets of discriminatory measures**

| Target         | Number of discriminatory measures imposed on target | Number of trading partners imposing discriminatory measures | Number of pending measures which, if implemented, would harm target too |
|----------------|---|---|---|
| 1. China       | 99  | 56  | 77  |
| 2. USA         | 86  | 49  | 19  |
| 3. Germany     | 84  | 30  | 30  |
| 4. France      | 78  | 29  | 24  |
| 5. Japan       | 78  | 46  | 23  |
| 6. Belgium     | 78  | 28  | 21  |
| 7. UK          | 72  | 29  | 20  |
| 8. Netherlands | 71  | 28  | 18  |
| 9. Italy       | 70  | 25  | 23  |
| 10. Sweden     | 70  | 23  | 21  |

**Table 5. Which countries have inflicted the most harm?**

***Note:** There is no single metric to evaluate harm. Different policy measures affect different numbers of products, economic sectors, and trading partners. GTA reports four measures of harm.*

| Rank | Metric, Country in specified rank, Number                              |   |  |   |
|------|--|---|--|---|
|      | Ranked by number of (almost certainly) discriminatory measures imposed | Ranked by the number (percentage) of tariff lines (product categories) affected by (almost certainly) discriminatory measures | Ranked by the percentage of sectors affected by (almost certainly) discriminatory measures | Ranked by the number of trading partners affected by (almost certainly) discriminatory measures |
| 1.   | Russia (20)  | Ukraine 733 (60%)   | Algeria 54 (68%)   | China (163)   |
| 2.   | Germany (15)   | China 329 (27%)   | Ukraine 38 (48%)   | India (141)   |
| 3.   | India and Indonesia (10 each)  | Ecuador 312 (25%)   | Ecuador 30 (37%)   | Indonesia (124)   |
| 4.   |  | Indonesia 311 (25%)   | Indonesia 25 (31%)   | UK (123)  |
| 5.   | Italy, Spain, and UK (9)   | Russia 258 (21%)  | Belarus and China 23 (29%)   | USA (120)   |
| 6.   |  | India 210 (17%)   |  | Russia (117)  |
| 7.   |  | Japan 133 (11%)   | Mexico 22 (28%)  | Germany (116)   |
| 8.   | China (8)  | UK 131 (11%)  | Germany 21 (27%)   | Spain (108)   |
| 9.   | Argentina (7)  | USA 124 (10%)   | Russia and USA 19 (24%)  | France (106)  |
| 10.  | Japan (7)  | Belarus 74 (6%)   |  | Poland (100)  |

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