

Consequently, even in industries where profit shifting is shown to be important, trade policies can only be justified if no other superior policies are feasible.

Sixth, adopting strategic trade policy would make the targeted high technology firm or industry expand by drawing resources from other industries in the economy. Resources and workers employed by high technology industries are generally limited even in advanced countries. Other industries must therefore contract, at least over the short term. Some of those other firms or industries may have excellent export prospects. In an economy wide sense, targeting specific industries can indirectly hurt other exports through the misallocation of resources. Some of these industries might also be oligopolistic and their strategic position will be worsened. The government authorities need to understand not only the targeted sector, but the rest of the economy to know if a policy is justified. Consequently, economy wide considerations radically increase the empirical difficulty of formulating interventionist trade policies and make it even more unlikely that these policies will do more good than harm.

Seventh, the political economy of strategic trade policy shows that the mechanism favours concentrated special interest groups in established industries and tends to ignore the dispersed groups of consumers and new emerging industries. Established industries may point to one niche or the other of their business as the "emerging" industry and lobby for protectionist or retaliatory trade policy measures. Special interests in one industry do not care if the rest of the economy is hurt. Therein lies the danger that trade policy may get captured by entrenched interests rather than promoting "winners".

Lastly, strategic trade policies are beggar-thy-neighbour policies. A country that attempts to use such policies will probably provoke retaliation. In many cases, a trade war between two interventionist governments will leave both countries worse off than if a hands-off approach were adopted by both.⁴⁶

In sum, the implementation of strategic trade policy imposes severe information requirements on policy makers and enforcement authorities. The way to avoid getting trapped in the above situations is to establish rules domestically and internationally. If such rules are

⁴⁶ For example, consider the case of the European telecommunications equipment industry, which can be targeted on the basis of criteria of externality and imperfect competition. It is a sector where nationalistic procurement by government owned firms allows countries to pursue protectionist policies without violating agreements on international trade. The result of such protectionist policies, however, is by most accounts harmful to all concerned. Each country tries to be largely self-sufficient in equipment. No country is able to realize the scale economies that would come from supplying the European market as a whole. The structure of the game between countries in telecommunications equipment is that of a prisoner's dilemma. Each country is better off intervening than being the only country not to intervene, but everyone would be better off if nobody intervened. See Paul R. Krugman, "Is Free Trade Passé?", *Economic Perspective*, Fall 1987: 131-44.