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The New Advocacy for Autarky: Self-Sufficiency is Now Once Again Becoming Popular for Geopolitical Reasons

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Abstract: International economic relations and trade in particular have been thriving since World War II. Whilst the lowering of trade barriers and the dismantling of trade restrictions have long enjoyed support both among trade economists and policymakers, there has recently been a swing back to protectionist policies. In virtually all major economies, a surprising new interest in autarky can be observed. Today, both the USA and the member countries of the European Union prioritize domestic production of certain products, especially semiconductors. China has taken a decisive turn to trade policies that emphasize self-sufficiency and domestic production. India, which has long favoured sourcing from domestic producers, has at least partially embraced self-sufficiency. We analyze and add a historical lens to these recent developments. If they will continue, we argue that the world will see negative effects on welfare if these trends continue unchecked.

Keywords: autarky, international division of labor, self-sufficiency

1 Introduction

A surprising renaissance of protectionist thinking has recently emerged in major economies. China, India, and the United States, the world’s three most populous nations, have altered their trade policy priorities. Starting in 2017, President Donald Trump vehemently promoted the purchase of American products. His successor, Biden, has likewise not been advancing liberal trade policies. In India, Prime Minister Narendra Modi is not only promoting the domestic production of goods (“Make in India”), but has at least temporarily been focusing on wider self-sufficiency. The biggest policy swing, however, has occurred in China. As early as 2018, General Secretary Xi called for a reduction of China’s dependence on imports and exports. Worryingly, Europe is also nurturing its protectionist reflexes. French
President Emmanuel Macron sees the need for a change in globalization from its previous dominant form since the early 1970s. In 2022, the European Union has been joining other economies in the surge of subsidies for semiconductor manufacturing. Suddenly, the call for self-sufficiency is back. Autarky enjoys a renaissance. This shift is alarming, especially in the European context, where economic cooperation has been considered the foundation of peace since the end of the second World War.

The SARS-Covid 2 crisis has by no means been the only reason, but has certainly been a catalyst for the new longing for autarky. The probably most important reason for this turnaround in trade policy has been the geopolitical conflict between the People’s Republic of China and a number of countries, first and foremost the USA. Both the U.S. and India aim to trade less with China in the future. But Beijing itself is also turning away from the world market and sooner or later no longer wants to be dependent on imports of important intermediate products, especially semiconductors manufactured abroad. Security of supply has become more important today than economic efficiency.

The main casualties of this turnaround will be Europe’s export-oriented economies. German companies in particular could run out of markets for their products in the medium term. However, the European Union’s trade policies in recent years have contributed to a certain frustration with globalization. The EU’s partially protectionist policies have not only made access to the European market more difficult but have also contributed to considerable trade surpluses for the group of states. With the departure of Great Britain, which has been running trade deficits in European and non-European trade for many years, the mercantilist character – having a preference for exports – of the European trade policy will become even more apparent.

In this paper, we will look at four major economies and their trade policies. The world’s largest economy, the United States of America, continues to implement partly protectionist economic policies. President Trump has of course emphasized an anti-Chinese trade policy, but he has not invented an approach that prioritizes domestic production. However, Washington has been very capable of concealing protectionist policies with opaque instruments like rules of origin in its trade agreements. Of course, the European Union has both embraced a mercantilist trade policy and has recently also been leaning toward self-sufficiency, in particular in semiconductor manufacturing.

China is a particularly relevant case, because it is sharply turning inward under Secretary General Xi Jinping. Whilst China, the world’s second-largest economy, has

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2 In this paper, we are defining “autarky” as an economic policy that aims at reducing the dependency on imports to a very low level. “Self-sufficiency” is defined as a very limited dependence on imports and is the result of autarkic economic policies.
been benefitting from the opening of its economy with the reforms of Deng Xiaoping in the late 1970s, today the Chinese leadership wants to turn the clock back to trade policies inspired both by Imperial and Maoist China. India, soon becoming the world's most populous state, has also been flirting with autarky, although in 2022 the government of Prime Minister Narendra Modi appears to gradually reconsider its recent swing towards self-sufficiency. A major force in the re-emergence of autarkic thought have been the sanctions applied against Russia. We argue that the sanctions contribute to a further weakening of the concept of a liberal economic order. Sanctions and autarkic thought have historically reinforced each other.

2 Self-Sufficiency in Large Industrialized Countries

A major source of economic policies that emphasize self-sufficiency have been the United States. There is ample evidence for the protectionist trade policies of the United States, which in history hardly ever implemented a policy of relatively unrestricted international trade. A large body of literature analyzes the country's trade policy from a range of perspectives (e.g. Irwin 2016; Blinder 2019; Fajgelbaum et al. 2020). But the United States continue to implement trade barriers. Whilst the US also uses conventional instruments like tariffs to support domestic producers, other non-tariff barriers are used as well. Since these are often opaque, policy makers and the public often fail to understand that despite partial openness, the United States is not a country of free trade.

In 2022, President Joe Biden has launched a massive programme to promote green technologies in the US. The Inflation Reduction Act (IRA), which will take effect on 1 January 2023, contains a massive component for the subsidization of electric cars. At 369 billion US-dollars, the US government is spending the equivalent of the 2019 German Federal Budget on subsidies. The programme has a significant bias in favour of US manufacturers: The 7500 US-dollar subsidy for electric vehicles is restricted to cars with US components and which are manufactured in the United States. Of course, such measures are hardly compatible with WTO rules. The EU trade commissioner Valdis Dombrovskis called the measures a discrimination of the European automotive industry, including the manufacturers of components such as batteries. But the fact that the US government is willing to confront its OECD-partner

3 Sam Fleming; Andy Bounds: How does the EU respond to Joe Biden’s $369bn green subsidies bill? Brussels seeks to mitigate threat posed by incoming inflation legislation that it says breaches WTO rules. Financial Times, 27 November 2022, available at https://www.ft.com/content/f16ddb43-818c-4c82-8700-0c710659d443.
countries should not surprise. Time and again, the US has embraced trade policies that favor US manufacturers.

Some observers have assumed that the previous President Donald Trump had been inventing policies that put “America First”. In fact, President Franklin D. Roosevelt made similar statements way back in 1933. In his inaugural address on 4 March, 1933, Roosevelt had clearly spelt out that the restoration of pre-crisis world trade was no priority for him. He argued:

> “Our international trade relations, though vastly important, are in point of time and necessity secondary to the establishment of a sound national economy. I favor as a practical policy the putting of first things first. I shall spare no effort to restore world trade by international economic readjustment, but the emergency at home cannot wait on that accomplishment” (Roosevelt 1933).

In order to shed some light on the strife for self-sufficiency in the United States, we will briefly look at three elements of trade US trade policy that favor domestic production: The Jones Act of 1920, the lasting legacy of the 1962/63 Chicken War between the USA and the nascent European Economic Community and the rules of origin on cotton-based textiles in the North American Trade Agreement USMCA. Whilst all three constitute a violation of the spirit of the multilateral trading system, there has not been any systematic attempt in Washington to abandon those restrictive trade practices. Our point is that no observer should be surprised by Biden’s latest trade policy twist: It merely reflects a long-standing practice of American economic policy.

For more than a hundred years, an unusual regulation has been applied in the U.S. coastal shipping industry that has been unsuccessfully denounced by the EU mission in Washington for decades: the Jones Act of 1920. This law, known in the original as the Merchant Marine Act, excludes foreign suppliers from U.S. coastal shipping. Vessels must be made in the U.S., the ship must fly a U.S. flag, be owned by a U.S. company, and have primarily U.S. citizens on board as crew (Fritelli 2003). Since US ships must operate under a crew comprising 75% American citizens, the OECD estimates that the operating costs of a Jones Act eligible ship are around 2.7 times that of a foreign-flagged vessel (OECD 2019, 17). Of course, the high costs of coastal shipping have to be paid by both US consumers and US industries and reduces the competitiveness of the latter.

Another area of protectionism in the US is the vehicle market. So-called light trucks, very popular in many parts of the USA, are almost exclusively made in the US because that segment is protected by a high tariff. Vehicles that are classified as light trucks attract an import duty of 25%, compared to 2.5% for normal cars and station wagons. An import duty of such magnitude is too big a hurdle for foreign competition.
In 2023, the 25% tariff on light trucks will be operational for a staggering 60 years. Initially, the tariff was introduced by the Kennedy and Johnson administrations during the so-called chicken war between West-Germany and the US. Due to the harmonisation of agricultural tariffs in the European Economic Community, Germany’s import tariff for frozen chicken tripled. America took Germany to the GATT and won. The dispute was settled, and the US was permitted to impose retaliatory tariffs on dextrose, cognac and light trucks. Despite several hearings in the US International Trade Commission, the tariff remains in place (Ikenson 2003). Whilst the high tariff is occasionally criticized (Griswold 2002), it remains in place, prompting US consumers to buy a product that is made in the USA.

A particularly opaque instrument the USA uses to protect its domestic producers is the fiber-forward rule in the United States–Mexico–Canada Agreement (USMCA). That rule states that cotton must be produced in either the USA, Canada or Mexico to be eligible for duty-free trade of textiles made of cotton. Producers from Africa and other parts of the world are excluded. Yarn is generally subject to the “fiber-forward” rule which means that the fiber must originate in a USMCA country. Of course, the USA imports a lot of textiles from China and other Asian economies, but these textiles are subject to US tariffs.

This short list of restrictive trade practices shall serve to illustrate that protectionist thinking has long been a prominent feature of economic policies in the USA. Distinguishing protectionist from autarkic thought is difficult. Today’s strategies for self-reliance in semiconductors in the USA, China and the European Union have a strong autarkic component. Security concerns have regularly been used to justify the exclusion of foreign competitors, for instance in the Jones Act of 1920. Of course, the countries of the European Union have also been applying restrictive trade practices for a long time. The EU has implemented restrictive trade practices – agriculture is known best – for a long time and may thus have contributed to raising the interest of developing economies in self-sufficiency.

The question hence arises as to whether, apart from geopolitical developments, other factors have dented the interest of developing countries in continuing to emphasize the benefits of the international division of labour. One answer can be found in the trade balances of the European Union. The 27 economies currently in the Union have been running significant trade surpluses since 2012. Over the period from 2012 to 2019, the cumulative trade surpluses in non-EU trade amount to around €1240 billion. This means that the EU-27’s trading partners had to run corresponding deficits and take on corresponding debt. The persistent surpluses of the EU-27 may have led to an unequal distribution of the benefits of the international division of labor.

Before the UK’s exit from the EU, these surpluses were not particularly noticeable because the trade deficits were compensated for part of the surpluses generated by the continental European economies. From 2012 to 2019, the UK’s cumulative trade deficit amounted to €485 billion, or just under 40% of the EU-27 countries’ surpluses. Without the UK, the surpluses of the EU-27 economies have become more apparent.

Critics may object at this point that trade surpluses are not problematic in themselves. While this may be true for trade between OECD countries, the situation of developing countries is different. These economies regularly have to borrow abroad to compensate for a trade deficit. Moreover, a trade deficit dampens domestic employment. The English economist Joan Robinson, therefore, pointed out more than 70 years ago that a trade surplus results in export of unemployment (Robinson 1947, 156). In recent years, the EU-27 has failed to shape its trade policy in line with this insight. Moreover, servicing external debt is difficult when developing countries are facing obstacles in exporting to the EU. In 2022, the rising value of the dollar has made foreign debt an even more pressing issue for developing countries.

While the results of the EU’s trade policy raised questions even before today’s pandemic, it is now apparent that Europe is by no means immune to the lure of autarky. Certainly, there is no voice today calling for a return to the teachings of Friedrich Zimmermann, whose two books in 1931 and 1932 paved the way for the autarky thinking of the Nazis in Germany (Fried 1931, cf. Helleiner 2021, 16). But it should not be forgotten that there has been no continental European country that has had such broad social support for liberal trade as Britain. While Indian and Chinese economic history are characterised by protectionist theories, free trade theories dominated in Britain. In the nineteenth century, free trade was considered a civil right and not just a method to increase economic growth (Trentmann 2008, 2 and 10). After Britain’s exit from the EU, the free-trader camp is missing a powerful voice within the European Union. In combination with the 2022 political instability, both the call for trade restrictions and for self-sufficiency have been receiving increased political support.

Three factors have contributed to the renewed interest in self-sufficiency in OECD-countries in general and the USA and the economies of the EU in particular: The pandemic, the geopolitical conflict with China and the war in Ukraine have all contributed to the surprising return of the state as an actor in economic policy. Particularly in the area of subsidizing the production of semiconductors, today there is hardly any difference between China’s state economy and OECD countries. What is downright frowned upon at present is the suggestion that it would make more sense to let other countries subsidize semiconductor production and then buy the chips at market prices. The belief that today’s semiconductor shortages will last for a long time is unshakable.
Not surprisingly, industry representatives are calling for an expansion of subsidies. The European Commission launched the “Chips Act” in February 2022, which aims at doubling Europe’s share of global semiconductor production to 20% by 2030 and is spending the astonishing amount of 43 billion euros for that goal. But in September 2022 Cedrik Neike, member of the board of Siemens, has asked the Commission to fine-tune its policies. The current emphasis on high-end semiconductors ought to be replaced by broad financial support for semiconductor manufacturers. An explanation why taxpayers should continue to provide support for the semiconductor industry is of course not provided. The fear that there might be a continuing shortage of semiconductors is considered a sufficient justification.

However, temporary shortages of certain raw materials or components are neither new nor problematic. In 1928, the agricultural economist Arthur Hanau had pointed out the phenomenon of the cyclical developments in commodity prices and production (Hanau 1928). If one follows Hanau’s considerations, a medium-term disappearance of today’s semiconductor scarcity and falling prices can be expected. In 2012, Toyota showed how quickly supposed scarcity can be overcome. When the People’s Republic of China restricted the export of so-called rare earths and the prices for these metals quintupled, Toyota reacted with innovation: it developed a technology that enables the production of hybrid and electric cars with much lower use of rare earths.

Given today’s geopolitical situation, it would certainly be reckless to rely heavily on Chinese suppliers in the future. But the regression to a state-driven economy that can be observed today seems ill-conceived. The diversification of risk is an essential task of private enterprise and should not be the responsibility of any government in a market economy. At least within the group of developed countries, the international division of labor should not be mindlessly thrown overboard. It should not matter whether semiconductors come from Seoul, Taipei or Dallas.

At this point, remarkable parallels to the economic policy debates of the early 1930s emerge. Not surprising is the emphasis on economic autarky in the Nazi state. After the sanctions of World War I, some economists believed that autarky was the answer to the economic challenges of the 1930s (Fried 1931). In a similar vein, Fried called for “freedom of economic activity through state planning” (Fried 1931, p. 262).

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5 The European Parliament and the member states are currently debating the Chips Act.
7 Hanau argued that low prices, i.e. close to production costs, will result in a decline of production, which in turn will drive up prices due to limited supply. The subsequent price increases will increase production, in turn depressing prices.
3 Economic Thought in Imperial China and Xi Jinping in Mao’s Footsteps

Of course, state planning has been central to China’s economic policies since 1949. However, it is astonishing that China has been embracing autarkic thought in recent years when considering the economic growth after Deng Xiaoping’s opening of the Chinese economy in the late 1970s.

For observers of China pre-pandemic, especially the Hong Kong Special Administrative Region, the country appeared to be a model of efficient production and liberal trade. Within four decades, China emerged as the largest trading power. In 2018, seven of the world’s top 10 container ports were located in China, including Hong Kong.9

However, this preference for trade and the exchange of goods is a very recent characteristic of Chinese society. Mao Zedong’s focus after the break with the Soviet Union was on self-determined development (zili gensheng). For Communist China, it was important to reduce economic and political dependence on foreign countries and exploitation by the USSR and capitalist countries (Helleiner 2021, 18). In doing so, Mao was able to build on economic policy traditions that had shaped the Chinese empires for centuries.

Confucianism counted traders as the lowest of the four classes. The highest class was made up of scholars, followed by farmers and craftsmen. Even within the already low class of traders, differentiation was made: Those who traded with foreign countries had the lowest standing because they showed that China was not self-sufficient. This was considered a weakening of imperial dignity.10

China’s economic thinking differed from the theories of Western economists for a remarkably long time. The benefits of the international division of labour were long ignored. Confucian scholars emphasised the benefits of agriculture, which is understandable considering the importance of agriculture for China’s early development. Confucian thinkers already addressed the question of how to organise the economy more than 2000 years ago. They did so in the “Salt and Iron Conference” in 81 BC, engaging in a controversy whose results would shape China well into the twentieth century (Helleiner and Wang 2018, 467; Hu 1988, 277f).11

Similar to India, a liberal trade policy in China has historically been associated with coercions enforced by foreign powers and traumatic experiences. Both China’s

10 Alain Bihr, Warum China den Kapitalismus nicht erfand. Le Monde Diplomatique, 7 November 2019, p. 3.
11 For a detailed discussion see Heribert Dieter, Die neue Liebe zur Autarkie. Risiken für die deutsche und europäische Exportwirtschaft, SWP-Aktuell 18/2021.
defeats in the two Opium Wars against Britain (1839–1842 and 1858–1860) and the Taiping Rebellion (1851–1864) prompted conservative scholars to call for a return to traditional economic policy concepts. The aim of the two Opium Wars was to force the Chinese government to lower tariffs, the dismantling of other trade barriers and cede territories. France participated in the second Opium War. Both opium wars thus served to enforce a liberal trade policy against the declared will of the imperial government of the Qing dynasty at the time.

In line with traditional views that placed merchants at the bottom of the social hierarchy, conservatives in the nineteenth century warned against an increase in trade and the introduction of new forms of industrial manufacturing, the introduction of railways and mining, because that could undermine the traditional order of society. They were sceptical about foreign trade, fearing that it would threaten social stability. Conservative thinkers believed that foreigners had little value to offer China. According to the worldview of these thinkers, international trade was only conducted when one wanted to show favour to foreigners. China, in the view of conservative scholars, was at the centre of a universal moral order and led as a paramount example (Helleiner and Wang 2018, 457).

The differences to the economic policy paradigms in Europe – with its early developed trade routes and its rapidly developed cross-border division of labour since the eighteenth century – are very clear. China was forced to participate in globalisation – narrowly defined in economic terms as the deepening of trade in goods and services as well as the cross-border movement of capital – and does not look back on a long tradition of liberal economic thought.12

Deng Xiaoping’s reforms at the end of the 1970s marked the beginning of the rise of the Chinese economy. Deng enforced a twofold break with tradition. On the one hand, he abandoned the previous Maoist economic policy and left room for private initiative and market economy elements. On the other hand, he overcame the aversion of Chinese economic policy makers to foreign trade and the cross-border division of labour. Given the centuries-long isolation of the Chinese economy and the even longer preference for domestic production, this second dimension of Deng’s reforms has probably been even more important than his pushing back of the state in production.13

12 Surprising parallels emerge with the assessments of John Maynard Keynes, probably the most important British economist of the twentieth century. In 1933, Keynes rejected the free trade doctrine, which had been dominant in England until 1914 and remained very popular thereafter and advocated the domestic production of goods. He demanded in 1933: “… let goods be homespun whenever it is reasonably and conveniently possible” (Keynes 1933, 758).

Since General Secretary Xi Jinping moved to the top of the Chinese Communist Party in 2012, he has been trying to reduce China’s dependence on foreign trade again. China is still the world’s workbench, but the share of exports in economic output fell from 31% in 2008 to just over half that figure, to 17%, in 2019, the last year before the pandemic. Whilst trade with the rest of the world is still significant, domestic sources of economic growth have become more important since the global financial crisis.

In November 2018, General Secretary Xi felt the time had come for a return to Mao’s old concepts. Xi complained that it was becoming increasingly difficult to source high technology from abroad. Growing unilateralism and protectionism of other countries would force China to turn to the path of self-sufficiency. Xi presented these thoughts in the northeastern province of Heilongjiang, located in China’s rust belt. That is where China’s industrialisation began.

In October 2020, General Secretary Xi specified his foreign economic policy reforms at the fifth plenary session of the nineteenth Central Committee of the Communist Party. The strategy, called “double circulation”, has two central elements: China is to become less dependent on foreign countries by strengthening domestic production and demand. At the same time, Xi wants to ensure that China remains indispensable for international production networks. China wants to break away from other markets, but these should remain dependent on supplies from China. In a nutshell: Autarky is good for China, but not for the rest of the world.

It remains to be seen whether Beijing will succeed in completely replacing Western high technology. Both in computer technology and in aircraft construction the technological hurdles that have to be overcome are not trivial. Nevertheless, General Secretary Xi has repeatedly made clear his intention to make the People’s Republic independent of Western imports. Remarks to the contrary, for example at the 2021 virtual World Economic Forum, seem unconvincing against the background of the current Five-Year Plan and probably primarily serve to conceal the new Chinese policy.

4 India: Back to Gandhi?

Before the pandemic, India was considered a promising economy that could follow the development path of other Asian countries. Liberalization of trade in goods

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16 Tetsuhi Takahashi: A Future in which China no longer needs the world, but the world cannot spin without it, Financial Times, 16 December 2020.
would have played a central role in this model. Prime Minister Narendra Modi’s
government made a drastic reversal of course in 2020 and has at least temporarily
been striving to partially decouple India from world markets. Strikingly, the ration-
nale for this U-turn in trade policy contains both economic and geopolitical
arguments.

Protectionist trade policies have long been enjoying broad political support in
India. Mahatma Gandhi had raved about “swadeshi,” an economic autarky of the
subcontinent. Gandhi’s vision was self-governing villages that would exist largely
without foreign trade. Gandhi rejected objections that such a policy based on
self-sufficiency would be inefficient, arguing that economic development was more
than material prosperity: ethical and spiritual dimensions were just as important
(Helleiner 2021, 13).

Since independence in 1947, Indian governments had consistently relied on
trade policies that offered a high degree of protection for domestic producers until
the severe economic crisis of 1991. With this emphasis on “self-reliance”, India was
not a stark exception among developing countries, but pursued a long-popular trade
policy that had been advocated in Europe in the nineteenth century first and
foremost by Friedrich List. The turning point came in 1991 with the collapse of the
USSR. Manmohan Singh, then finance minister and later prime minister, praised
the economic successes of East Asian economies and imposed a significant liberal-
ization of foreign trade on his country. Singh convinced the Indian people that
economic reforms, including liberalization of foreign trade, were necessary. Tariffs
on industrial products (simple average) fell from 82.1% (1990) to 7.9% (2018).17

The effects of liberalization have been remarkable: India’s economic output
grew from $266 billion (1991, in current U.S. dollars) to $2837 billion in 2019. Despite
strong population growth – the country’s population grew by about 500 million
people between 1990 and 2019 – per capita economic output grew fourfold over the
same period, from $567 (in 2010 U.S. dollars) to $2128 in 2019.18 Of course, that
progress was not entirely due to liberalization, but the removal of trade barriers
helped improve the welfare of hundreds of millions of Indians.

However, that policy of abandoning import substitution and embracing the
world market was never uncontroversial. After the country’s independence, free
trade was repeatedly interpreted as a form of imperialism and an obstacle to
achieving full independence (Nilekani 2009, 121). Protectionist reflexes were
repeatedly evident in India’s lively debates on foreign trade. In the World Trade
Organization (WTO), India was among the skeptical voices even before the most

17 Data from the World Bank, World Development Indicators, available at https://databank.
worldbank.org/source/world-development-indicators.
18 Ibid.
recent shift away from deepening the international division of labor. India was one of the main opponents of the Doha Round and also opposed the conclusion of plurilateral agreements within the WTO.\(^\text{19}\) For a long time, many Indian observers saw their domestic companies as too uncompetitive to match corporations from more advanced economies.

In addition, India has chronic trade deficits. From 2010 to 2019, the cumulative trade deficits (goods only) amounted to around USD 1.542 billion.\(^\text{20}\) The surpluses in services trade could only partially compensate for these deficits in goods trade. On balance, India has been consistently dependent on capital imports and thus on the assessments of the providers of capital. For some Indian observers, this dependence poses a problem.

Indian economic history plays an important role in assessing the effects of liberalized trade. Many Indians have not forgotten that the British colonial power enforced free trade just when its own textile industry had become competitive through the introduction of mechanized looms. In the early eighteenth century, Indian textiles still accounted for 25% of the world textile trade. In the nineteenth century, exports of British textiles to India grew rapidly: from 60 million yards of fabric in 1830 to 968 million yards of fabric in 1858 (Tharoor 2016, 9). India became the most important market for British textiles: Whilst in 1830, a mere 6% of British textile exports were shipped to India, that figure had risen to more than 50% in 1873 (Goswami 2004, 62). As a British colony, India was part of a British-centered world economy and participated in a system of “free-trade imperialism” (Goswami 2004, 41). India’s exports consisted of raw cotton, opium, tea and indigo. During the American Civil War, raw cotton exports from India increased significantly and more than doubled between 1861/62 and 1865/66 (Harnetty 1971, 414).

In the eighteenth century, Britain had largely banned the import of textiles – also from India – with restrictive trade laws, e.g. the Calico Act of 1701, thus worsening the development prospects of the Indian textile industry (Nilekani 2009, 120). In the nineteenth century, British colonial masters extolled free trade, which was of course easy because the factories in the United Kingdom were the most competitive in the world. The consequences of the decline of the Indian textile industry were disastrous. Weavers who had become unemployed pushed into agriculture, creating an oversupply of labor and falling wages. The entire Indian economy was affected by rising imports from Great Britain.

\(^{19}\) Alan Beattie, Protectionists put brakes on trade liberalisation. Powerful domestic interests temper promises to embrace international deals. Financial Times, 19 December 2019, available at https://www.ft.com/content/c8a1e3fe-0bbb-11ea-8fb7-8fcec03b0f9.

For Mahatma Gandhi, the importation of clothes was akin to the subordination of the Indian people to the British colonial power. In 1921, Gandhi criticized the Indian dependence on Imports. Before the arrival of the East India Company, India manufactured all its cloth. That self-sufficiency was replaced with a dependence on imports, Gandhi argued (Trivedi 2007, p. xx).

The decline of the Indian textile industry was not compensated by other, new industries. On the eve of World War I, in 1913, industrial production accounted for 3.8% of India’s economic output. By the time of India’s independence in 1947, the share had grown to 7.5% of economic output, but the number of people employed in industry was a mere 2.5 million out of a total population at the time of 350 million (Tharoor 2016, 11).

The pandemic has been a catalyst for a renewed focus on trade policies that prioritize domestic production. Prime Minister Modi emphasized in May 2020 that India must emphasize self-sufficiency. He outlined a tension between globalization aimed at human needs and economic-centric globalization. India must prioritize human needs rather than economic profit, he said. Modi unveiled a campaign to strengthen India’s self-sufficiency – Atmanirbhar Bharat – in May 2020. Modi praised the virtues of an economic policy based on self-sufficiency and predicted an increase in “happiness, satisfaction and empowerment” as a result of the new economic policy.

At first glance, it seems as if the Modi government has simply discarded the reformist zeal of the early years and replaced it with a romanticized turn back to the trade and development policy concepts of the 1960s. Certainly, there are good reasons for not wanting to be dependent on foreign supplies of important medical products, for example. In India, however, geopolitical considerations help to explain the swing in trade policies. India was affected by a significant escalation of the conflict with the People’s Republic of China in 2020. So far, border conflicts in the Himalayas have cost only a few dozen lives. But against the backdrop of growing tensions, the Indian government has decided to no longer see China as a potential ally but as a competitor and to fight it on different levels. For the Indian government, the concept of decoupling from China has become more attractive. So far, mainly Chinese software providers have been affected by Delhi’s new policy. In the so-called digital attack, popular Chinese apps, including Tencent and Alibaba, were banned. In two batches, over 260 apps were excluded from the Indian market. Apple and Google had to remove the apps from their servers.

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22 Ibid.
But beyond the restricted trade in services, trade in goods has also been affected. In March 2020, the Indian government presented a package of industrial policy measures that created incentives for the production of selected goods. This “Production Linked Incentive” (PLI) supports the creation of national production networks for mobile phone technology, pharmaceuticals, cars, textiles, batteries, solar technology, steel and not to forget food.  

Prime Minister Modi decided in 2019 that India would not participate in the Regional Comprehensive Economic Partnership (RCEP) free trade area initiated by the ASEAN group. China’s participation was probably the most important reason for Delhi’s withdrawal. Foreign Minister Subrahmaniyam Jaishankar argued in November 2020 that India had in the past too often allowed itself to be swamped with products produced abroad and subsidised there. This policy of openness has been replaced by a policy of self-sufficiency.

Whilst the reduction of trade with geopolitical rivals is a plausible political goal, for a long time the Indian government found it also difficult to agree on trade liberalization with other, geopolitically innocuous actors such as Australia or Sri Lanka. The most important unanswered question, however, is the economic consequences of the love for autarky. Arvind Panagariya, former G-20 Sherpa of the Modi government, questions how the Indian government will achieve the self-imposed growth targets of 8 to 10% per year without reducing the level of protection of the Indian economy. To put it bluntly: It will be difficult for India to achieve the same growth effects in the domestic market, which is less than three trillion US dollars, as in the world market, which is about 30 times larger.

India’s turning away from the world market, however, may in the future be replaced by a gradual opening. In 2022, the Indian government has taken the offensive and is liberalizing the Indian economy with a strategy consisting of three components: infrastructure is being expanded, numerous free trade agreements are being pursued, and at the same time the government has introduced social policy measures to protect those who lose out to liberalization.

The new trade policy includes a number of trade agreements pursued by the Indian government. The agreement with Australia (Australia-India Comprehensive Economic Co-operation Agreement AI-CECA) came into force provisionally in April 2022. While the agreement has significant exceptions for trade in sugar, dairy and wheat, it is India’s first trade agreement in more than a decade. An agreement

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25 Mohamed Zeeshan: India’s rejection of free trade pact will make it poorer. South China Morning Post, 23 November 2020, p. 11.
with the former colonial power, the United Kingdom, is expected to be completed in 2023. The Indian government’s commerce secretary, BVR Subrahmanyam, said in mid-July 2022 that other agreements with Canada, the European Union, Israel and, in the medium term, the Free Trade Area of the African Continent are to follow.27

The sociopolitical flanking of liberalization is of particular importance, however. Only with a supporting welfare policy could the Indian government’s policies develop political sustainability. The government wants to cushion the disadvantages of liberalization measures with targeted sociopolitical aid. This point is particularly important in the world’s largest democracy. In the past, India’s voters have reacted very sensitively to the deterioration in their economic situation as a result of liberalization measures. The government has now installed a system that allows direct support payments to citizens who do not benefit directly from the opening of the country.

The increase in skepticism towards the People’s Republic of China that can be observed worldwide would offer the country the chance to develop more quickly. Right now, many companies are waiting for the country to open up and would probably also be willing to invest massively in India. If New Delhi wants to exclude Chinese suppliers, bilateral trade and investment agreements would be a way out. Both a free trade agreement with the European Union and with the United States would allow New Delhi to reduce economic ties with the PRC without giving up the benefits of the international division of labor. India’s search for its own approach to international trade and finance was becoming very clear in 2022 when the country refused to apply the sanctions of Western countries against Russia.

5 Sanctions as a Catalyst for Autarkic Thought and Policy Implications

Since February 2022, economic sanctions have been applied against Russia. The sanctions were imposed to punish Russia’s attack, which violated international law. The punishment of the Russian government and society continues to find much support in Germany, other European countries and the USA. Like in previous cases, the application of sanctions serves to demonstrate to domestic constituencies that protesting governments are willing to “do something” in order to protest against

the target’s behavior (Kaempfer and Lowenberg 2007, 870). Critics of the sanctions are regularly asked whether remaining inactive is an alternative. There is little discussion, however, about whether economic sanctions are a wise policy. The question of what happens if the sanctioned state does not end its war of aggression was and is given little space in the debates. This is negligent because the sanctions are having an effect, albeit quite different from what the sanctions advocates expected.

In economic history, economic sanctions and autarkic thought have reinforced each other. In his timely book, Nicholas Mulder has argued that the sanctions imposed on Germany and Austria-Hungary in World War I have contributed to the search for self-sufficiency in the 1930s (Mulder 2022, 11). The previous experience with sanctions contributed to the destruction of the existing economic order in the interwar period, which saw the collapse of the efforts to restore the Gold Standard after President Franklin D. Roosevelt rejected them during the London Monetary Conference of 1933 (Morrison 1993, 313).

Mulder suggests that many countries reacted to the worsening economic prospects by launching policies to reducing interdependence and thus trying to increase self-sufficiency (Mulder 2022, 9). Moreover, the continuing threat of sanctions destabilized international relations further. Economic sanctions thus did not stabilize international relations, but rather contributed to rising tensions. Mulder even suggests that Germany’s and Japan’s aggressive policies were intertwined with the threat of a renewed economic war:

“Conquest appeared as an avenue of escape from anxiety of living under the Damoclean sword of international blockade. Over time, the seeming inevitability of economic war prompted both Adolf Hitler and the Japanese leadership to secure resources by any means available. The internationalist search for more effective sanctions and the ultra-nationalist search for autarky thereby became locked in an escalatory spiral” (Mulder 2022, 11).

In the twenty-first century, sanctions most likely will not secure peace. Mulder does not expect that sanctions will persuade Russia to withdraw from Ukraine. However, today’s sanctions certainly have undesirable side effects: they may contribute to the formation of a Sino-Russian bloc. As in the 1930s, the world economy is thus breaking up into blocs that compete with each other politically. Today’s economic interdependencies are reduced by political measures, at least with outlawed countries. The militarization of international economic relations is a

dangerous fallacy that will lead to a continuing weakening of the international division of labor.

In addition, international finance is also affected. The question is whether today's inclusion of the financial sector in the sanctions is a convincing approach or whether earlier policies have been more plausible. Certainly, financial sanctions have been imposed on smaller economies time and again, but Russia is a much larger economy. But what are the medium-term consequences of financial sanctions?

For now, they are spurring the search for alternatives. CIPS, SWIFT’s Chinese competitor, saw a sharp increase in transactions from May to July.29 The longer sanctions are imposed, the more non-Western countries will find ways to process payments outside the Western financial system. The sanctions alliance undermines the foundation of the international division of labor and thus harms itself in the long run. Without a functioning financial system free of political interference, the emergence of an economic Iron Curtain (as former U.S. Treasury Secretary Hank Paulson put it back in 2018) will increase in an era of ongoing geopolitical tensions. The seizure of state and private assets by the governments of the sanctions alliance could stimulate comparable actions in the People’s Republic of China, for example.

A second effect of financial sanctions is that currency reserves become less attractive. There is a latent risk that these assets will be seized. Ironically, the globally observed increase in foreign exchange reserves is itself the result of inadequate structures. When the countries of Southeast and East Asia were caught in the maelstrom of the Asian crisis 25 years ago and faced bankruptcy, the U.S.-led International Monetary Fund failed. Its crisis policy exacerbated the crisis. The lesson learned by many countries was to strengthen their own resources by building up high foreign exchange reserves. South Korea, for example, has increased its foreign exchange reserves by more than 700% since 1998, China by 2100% and Russia by more than 4800%.30 In the future, reserves will increasingly be held in other forms, such as gold, cryptocurrencies, or possibly even emerging market government bonds. A reallocation of the currency reserves of non-Western countries will also make a further contribution to the rise of interest rates in OECD countries.

A third consequence of the financial sanctions is political: The financial sanctions affect all countries trading with Russia, but non-Western countries were not consulted or even asked for approval before the sanctions were imposed. In India, for example, this is causing continuing disgruntlement. Germany in particular, which always attaches great importance to multilateral cooperation, has not done itself any favors by allowing the sanctions alliance to go it alone. The British Guardian scoffed at the end of July 2022 that the sanctions were “based on the

30 World Bank data, foreign exchange reserves excluding gold in current U.S. dollars.
Third, and finally, the sanctions have consequences for international trade in goods and services. The former chief economist and current professor at Yale University, Pinelopi Goldberg, already pointed out in March that the trade sanctions harmed all states and were the final nail in the coffin for the rules-based international trade order (Goldberg 2022). The militarization of international trade in goods and services will cause economic harm around the globe and will impoverish hundreds of millions of people, who have neither committed anything worthwhile to be sanctioned for nor have they and their governments been agreeing to the actions of the Western alliance. Needless to mention, the sanctions also have severe effects on the civil society in the West and Russia, causing political, economic and social instability at a time where global action is urgently needed to secure sustainability goals. Cooperation, compromise and progress continue to be crucial to secure the benefits of the current system, which had promoted an international division of labor since 1945.

One would thus have thought that both state planning and autarkic thought have been sufficiently discredited. However, there is not only a return of “the bossy state”, but at the same a return of autarkic thought even in economies that have been benefitting from the international division of labor of the past decades. A particularly remarkable example of a politician who favors at least partial autarky is the German Minister for Economics, Robert Habeck. In early 2022, he surprised observers by referring several times to the supposed benefit of Germany's partial self-sufficiency. Both with regard to the import of raw materials and the financing of wind power farms, Habeck struck a new note. But if Habeck is determined to make Germany's economy less dependent on imports of raw materials, he could set in motion a dangerous spiral of escalation.

In addition, Habeck’s policies would constitute a break with previous economic policies. Over the past five decades, there had been a consensus across party lines in the Federal Republic of Germany on the benefits of the international division of labor. The German economy profits from the exchange of goods and services, but also from unrestricted capital flows. Habeck challenged this consensus: he described the “global hunger” for fossil energies, for natural gas, oil and coal, as the cause of

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31 Simon Jenkins, The rouble is soaring and Putin is stronger than ever – our sanctions have backfired. The Guardian, 29 July 2022.
32 The Economist, 15 January 2022.
the high level of energy prices even before the Russian invasion of Ukraine.\footnote{Protocol of the 11th Sitting of German Federal Parliament on 13 January 2022, available at Plenarprotokoll 20/11 (bundestag.de), see also Olk, Julian; Stratmann, Klau: Energiewende; Habecks Balanceakt, Handelsblatt, 14 Januar 2022, p. 14.} Habeck called for Germany to become less dependent on imports of raw materials.

On closer inspection, that policy has two decisive weaknesses. Firstly, an energy transition that relies on domestic raw materials cannot succeed. If today’s motor vehicles are to be replaced by electric vehicles, Germany will have to import large quantities of cobalt, for example. About 10 kg of the rare metal are needed per car battery. The current main suppliers are mines in the Democratic Republic of Congo, the majority of which are operated by Chinese companies. In view of the increasing demand for electric cars, the price for cobalt has already risen from around 42,000 US dollars per ton in June 2021 to about 80,000 US dollars per ton in April 2022. Since then, the price has fallen to about 50,000 US dollars per ton. The structure of Germany’s dependence on raw materials would be changed, but not reduced, at least in the short term. However, Daimler and Tesla are working on cobalt-free batteries, but their suitability for large-scale production has not yet been established.

Secondly, the statement by the German Minister of Economics of Europe’s largest economy on the disadvantages of imports is surprising. For decades, Germany has had a trade surplus, meaning that it sells more to foreign countries than it buys from them. For example, in the last year before the start of the pandemic, 2019, German companies exported goods worth around 1300 billion euros with imports of 1100 billion euros. This policy has been criticized for many years by Germany’s trading partners, the USA for example. The European Commission has also repeatedly demanded that Germany reduce its trade surplus, which corresponds to the deficits of other countries. A German Minister of Economics who wants to reduce (raw material) imports could provoke economic policy reactions in other countries: Why buy German industrial products if Germany attempts to buy less abroad? Habeck’s cautious striving for (energy policy) autarky opens a Pandora’s Box.

The renewed interest in a trade policy based on self-sufficiency in the USA, in the EU and in the two most populous countries in the world has different reasons. In both India and China, geopolitical tensions play a central role. At the same time, all large economies appear to be retreating from trade policy concepts that shaped the global economy for decades.

This development is problematic for Germany and other European economies. If China in particular succeeds with its strategy of local production, the best years of business in China are likely to be behind for German industry. The previous model, which provided Germany with high employment and sustained high trade surpluses,
would be put to the test. The German economy would have to reorient itself and rely more on European domestic demand.

Today, some voices are calling for Europe to strengthen its “strategic autonomy”. Voices are being raised calling for a campaign to buy European products. In addition, trade policy is expected to take into account the social situation in the countries of origin of imports and the effects of foreign production on climate change. The risk that this could entail a partial decoupling of the EU-27 from the world market is noteworthy. It would probably be particularly tragic for the developing countries of Africa if the EU were to rely heavily on self-sufficiency in the future. Gabriel Felbermayr, Director of the Australian Institute for Economic Research, fears above all that the EU’s bad example could find imitators.

Precisely because developing countries will be even more dependent on the EU as a sales market in the future, a reorganisation of European trade policy would be opportune anyway. In view of the economic damage caused by the Corona virus and the measures taken to contain it, especially in developing and emerging countries, the EU should liberalise its trade policy now. Both in the area of industrial goods and in agricultural trade, there is a wealth of options for reducing trade barriers. The European Union could formulate a balanced balance of trade as a trade policy goal. On the other hand, it would be inappropriate and misleading to counter protectionist developments in other economies with protectionism of our own.

References


34 Martin Sandbu: Sweden flies the flag for the free-trade cause in the EU. Financial Times, 9 February 2021.