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New Shades of Protectionism and the Role of Multinationals

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Like all crises in the past, the economic downturn of 2008-2009 caused some frictions in the international trading system. Import tariffs, the traditional instrument for protecting domestic industries, however, have not played the primary role in this, particularly not in industrialised countries. The WTO rules have proved to be an efficient shield against a wholesale descent into protectionism in this respect. However, in other policy areas, such as state aid and WTO contingency measures the results are more mixed. While an all-out subsidy war has not broken out, heavy intervention has taken place in the automotive industry. This was much to the benefit of leading multinationals, who have used their international presence and mobility to extract various kinds of public support from governments. Neither governments nor WTO rules have managed to avoid costly subsidies. Indeed governments have found themselves caught in an international subsidy competition inflicted on them by global car manufacturers. This has allowed the car industry to take itself out of the existing international disciplines on subsidies. While this is not classical protectionism offered to strictly national industries, we may see a new mutation emerging, wherein multinationals more effectively play governments against each other to lobby for local assistance for what are actually global operations.

1. Introduction

"Free trade is God's diplomacy" wrote Richard Cobden in 1857. Economic policy, however, is not guided by divine powers but by pressure from interest groups and policy makers' genuine interest in domestic constituencies. This is particularly true in times of crisis. Economic downturns, in general, are accompanied by a hike in trade barriers. The views on how far the world trading system has slipped towards protectionism since the onset of the current crisis are very divergent, ranging from almost daily breaches of free trade promises¹ (Evenett, 2009) to a more cold-minded assessment that there is no new wave of pro-

tectionism yet (Messerlin, 2009). Factors working against the emergence of strong protectionist tendencies include the international discipline provided by WTO and a shift of business interests away from protectionism towards open markets. Both factors are reflected in current developments. We have not seen a systemic surge in import tariffs, while investment regimes have largely remained favourable towards foreign investments.

There remain, however, policy areas with potentially large impact on trade, and where WTO rules are less effective in avoiding trade-distorting behaviour by governments and firms. These include state aid and arguably the use of WTO trade defence measures. While it is highly unlikely that the protectionist use of WTO trade defence measures such as antidumping tariffs have contributed significantly to the great trade slump between November 2008 and February 2009 (Francois – Woerz, 2009), both because of the timing

¹ According to the second report of the Global Trade Alert a member of the G-20 has broken their no-protectionism pledge on average every three days since November 2008 (Evenett, 2009).

and the share of world trade affected, the use of subsidies in selected industries has been substantial. In addition, there has been and continues to be direct state intervention in the restructuring of motor vehicle production, above and beyond direct subsidies. Subsidies may not necessarily curtail existing trade flows. However, their potential to distort trade flows is high. They are tilting the playing field in favour of firms receiving public support. In the car industry the world's leading producers were all granted large amounts of subsidies from different governments. Their international presence put them in a most favourable position to extract public funds by creating a type of "subsidy competition" between governments. This development is very much to the detriment of the G20's commitment to open markets and fair and transparent competition.

2. Classical Protectionism: Tariffs

The most obvious way for countries to protect domestic firms from foreign competition is the imposition of new import tariffs or quotas. So far the increase in the use of these tools has been limited, suggesting that the world's trading partners have so far respected their obligations to each other stemming from WTO rules and regional trade agreements in this respect. This is good news for world merchandise trade. Around 30% of world trade is completely tariff free because it takes place within the free trade areas of industrialised countries, that is mainly EU and NAFTA (Table 1). Another 40% of world trade constitutes imports from OECD-members for which their applied rates equal (or are very close to) the maximum tariff allowed under the WTO GATT (bound rates)². This implies that almost 70% of world merchandise trade is strictly bound by currently applied tariffs. Moreover, a significant share of the remaining trade is on the account of East Asian countries whose applied tariffs are also rather close to their bound rates for the majority of tariff lines.

Table 1: Breakdown of Merchandise trade

	2006	2007	2008
NAFTA imports	21.20	19.48	19.83
Intra-NAFTA	7.15	6.54	6.51
Extra-NAFTA	14.05	12.95	13.32
EU imports	38.53	38.73	38.16
Intra-EU	22.84	23.39	22.33
Extra-EU	15.69	15.35	15.83
Total OECD imports	70.74	68.95	67.25
of which EU	38.53	38.73	38.16
of which NAFTA	21.20	19.48	19.83
other	11.01	10.73	9.26

Quelle: UN COMTRADE, WITS. EU is EU25.

² The sole exception to this is Australia.

Hence, leeway for the world's major trading nations for import protection via general tariff increases is basically non-existent. Provided the whole global free trade architecture does not fall into pieces, fears of large-scale protectionism in this area are unfounded.

In addition to the shield against protectionism provided by the WTO, the internationalisation of firms also supports low tariff regimes. This is because multinationals are deeply involved in global sourcing and therefore are both heavy exporters and importers. The reliance on global sourcing and potential negative consequences of increased tariffs on downstream operations makes high tariff regimes less likely (Francois – Nelson – Pelkmans-Balaoing, 2008).

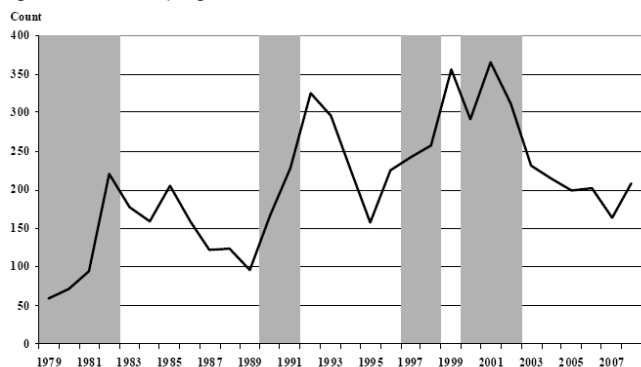
The disciplines imposed on governments of industrialised countries by the WTO and regional trade agreements implies that if they give in to domestic interest groups asking for protection they have to resort to other instruments. These include WTO trade protection mechanisms (including antidumping actions, countervailing duties and safeguards) and firm subsidies. We will discuss developments in both these policy areas since the outbreak of the crisis with a view to the role of multinational firms.

3. Administered Protectionism: Antidumping

The fact that industrialised countries' pre-crisis tariff rates largely equalled bound rates forces them to resort to trade defence measures in cases where domestic producers or labour unions successfully lobby for import protection. Trade defence measures form an integral part of WTO rules. These contingency measures are viewed by many scholars of the trading system as a safety valve and give WTO members the option of avoiding drastic and/or politically problematic increases in imports of specific goods (safeguard measures) and to defend themselves against unfair practices of other WTO members (countervailing duties against subsidies) or foreign firms (antidumping measures).

In practice, however, a good deal of the antidumping (AD) duties, countervailing duties (CVD) and safeguard measures are initiated and implemented to shelter domestic firms from foreign competition and not necessarily to counter wrongdoings by trading partners. Since demands for protection from foreign competition increase in times of crisis, contingency measures tend to rise during economic downturns (Francois – Niels, 2006). Figure 1 shows that the number of antidumping initiations typically increases during economic downturns.

Figure 1: Anti-Dumping Initiations 1979-2008



Quelle: WTO. Grey areas indicate periods of economic recession.

Anti-dumping measures are the most intensively used contingency measures. In theory, they give countries the flexibility to defend themselves against selling practices of foreign firms deemed unfair³. Since anti-dumping measures are implemented against particular firms they are very specific. The specificity of anti-dumping measures also make them a very suitable tool for providing protection to particular interest groups. This means that trade barriers can be implemented for imports from selected firms from selected countries without otherwise undermining the general structure of bindings on import protection. This provides some shelter against import competition from the targeted firm(s) but leave the remainder of the trade flows unaffected, even those within the product categories (tariff lines) hit by the antidumping measure. This is not the case with global safeguard (GS) measures. GS measures set a quantitative restriction on the permissible market share of all imports in the targeted tariff line(s). Historically the GS clause has been used much less frequently than the antidumping option (Figure 2).

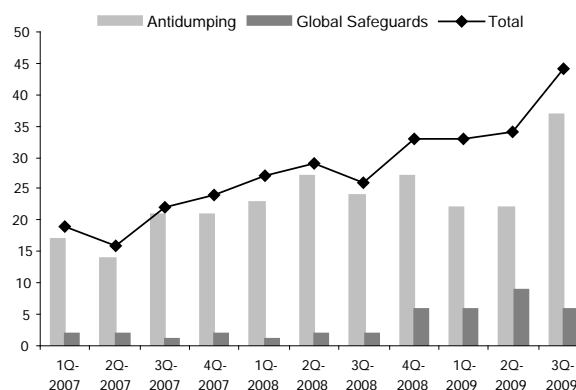
The developments since the outbreak of the global economic crisis show the same pattern: the use of WTO trade defence measures increased markedly with a strong focus on antidumping. This does not come as a surprise and so far it is still in the range of increases observed in previous crises. In fact the measurable impact on trade flows is very small. In the period from the 1st quarter 2008 to the 1st quarter 2009 initiated trade defence measures hit less than half percent (0.45%) of global trade (Bown, 2009a). For 2009, data point to a 30% increase in remedies (Bown, 2009b). This implies 0.15% of trade has been affected by the increase in trade remedies.

The misuse of trade defence measures for protectionist purposes is nevertheless an unpleasant development since it entails the risk of tit-for-tat retaliation and cascading protectionism. The latter refers to the fact that tariffs on intermediate inputs generally increase

³ This includes charging lower foreign prices than domestic prices and prices below production cost.

the prices of domestic goods that depend on those imported inputs. This increases the likelihood that producers of these downstream goods will demand import protection (Hoekman – Leidy, 1992; Feinberg – Kaplan, 1993).

Figure 2: Initiations of new Trade Defence Measures



Quelle: Bown, 2009: "Global Antidumping Database". The difference between Total trade remedy measures and antidumping global safeguard measures are countervailing duties and China-specific safeguard measures.

In general, multinational firms are expected to have little interest in trade barriers (including trade defence measures) because it reduces the efficiency of their global supply networks both with foreign affiliates and independent firms. In the recent special safeguards action in the U.S. in tires from China, for example, producers were opposed to the measures taken, and it was instead pressure from labour unions that led to the decision to impose duties. In specific cases, however, multinationals have been shown to exploit the system of WTO administered protection mechanisms to their advantage. Indeed some of the antidumping measures implemented since the 1st quarter of 2008 involve anti-competitive behaviour by multinationals. Anti-competitive behaviour includes both attempts to segment markets and support for import restriction measures once a foreign affiliate is set up and the market is not served via exports anymore.

One case of using AD for anti-competitive behaviour involves the Indian and Chinese subsidiaries of Osram, a leading light bulb producer with headquarter in Germany. In February 2009 India imposed an AD measure on "compact fluorescent lamps" from China which consisted of a voluntary price increase by Chinese producers. Higher prices charged by foreign exporters typically translate into lower imports. Interestingly, the Indian firm petitioning for the AD measure was Osram India Pvt. Ltd., the Indian subsidiary of Osram and among the targeted Chinese firms that joined in the price agreement was Osram China Lighting Co. Ltd, the Chinese subsidiary of Osram. This suggests that the Indian and Chinese affiliates of Osram took advantage of the AD price agreement to segment markets.

Another interesting case, from the steel industry, involves the EC as initiating party. In December 2008 the EU imposed AD duties on “certain welded tubes and pipes of iron or non-alloy steel” from Belarus, China and Russia. Two months later preliminary AD duties on “wire rod” from China, Moldova and Turkey followed and in April 2009 the EU added preliminary AD duties on “certain seamless pipes and tubes”, this time from China. Surprisingly, none of these measures included India, a major exporter of steel products, as a target country for AD measures. In 2006 Indian steel producer Mittal⁴ had acquired the European Arcelor and in 2007 the Indian conglomerate Tata had merged with British Corus (Bown, 2009a).

Here we have one case where the strategy of a multinational company consists of using AD measures to segment markets and increase the producer rents, and another case where a multinational company has joined forces with domestic producers of the host country to lobby for specific import protection.

4. New Protectionism: Subsidy Games

The world is very unlikely to re-experience an old-fashioned, broad-based 1930-style of protectionism. Tariff increases have been marginal (and limited to individual countries such as Ecuador or Russia which is not a WTO-member). WTO GATT disciplines are designed to prevent this from happening, while the global fragmentation of production has altered the political economy of protectionism. However, while global sourcing may undermine political dynamics for general increases in tariffs, it may also be driving the political game toward more lobbying for subsidies. Indeed, firms with production facilities scattered around the globe may find themselves in a quite favourable position for extracting subsidies from governments.

Government subsidies to support both struggling sunset industries and aspiring new industries have a long tradition in industrialised countries. Also, their use is not confined to times of crisis. In 2007, for example, EU member states, on average, spent 0.53% of GDP on state aid (Eurostat). The long tradition of firm subsidies does not alter the fact that they are problematic with a view to fair competition among firms in international markets. Also, in times of economic hardship they tend to increase, in particular to incumbent but struggling firms. This is evidenced by the gigantic amounts involved in the bank bailouts during the course of the financial crisis. Spending on stimulus measures in 2009 alone will amount to about 1.7% of GDP in the U.S. and roughly 1% in the EU (Saha – Weizäcker, 2009). This will burden governments with debts and the strains on fiscal budgets will be felt (by taxpayers) for

years and probably decades. Government bail-outs and state aid also constituted 32% of all trade-related measures that have been implemented by members of the G20 since their first meeting in November 2008 (Evenett, 2009). This extraordinarily large share of state aid was predominantly to the benefit (including the rescue) of banks deemed of systemic importance (read: big enough to not let them fail). The financial sector is an issue apart and the bank bailouts may have been the lesser of two evils. But subsidies granted to the real economy also stepped up. Unfortunately, transparency is not really impressive in this area and so little is known about the amounts involved let alone to whom. In addition, the game is ongoing and so we do not know the final score yet in terms of dollars, euros, and pounds. Despite the scarcity of reliable information, it is safe to say that the automotive industry has been the primary beneficiary when it comes to financial benefits granted by governments. Back in March 2009, the World Bank estimated the global amount of subsidies to the car industry at USD 48 billion of which USD 42,7 billion was granted by industrialised countries (Gamberoni – Newfarmer, 2009).

Subsidies are a prime example of measures that do not necessarily curtail existing trade flows. Yet they can be a powerful tool for distorting international competition and the location of production. The recent French plan to make subsidized loans in an amount of EUR 3 billion each to national car manufacturers PSA Peugeot Citroen and Renault was contingent on the relocation of foreign production units back to France. The European Commission halted this design of the subsidy after loud protests from Slovakia and the Czech Republic. The formal pledge for locating production in France was avoided but the French government relied on “moral obligation” of car makers and these undertook to not shut down plants for the next five years (OECD, 2009).

The fact that crisis-related state aid has been concentrated on the car industry is important because it accounts for more than 7% of world trade (Table 2). For the OECD and in particular for the EU this share is even larger. The high trade intensity of the car industry implies that state intervention in the restructuring of firms has the potential to be highly trade distorting. There are also several factors that help explain why it is the automotive industry that has extracted large amounts of taxpayers' money from governments in this process. First, the automotive industry is the major manufacturing industry in many OECD countries. In addition, it suffers from huge overcapacity estimated at about 20 million units in 2008 (The Deal, 2008) of which 7 million in Europe and 6 million in the U.S. (The Economist, 2009). Similar experiences have been made in previous crisis with other industries characterised by massive overcapacities at the time, including steel and shipbuilding.

⁴ In legal terms, Mittal is not an Indian firm anymore because it is registered in Luxembourg and the Netherlands Antilles.

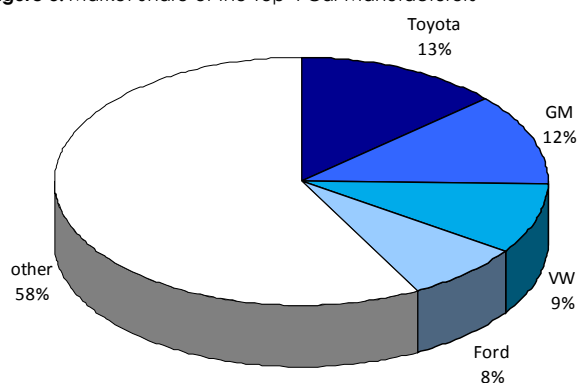
Table 2: The Role of Cars in World Trade

	motor vehicles and parts	motor vehicles	Parts
share of world trade			
2006	7.80	5.71	2.09
2007	7.96	5.85	2.11
2008	7.10	5.21	1.89
share of intra-OECD trade			
2006	11.58	8.90	2.68
2007	11.42	8.88	2.54
2008	10.06	7.90	2.15
share of intra-EU trade			
2006	13.05	9.14	3.91
2007	13.34	9.41	3.93
2008	11.82	8.40	3.43

Quelle: UN COMTRADE. EU is EU25.

Another reason why state intervention may be problematic in the case of motor vehicles has to do with the oligopolistic market structure of the industry. The industry is characterised by a limited number of large multinational firms. Among these global players, the top four producers – Toyota, General Motors (GM), Volkswagen and Ford – have a market share of over 42% (Figure 3). This means these four firms collectively account for roughly 3% of world trade and over 4% of OECD trade. Collusion, including among firms, is much easier if their number is small because the free rider problem is easier to control.

Figure 3: Market Share of the Top 4 Car Manufacturers



Quelle: OICO World Ranking of Manufacturers 2008.

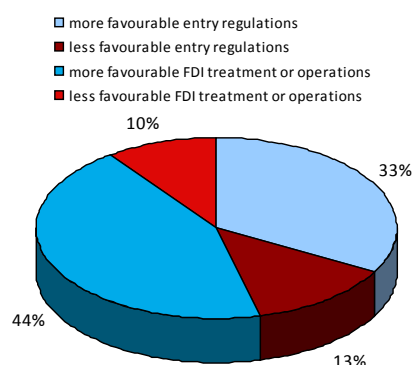
The oligopolistic market structure prevailing in the automotive industry, coupled with the size of the industry in terms of trade, output and employment can be seen as problematic from a political economy point of view. Large industries can be of greater importance to political decision makers and hence

more likely to be successful in their lobbying activities. The car industry, having a high concentration ratio, is expected to lobby for subsidies rather than for tariff protection (Grossman – Helpman, 1994). Moreover, subsidies are preferred because they leave complex production chains intact. In addition the fact that the car multinationals have scattered their production facilities all around the world puts them in a favourable position to demand subsidies by playing governments against each other. Hence, the constellation in the automotive industry including large overcapacity, deep trade integration, oligopolistic market structure and large share in output makes it the logical candidate for subsidies while its importance in world trade makes those subsidies highly problematic from a trade perspective.

5. Multinationals on Subsidy Binge

The integration of markets and production via FDI activities of multinationals has become the centrepiece of the globalising world economy (Sauvent, 2005). All leading multinational firms run multiple production facilities in several parts of the world. This implies that the world economy of today is especially vulnerable to investment protectionism. Investment protectionism is about governments preventing multinationals to set up affiliates abroad or acquire existing foreign firms. Fortunately, this has not happened so far, at least not on a great scale. The general trend in FDI policies is still towards increased openness (UNCTAD, 2009) (Figure 4). Likewise the latest joint OECD – WTO – UNCTAD report on trade and investment measures (OECD – WTO – UNCTAD, 2009) concludes that overall investment policy measures taken by member of the G20 were directed towards increasing openness and clarity for foreign investors facilitating international investment and financial flows.

Figure 4: Nature of FDI-related measures in 2008



Quelle: UNCTAD, World Investment Report.

There is, however, a worrisome aspect related to international investment and the ability of multinational

firms to shift production from one country to another quite easily.

The locational flexibility of multinationals is not a new observation and the notion of "footloose capital" has triggered concerns about negative effects for internationally less mobile factors such as unskilled labour. If capital is able to move around at low cost, any additional costs (such as government taxation) imposed on them by one country, could make multinationals leave for another country. With increasing international integration of markets (i.e. reductions in trade costs), multinationals get more sensitive to financial incentives offered by potential host governments (Ottaviano, 2004). The advantages associated with the geographic flexibility of multinationals and the impact on government policies is at the heart of the theory of international tax competition. This theory suggests that the geographic flexibility of multinationals eases the tax burden for capital (the mobile factor) to the detriment of labour (the relatively immobile factor). For OECD-countries there is some evidence that multinationals have benefited from international tax competition between governments through lower taxes on profits and that it has intensified since the 1980's (Winner, 2005).

Akin to the logic of the international tax competition between governments, global car manufacturers have now managed to play out several governments against each other in their quest for subsidies. The fact that the industry is suffering from considerable overcapacity turned out to be quite advantageous in this. The subsidy competition game played by global car manufacturers is quite simple. Governments that are unwilling to fork out money during times of crisis are confronted with the prospect of having the local production facilities closed. The knowledge about the need to curtail global production capacity makes such a threat credible. GM played this strategy very successfully against the Australian government. After the announcement of closing a factory in Thailand, they managed to extract subsidies from the Australian government for their local subsidiary Holden (Francois, 2008). Of course, GM, Toyota and Chrysler have also lined up for subsidies in the U.S. and booties were ample.

In the EU the sale of Opel, the German branch of GM, entailed an interesting subsidy competition among EU member states with Opel production facilities ("Opel-countries"). The German government pledged EUR 4.5 billion in state aid (EUR 3 billion in guarantees, EUR 1.5 billion for a bridge-loan) for the consortium of bidders consisting of the Canadian car part supplier Magna and Russian Sberbank. It was clear from the outset that Germany's primary interest in this deal was to minimise domestic job losses and to ensure that all four German production sites would remain open. In fact, the EUR 4.5 billion in state aid was only offered to the Magna-Sberbank consortium but not to the other bidders for Opel, presumably because its restructuring plans for Opel, which contains around 11,000 Opel job cuts in Europe (FAZ, 2009), would affect Germany less

than the concepts of rival bidders. Germany also invited other Opel-countries such as Austria, Belgium, Poland, Spain and the United Kingdom to participate in the EUR 4.5 billion-rescue operation for Opel and was demanding a fair burden sharing. The deal, however, frustrated Opel-countries that would – according to Magna's plans – be more than proportionally hit by its restructuring operations. The prospect of a plant closure in Antwerp (involving some 2,500 job losses) and severe job cuts in British Vauxhall plants (around 1,400) evoked protests in Belgium and the United Kingdom. Both countries accused Germany of having used its state aid to the Magna-Sberbank consortium to 'buy' Opel jobs in Germany (FAZ-online, 2009a) and in October the European Commission raised doubts about the state aid for Opel, the critique being not the state aid per se but the German attempt to influence the bidding process for Opel in favour of Magna-Sberbank. After the French car subsidy case, the very public role played by Brussels in the Opel restructuring demonstrates that, at least in Europe, there are some mechanisms that limit the scope for Member governments to fight subsidy wars in times of economic crisis.

As it turned out now, however, the European Commission will not have to rule on the Opel sale because on November 3rd GM surprisingly announced that it will keep Opel (GM media, 2009)⁵. With this decision by GM – which after a USD 50 billion bail-out emerged in July from a bankruptcy procedure as a debt-free company 60% owned by the U.S. – the next round of the subsidy game has been launched and the cards reshuffled. GM itself will turn to European governments for assistance to cover its expected restructuring costs of EUR 3 billion which it hopes to come from the United Kingdom, Poland, Spain and Germany (WSJ, 2009). The German government, from which GM expects EUR 2 billion in state guarantees, might now insist on the repayment of the outstanding bridge loan which is due end of November. While the Opel works council now fears the closure of plants in Bochum and Kaiserslautern (both Germany) (FAZ-online, 2009c) the UK-governments is confident that the British Vauxhall plants at Ellesmere Port and Luton have a bright future and announced to closely work together with GM in the restructuring operations, explicitly mentioning the possibility of state aid to secure jobs (Financial Times, 2009).

While one may be familiar with governments quarrelling over firm subsidies (such as the mutual accusations of the U.S. and the EU over support for Boeing and Airbus or the EU - Korea dispute over state aid to shipyards), this case is different. Here different national governments are not subsidising each their national

⁵ According to media reports the board of GM reconsidered the sale of Opel only after being asked by the Commission for confirmation that the sale of Opel to the Magna-Sberbank consortium had not been influenced by political pressure (FAZ-online, 2009b; Financial Times, 2009). Officially, the U-turn in GM's strategy is based on commercial grounds (GM media, 2009).

champion. The dispute here involves just one large multinational firm that can decide where to realise the needed capacity (and job) downsizing and may make this decision dependant on the amount of state subsidies offered to them.

'Shopping for subsidies' by multinationals adds a new shade to the existing spectrum of protectionism. It is the result of the international mobility of multinationals and their ability to shift production around globally. After having used this advantage to avoid taxation by host governments (international tax competition) global car manufacturers have now used their political weight and their international leverage to initiate a subsidy competition among national governments, a process with some similarity to the international tax competition during times of expansion.

Certainly, the multinational firms' capability to play out national governments against each other for subsidies also requires the appropriate environment. Governments provided this by failing to coordinate and jointly restrict subsidies to multinationals. Moreover, the WTO does not exercise the same authority in the field of firm subsidies (covered by the Agreement on Subsidies and Countervailing Measure, ASCM) as it does via the GATT in the field of tariffs⁶. In fact, the European Commission was tinkering with the idea to take the U.S. to the WTO for the support provided to GM and Chrysler. But it quickly dropped this idea when it became apparent that large European car manufacturers would also require assistance (Hufbauer – Stephenson, 2009). Certainly, a country's own subsidies do not prevent it from initiating a subsidy case against another WTO-member. The most likely reaction, however, is then the initiation of a counter-case. Meanwhile, the main producer countries of cars, including Japan, Germany, the United States, France, Spain, South Korea, China and Brazil, have subsidy programmes in place to support car manufacturers. Therefore a WTO-case over car subsidies is highly unlikely and the result is that the car industry managed to put itself outside the international framework provided by the WTO's ASCM.

It seems that the political market for state support successfully managed to innovate around existing international disciplines (Francois, 2009), creating countless subsidy programmes that come in all forms and shapes, including tax credits, de-minimis grants, R&D subsidies, green subsidies and subsidised loans and guarantees.

In the EU, the European Commission could have taken a tougher stance against the scale up of subsidies to the car industry but chose not to do so. While the Commission stopped French plans to make subsidised loans to national carmakers conditional on guarantees to secure French plants and jobs and also intervened (possibly in a decisive way) in the Opel case, it predominantly deals with 'strings' attached to national

⁶ The same is true for the EU and NAFTA.

subsidies that overtly discriminate between EU member state on the ground of nationality. The impact of these interventions is far from clear (see French car makers' "moral obligations" and the next round in the Opel subsidy game).

Moreover, by adopting the *Temporary Community framework for State aid measures to support access to finance in the current financial and economic crisis* ("Temporary Framework")⁷ in December 2008, the European Commission facilitated the granting of subsidies. The Temporary Framework offers member states increased flexibilities for selected forms of state aid⁸ such as de-minimis subsidies, subsidised interest loans and grants for 'green products'. Member states have made intensive use of the Temporary Framework⁹ and despite the fact that the Commission likes to see it as a horizontal programme, the subsidies granted under the framework are strongly focused on the car industry (European Commission, 2009). Therefore, also within the EU, the framework was not appropriate to avoid large amounts of national subsidies going into global operations of multinational firms.

6. Résumé

It is too early to give a final judgement on whether there will be extensive protectionism emerging out of the crisis. Tariffs are (for the most part) safe and the potential of WTO trade defence measures to turn-off trade flows are minor in comparison. The interventionism taking place in the car industry, however, is certainly bad as it both distorts competition among internationally competing firms and undermines international trade rules. The subsidies granted to the car industry are problematic for another reason: in some cases global car manufacturers have extracted these subsidies by threatening national governments with plants closure and job cuts. In the worst case this type of an international subsidy game between national governments – which is basically a harmful international tax competition in reverse – will spill over to other industries. The question is then: who is next in line?

7. Policy Implications

The global economic crisis has led to increased pressure on the world trading system as evidenced by the

⁷ The Framework is called temporary because measures may only be implemented until end of 2010.

⁸ Additional measures in the Temporary Framework include the possibility of higher public injections to risk capital of small and medium-sized firms (SMEs) and official Export Credit Agencies (ECA) may engage again in the short-term insurance business within the EU market, a domain which previously was considered to be "marketable risk" and therefore "no go" territory for public ECAs.

⁹ As of September 9th, 2009 more than 50 measures have been notified and cleared by the European Commission.

increase in the use of WTO trade remedy measures. However, the impact on trade of this increase has actually been quite small: on a trade-weighted basis an additional 0.15% of world trade will be affected by trade remedies measures in 2009. While antidumping and safeguards do not pose a systemic risk, there should be worry about the new willingness to provide state aid, in particular with multinational firms going on an international subsidies spree. This is because subsidies clearly are not well contained by current trade rules

Given the current developments in trade-related policy areas the following policy suggestions are offered:

1) Rather than piecemeal subsidy games between governments, a coordinated approach to restructuring in motor vehicles is called for. This could be carried out under the auspices of the OECD, much like earlier efforts in the steel industry and shipbuilding. In the absence of coordination, global multinationals can use their international mobility to induce international subsidy competition between different jurisdictions (in the car industry this has already been going on). Avoiding such a scenario requires national governments to colude.

2) Policy makers should increase transparency in the area of subsidies. Even in the EU, where common rules on state aid exist and support schemes must be notified to the European Commission, transparency is low. This stems from the fact that often only state aid schemes are made public but not the individual subsidies granted. For example, the Austrian aid programme for large firms (*Unternehmensliquiditätsstärkungsgesetz*) which is worth EUR 10 billion was made public. But no official information on the firms that benefited from this aid scheme (which is managed by Austria's export credit agency OeKB), let alone the amounts of subsidies paid out, is publicly available. Anybody interested in this matter has to rely on press reports¹⁰. Such secrecy in a policy involving large amounts of taxpayers' money helps firms to extract large amounts of subsidies. If subsidies are granted to firms, the legitimate interest of the public should prevail over business confidentiality.

3) In the EU, state aid rules (and competition rules in general) should be part of economic framework policies and not industrial policy or fiscal stimulus programmes. Therefore they should be independent of the business cycle and not to be changed during times of crisis. For EU member states this would imply waiving the flexibilities provided by the Temporary Framework adopted by the European Commission.

4) If governments find it impossible to avoid WTO trade remedy measures because of domestic pressures, global safeguards should be given priority over selec-

tive anti-dumping measures (and countervailing duties). Global safeguards are less discriminatory and less prone to abuse for anti-competitive behaviour.

8. Literature

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