Is free trade a solution to global poverty or a cause of it?

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Free trade advocates for the liberalization of any barriers to the flow of goods, generally through the elimination of quotas or special taxes on goods being brought into or out of a country. Through this, it aims to increase growth and ensure competitiveness, while providing consumers with a wide range of products. Proponents claim it has lifted more than 1 billion people out of poverty in the past 20 years,[1] and undeniably, free trade is a cornerstone of the globalized world we live in today, having played a key role in the rapid economic revolution of the past 150 years. It has made the average person wealthier and boosted technological development, yet at a high cost – contributing to growing inequality and exploitation. This essay argues that while free trade is an essential part of any effort to reduce global poverty, protectionist measures must also be considered by policy makers, if only to ease the difficult transition of industries into a more liberal system.

Promoting growth is perhaps the least challenged benefit of free trade. Evidence largely supports a strong correlation between increased openness to trade and an increase in GDP,[(a)] with one study finding that a 10% increase in trade openness corelates with a 4% increase in income per head.[2] This is unsurprising considering how liberalization incentivises domestic businesses to expand internationally, which in turn can often lead to increased production and GDP growth. The EU Single Market is a key example of this. Through the complete removal of any barriers to the transport of goods, capital and people between members[(b)] the single market has contributed to the value of trade between participants quintupling since it was signed in 1993.[3] This is why despite leaving the EU in 2019 the UK still pushed for a free trade deal with the Europe, ultimately with 2021's Trade and Cooperation Agreement, which ensured imports from the EU were still worth £454 billion in 2024, 51% of the UK's total.[4,(c)(d)] Britain is clearly dependent on the EU as a trading partner, and her government's post-Brexit actions strongly demonstrate this. Yet in the fast-evolving modern world, the significance of free trade is not merely limited to those who rely on a single nation or bloc as a market. World population is projected to increase by a further 2 billion in the next 40 years,[6] with this amplification centred on developing countries; potentially, economic growth may well be necessary for ensuring poverty rates continue to fall. A 2024 British International Investment report found that 'growth anywhere in an economy will reduce poverty if there are strong enough economic linkages to the livelihoods of people living in poverty', with this being especially true for industries in which significant productivity gains are feasible.[7,(e)] Besides leading to higher wages and consumption, such growth generally increases government income through taxes, which can be used to finance public infrastructure development and welfare. According to the same report, however, poverty rates can even be negatively impacted if growth is 'concentrated in sectors that predominantly benefit elites, without creating many jobs and with few spillovers to the rest of the economy'.[7] The OECD found similar results in 2014, warning that if low-income earners fall significantly below the rest of the population, further growth is extremely likely to merely exacerbate financial disparities.[8]

Angola, a country whose relatively undiversified economy is entirely centred around oil exportation, is a good example of this. Angola has a globally significant oil industry, consistently being one of the world's largest exporters, [(f)] and between 2001 and 2008, oil exports trebled as the country gradually recovered from the horrors of civil war[(g)], resulting in an average GDP growth of 11.1%.[9] Real GDP per head also more than doubled over the same period. However, poverty remains a huge problem in Angola; largely thanks to extensive corruption – the 5th worst in the world in 2015[10] - and the dominant oil and diamond industries proving very poor for job creation. In fact, $2.15/day extreme poverty reduced just 6% over the 2000s, while $6.85/day poverty even rose from 67% to 69%.[7] Free trade may have helped Angola's top industries become internationally competitive and allowed the country to consistently run impressive trade surpluses,[(h)] yet it has not had a significant impact on the lives of ordinary citizens. Angola is a clear example of the fact that while growth, and the free trade that creates it, may be an important condition for sustained reductions in poverty, it is no guarantee for any progress to occur. Poorly (or nefariously) run economies in which the divide between the highly productive industries and the population is too great – an unfortunately common occurrence in the developing world - can experience huge amounts of 'growth', without ordinary people even realising.

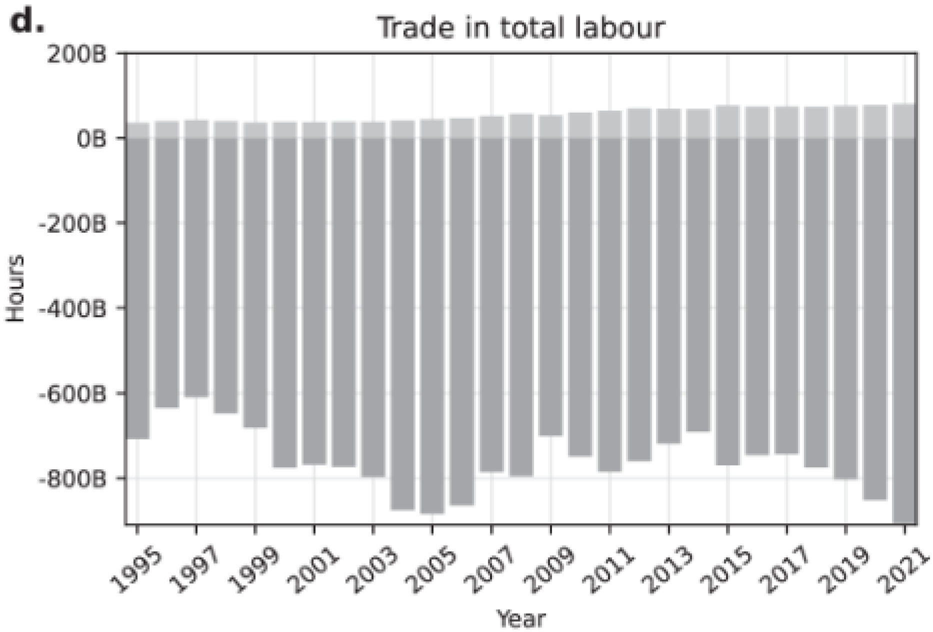
In tandem with this, free trade opens an economy to foreign direct investment, financing domestic business expansion and the building of new infrastructure. Most significantly, this happened in China following Deng Xiaoping's 'Reform and Opening up' programs of the 1970s. These introduced 'Special Economic Zones', in which entrepreneurship and FDI was encouraged – the landmark of China's transformation into a so-called socialist market economy. This largely took place through tax breaks – corporate tax is 24% lower in SEZs.[12] The SEZ program has seen incredible results, completing 225,000 joint ventures by 2003 and contributing on average 22% of China's GDP.[13] Encouraging foreign TNCs to invest in China has massively expanded the nation's now cutting-edge manufacturing and service industries, creating potentially millions of new jobs and kickstarting the largest urbanization in history. Just 38 million people lived in cities when the PRC was founded – by 2023, that number was 674 million. In addition, by stimulating private investment into housing, energy, and the production of consumer goods – all areas China's FDI-encouraging programs focused on - domestic consumers have access to a wider range of important products and services, potentially at a lower price due to increased competition[15]. That poverty has been reduced in China since its transition from a largely agrarian society to the 'factory of the world' is unequivocal: the extreme poverty rate,[(i)] fell from 66.2% in 1990 to just 0.1% in 2019,[16] with GDP per capita rising by a staggering 3100% in the same period.[17] China is history's most important example of the potential benefits of opening borders to foreign investment. When managed correctly, FDI can revolutionise labour markets while improving infrastructure and welfare, both indirectly and through tax revenues.

Trade liberalization is also likely to lead to increased competition, which has the potential to increase the quality and variety of goods and services available to consumers. Increasing the number of businesses offering a product reduces the risk of predatory price rises – something all too easy in restricted monopolistic or oligarchic economies – and ensures higher standards. Conversely, shielding businesses from competition only incentivises them to increase profit margins and reduce quality. Once again, history gives many examples of this, for instance Reichswerke, Nazi Germany's state-owned industrial conglomerate.[(j)] As Overy argues, the company's protection from foreign and domestic competition contributed to high levels of inefficiency. None of the pressures that push businesses in a free market towards optimal management structures or efficient distribution of resources applied, and as a result, Reichswerke continued to operate in a bloated manner.[18] While it can be true that in this regard a lack of free trade can be compensated for through sufficient domestic competition, in practice, this rarely if ever happens. Particularly in many developing countries, it is all too easy for a handful of companies to gain monopolies over the market and huge political influence alongside this. In South Africa, for example, less than a dozen businesses hold almost complete control across all industries and are notorious for using this power to set high barriers for international trade and control prices – many have profit margins more than 50% higher than their European counterparts.[19] Just this year Eskom, a South African electricity company with a

95% market control over domestic energy generation,[20] raised electricity tariffs to 12.74%, accompanied by an 88% fixed monthly charge for many citizens.[21] In many cases, it requires free trade, and consumer access to global markets, for proper competition to be ensured, which in turn should promote fairer prices and wages, along with goods that are better both in quality and production efficiency - a key step in the fight against poverty. Thus, free trade can be used as a tool to boost productivity and combat exploitative or inefficient business practices.

However, it is important to point out that obviously, free trade does not stop these practices or prevent semi-monopolies forming. American average tariff rates averaged only around 2% throughout the previous two decades,[22] and the country was a strong proponent of free trade,[(k)] yet partial or complete oligarchies are almost as significant there as in South Africa. According to Forbes, just 3 companies control more than 95% of credit cards,[23] while Google alone controls over 90% of internet searches[24] – despite there being almost 7,000 such engines available in the US. Clearly, large companies benefit from economies of scale and can easily use their financial advantages and global brands to undercut competition anyways. Once again, we see that while free trade is a useful tool, it can be quite a limited one, merely able to *encourage* competition, not enforce it.

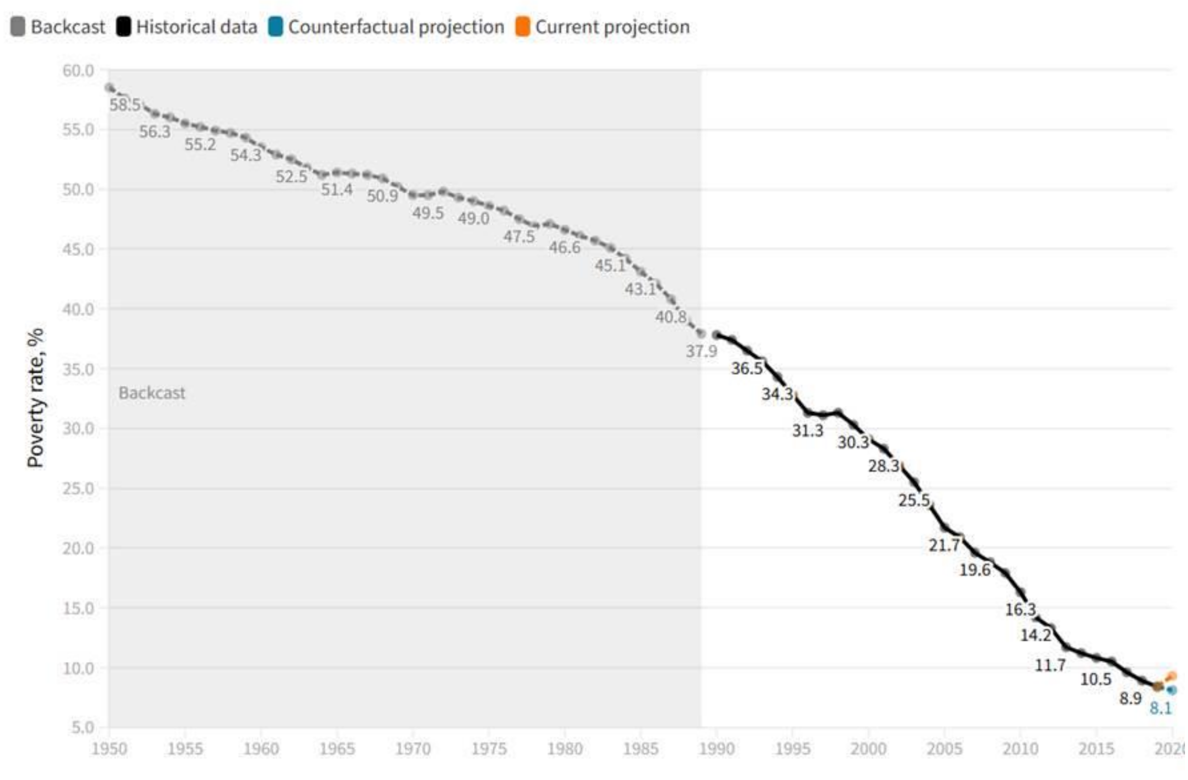
Facilitating foreign exploitation is another major risk of free trade. Trade rarely guarantees an equal exchange, and invariably, powerful economies use their financial or military superiority to sign highly one-sided deals. There have long been major concerns that predatory FTA's support a net resource and capital appropriation from the Global South to the North.[25] In 2021 alone, it was estimated that this amounted to 826,000,000,000 hours of labour (see chart), or €16,700,000,000,000 in wage terms.[26]



Generally, this is done through price and wage squeezes, which create large price inequalities between regions and forces the South into a constant net exportation of goods and labour to pay for artificially overpriced imports. The imposition of 'draconian' structural adjustment programmes (SAPs) across the global south in the late 1980s particularly shaped this unequal exchange,[26] compelling countries to open trade or cut government spending as a prerequisite for IMF loans – potentially forcing austerity or unwanted competition onto them. For those developing countries targeted by such reforms, trade liberalization is a dangerous risk in the short term. Underdeveloped industries can be swamped by their more advanced foreign competitors, resulting in declining domestic jobs and businesses.

List's Infant Industries Theory aims to provide a solution, arguing that protectionism must be used as a precursor to gradually-introduced liberalization, which allows key industries to grow before being exposed to international markets.[27] The USA followed such ideas during the late 1800s, becoming the world's foremost industrial power in the process.[28,(l)] While evidence suggests that this was an example of causal fallacy – it is generally agreed that the American economy grew in spite, not because, of tariffs - certain industries, such as iron, benefitted significantly from protectionism.[30,31] By 1910, the US produced 41% of the world's iron and steel[32]- almost double its nearest competitor. Granted, there are major critiques of the Infant Industries theory in practice, mostly it being extremely difficult to remove - protected businesses are unsurprisingly loath to relinquish their advantages. Yet it is once again clear that free trade's implementation is far from risk-free and must be managed carefully. Millions in developing countries continue to suffer from exploitative deals packaged as mutually beneficial liberal reforms.

Figure 2: Global extreme poverty, 1950-2020



Since 1990, alongside some of the most significant liberalization efforts in history, $2.15/day poverty has declined by almost 38%. The increases in productivity, investment and competition encouraged by free trade certainly outweigh the ever-increasing inequality and exploitation it has also contributed to – significant as those issues may be. Although ultimately a key piece in the difficult puzzle of reducing poverty, unfettered free trade on its own does not guarantee any major results. In many cases, the wider structural concerns in developing economies must also be addressed before eliminating global poverty is a feasible goal.

Footnotes

a. The aggregate value of all goods and services produced in a country per year, and the primary measure of growth
b. Members include all EU members and several other European countries such as Norway and Iceland
c. Perhaps surprisingly, a similar percentage to the early 2010s.
d. The alternatives looked grim, with the CEP estimating in 2016 that a complete severance of ties with the single market could cost the UK up to 9.5% of GDP by 2030 – more than £150 billion.[5]
e. Historically, growth in the agricultural industry has proven most significant in reducing poverty
f. A struggle between communist and anti-communist guerillas following 1975 liberation from Portuguese control
g. In fact, often the largest supplier of its biggest trading partner, China
h. $47 billion in 2012[11]
i. Defined by the World bank as the proportion of the population living on less than $1.90 a day
j. Employing up to 500,000 workers at its peak, Reichswerke was likely the largest company in the world at the time and was responsible for much of the raw mineral extraction which funded Germany's war effort [18]
k. At least before Trump's presidency
l. The aggregate value of US-produced goods increased from $5.4 billion in 1879 to $13 billion in 1899, while the number of industrial worker's doubled during the same period[29]

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