Chapter 17
State Interventionism in Foreign Trade:
A Response to Market Inefficiency

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ABSTRACT

The chapter refers to the literature to show how the state mitigates the effects of market failures in foreign trade through intervention in response to inefficient markets at national and international levels. The research study leads to several conclusions. Firstly, theoretical research focuses on the effects of market inefficiency on the domestic market, apart from the analysis of an international perspective, which implies that in the conditions of globalization there is a need for extended research in an international context. Secondly, state interventions are necessary in creating administrative and legal conditions for facilitating trade exchange in the context of the role of transnational corporations in the global economy, as well as in reducing the adverse impact of international turbulences on the competitiveness of national entities through the use of export supporting instruments.

INTRODUCTION

The concept of market mechanism inefficiency is not accepted by classical economic theory. Its founder, A. Smith, claimed that the market mechanism, incorrectly referred to as ”invisible hand”[1] (Rothschild, 1994), ensures self-regulation of prices, the volumes of goods and services as well as revenues, and that its efficient functioning relies exclusively on unrestrained activities.

However, the Great Depression highlighted the weaknesses of a free market economy, reminding economists about the inefficient market hypothesis developed by C. Launhardt (Ritzmann, 1983) at the end of the 19th century (also referred to as market inefficiency or market failures), as well as about mercantilists' postulates regarding the protection of markets against foreign competition and state support for industrialisation (Bochenek, 2010, p.72). Of course, it was just a starting point for further analyses and new proposals for counteracting negative phenomena. The recovery measures were proposed by Keynes,

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who recommended transforming the state into an active investing entity. Government programmes were to be treated not as permanent components of an economic system but temporary measures in those areas in which private enterprises were not inclined to engage. Such views were also accepted after the war, attributing to macroeconomic policies, referred to as adjustments, the ability to support market mechanisms[2] (Bochenek, 2010, p.73).

State interventions were also designed to support foreign trade activities. The views advocated by mercantilists were abandoned (at least officially), but protectionist activities have recurred in the recent years (Szymanik,2017c), which implies that entrepreneurs who operate in overseas markets require state intervention. Economic realities are trading conditions which are not created by a free market but international agreements, as well as by an increasing impact of international corporations which exert pressure on particular countries, resulting in the opposition of smaller market players who require state intervention.

The paper and its second part present a review of literatures to show the ways in which the state attempts to mitigate the effects of market inefficiency in foreign trade through interventions, thus responding to market failures at national and international levels.

A HISTORICAL OUTLINE

The concept of market inefficiency or market failures was introduced by a German researcher at the end of the 19th century. The opinion that markets were not able to cope with violent economic changes was to be justified by the Great Depression.

It is believed that the first macroeconomic analysis of market inefficiency is the 1936 publication of Keynes' *General Theory of Employment, Interest and Money*. The author identified the main causes of the phenomenon – inflation and unemployment. If such phenomena exist, it is necessary to identify the limitations of market mechanisms and seek solutions for mitigating the effects of market failures.

Interventionism had led to positive effects by the end of the 1960s. The first oil crisis of 1972 undermined the belief in the state's ability to eliminate or mitigate the effects of economic disturbances. Ultimately, the occurrence of stagflation and slumpflation led to the rebirth of neoliberal concepts. M. Friedman claims that all economists – monetarists, the followers of Keynes, and all the others recognise the existence of market inefficiency (Snowdown, Vane, Wynarczyk, 1998). Therefore, even his criticism of state intervention as a threat to individual freedom did not indicate the denial of the existence of market failures – it only implied the need for reducing the government's role, which was to lead to economic growth and stability. However, Keynes claimed that state interventionism could not be justified only by the necessity to correct market failures. Similar views were held by the representatives of the neoclassical school, advocating the state's conscious self-restraint in its economic activities. This view was rejected as unrealistic (Bochenek, 2010, p.74).

The advocates of the state's active role believe that interventions are necessary despite a number of ineffective government programmes. Because interventionism is a permanent characteristic of contemporary market economies (Markowski, 1992), correcting market mechanisms should be based on reasonable and effective economic policies (Leszek, 2010) rather than on the total rejection of such policies. Therefore, economic debates should focus on defining an appropriate scope of intervention for the benefit of markets – not on the issue whether markets are efficient or not.