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Robinson and Friday Invent the Central American Common Market

There are many reasons why import costs rise and export income drops. Here we will comment on one of many phenomena that contribute to aggravating this scenario: the use of a common market's tariff policy to encourage industrialization.

First, it is important to emphasize something so obvious that it may go unnoticed. The very existence of demand for credit is irrefutable evidence of productive activities that are truly economic. In other words, activities with yields high enough to attract investment, even after capital costs. But what happens if capital ends up invested in activities that are in fact uneconomic, induced by an artificial yield guaranteed by tariff policy (or economic policy in general)? These investments will be carried out at the expense of true economically profitable activities, whose profitability is hindered by the tariff policy.

It goes without saying that this phenomenon affects not just imports and/or exports. It applies to the allotment of all resources and to every productive activity. However, here we will deal only with its effect on the balance of trade.

Nowadays, the market for almost any productive activity is guaranteed as long as it "adds value" or generates "employment," independent of whether it is truly economic.

Tariffs are levied to ward off importation of goods into Central America from other parts of the world, even though it would be less expensive to import them. This forces us to produce and import these goods from within Central America at higher prices. For example, you can import a product from Europe or the U.S. that costs Q50 per ton. But—presto!—it is made in a Central American country and the price rises to Q100 per ton. All of a sudden it turns out that, although you still import the same amount of product (now made in Central America), the cost increases 100%. You could argue that this price increase for imports is automatically compensated because exports from the respective countries also rise. This is only true, though, as long as what they produce and export is equally uneconomic.

Even if export and import accounts were balanced, the situation would be absurd. Imagine, for example, two businessmen: Robinson who lives in Honduras, and Friday who lives in Guatemala. Their exchange might go something like this:

Robinson: Listen, you import 50 tons of Yeye from Germany at Q120 per ton, and I'm importing 100 tons of Gogo from Japan at Q60 per ton. It occurs to me that it would be good business to set up a factory to produce Yeye; but, for the business to work for me, I'll sell it to you at Q200 per ton.

Friday: What are you trying to do, my friend Robinson, put me out of business?

Robinson: Don't worry, amigo. You'll set up a factory to produce Gogo and sell it to me at Q100. That way, what you lose when you buy, you get back when you sell.

Friday: I'm not convinced. What would we have gained?

Robinson: Don't interrupt me. What's more, it occurs to me that I've discovered the formula to make my fellow citizens rich. If we generalize the procedure, we can have a closed market without competition from outsiders. The wealth will stay at home; we can create many jobs and increase the purchasing power of the entire population.

Friday: But, can't you see that if the two of us buy raw material from each other at twice the price, the costs for both of us will increase; unless the increase is exclusively profit, in which case it's pointless for both of us to raise our prices.

Robinson: That doesn't matter, because what you lose in the purchase, you gain in the sale.

Friday: And who pays for these higher costs?

Robinson: You know . . . to have a common market, the consumer has to make some sacrifices. But he benefits in the long run, so it's fair to raise import tariffs so we can raise our prices.

Friday: Didn't you say that your formula will increase consumers' purchasing power? How are you going to increase their purchasing power by raising prices?

Robinson: Don't be so closed-minded! When you generalize the procedure, the number of jobs will go up and there will be more consumers.

Friday: But, don't you realize, Robinson, that those factories and jobs will be created by diverting capital resources and labor away from other activities?

Robinson: From which ones?

Friday: From others!

Robinson: Too vague! You can't even give me one single example!

Friday: As long as there's demand for capital, even though *I* may not know what other specific activity will be carried out, those searching for capital *do* know. There are so many things we need.

Robinson: Since you don't have any arguments, I'd like to offer you more support for my terrific idea. Let's go back to my example. It's easy to see that, besides increasing everyone's exports, gross national product also rises.

Friday: Please, don't insult my intelligence!

Robinson: Don't misunderstand me, dear friend. I'm referring to the "Gross National Product" index used to measure a country's wealth. It's obvious that every ton of Yeye produced in Central America will increase GNP by Q80, and every ton of Gogo will increase it by Q40.

Friday: I don't understand! The amounts of Gogo and Yeye won't increase. We'll have the same amount, so we won't be any wealthier!

Robinson: That's the problem with you empiricists! If you had studied economics, you'd know that wealth is measured according to GNP.

Friday: Pardon my ignorance, Robi. I thought that the more things we had, even if their price was less, the richer we'd be. Economic science really is difficult! I can't begin to comprehend how it is that the more we lose, the wealthier we'll be. I don't understand how we're going to be wealthier if we buy everything from each other at a higher price. I don't see how, if you take purchasing power away from the population, we're going to have more jobs. I don't understand how we're going to be better off by investing in uneconomic activities and sacrificing profitable ones. And, finally, I don't see how we're going to avoid an unfavorable trade balance if you lower the real productivity of the entire economy.

Robinson: Can't you see that when we produce within the Yeye and Gogo region, then we lower imports for the region?

Friday: No, I don't see it. When you substitute an imported product with local production, you're forced to utilize part of our scarce resources to produce it. If this production is uneconomic, you not only lose this difference in cost, but also the economic yield those resources would have produced had they been well employed. The loss is multiplied. What's more, given that the entire country loses domestic purchasing power, the volume of other activities also drops. This *lowers* the productivity of our entire economic system. Our purchasing power drops, and with it our standard of living. As soon as our industries become less competitive, foreign products become relatively cheaper, this tends to increase imports.

Robinson: You can deal with that by raising the tariffs on anything else that's imported!

Friday: That will raise the cost of imports even more because, instead of importing cheaper things from outside our region, we'll import them at higher prices from C.A. In the end, we'll be poorer!

Robinson: Even if you're right, Friday my friend, we're not going to pay any attention to you, because it's better to be poor than to depend on foreigners. We'll be poorer, but our poverty will be national! And if we don't follow this path to industrialization, we'll turn into a country of buyers.

Friday: That, I really don't understand. Please explain.

Robinson: If we don't protect our production, industrialized countries will flood us with their cheaper goods. I repeat, we'll become a country of buyers!

Friday: But if we just buy and don't sell, what are we going to use to pay for our purchases? I don't imagine they're going to give them away to us. If that were the case, all the more reason not to produce them locally. I suspect we'll have to give them something produced here in exchange. Unless you sell some thing or service, you can't become a "purchaser." That's obvious.

Robinson: Of course. But as you know, the prices we get for our agricultural products are dropping lower and lower, while the prices of what we buy are going up and up.

Friday: So, who understands this mess!

Robinson: Why don't you study economics?

Friday: Let's get this straight, once and for all! You just told me that we're being flooded with cheap things—which keeps us from industrializing. Therefore, it's false that prices abroad are very high. It can't be that prices abroad are high and low at the same time. What's more, if we receive poor payment for our products and pay a lot for theirs, we'll be able to buy less and less from them. That means that every day our local manufacturers will have less competition and our industries will flourish.

Robinson: You finally came up with something constructive!

Friday: I think we'd better have another drink and talk about the problem in Vietnam.

Translated from the original Spanish
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