Chapter 9 (Salvatore)

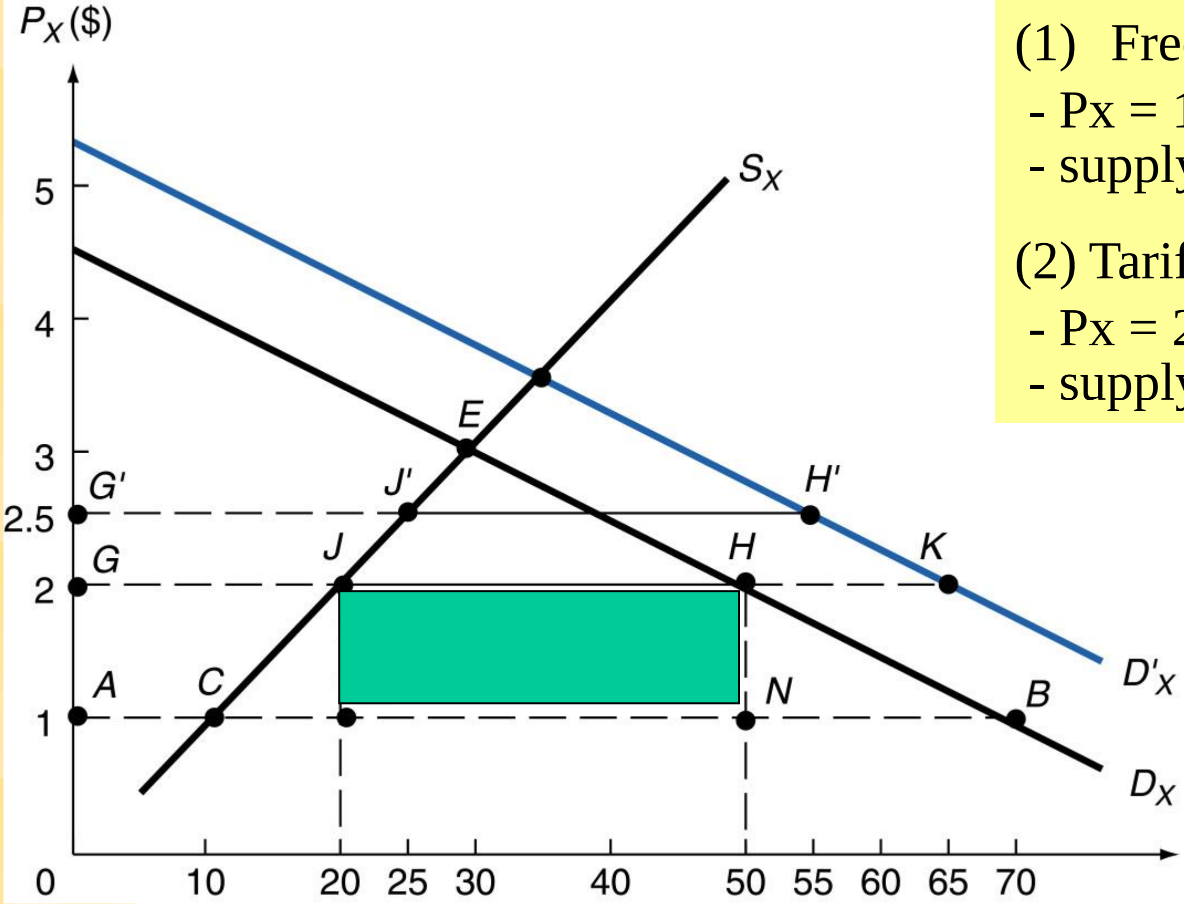
- Nontariff barriers (NTBs):
- Definitions: trade barriers other than tariffs
- Types: import quotas, voluntary export restraints (VERs), anti-dumping duties, export subsidies, technical, administrative and other regulations, etc.
- New protectionism: The recent trend of protectionism which uses more of nontariff barriers such as VERs, antidumping duties, etc.

9.2 Import Quotas

9.2A. Effects of an Import Quota

- Quota: Direct quantitative restriction on the amount of a commodity allowed to be imported or exported.
- Import quota vs. export quota

9.2 Import Quotas – Simple I.Q.



(1) Free trade
- Px = 1$ - demand : 70X
- supply : 10X - import : 60X

(2) Tariff : 100% (1$→2$)
- Px = 2$ - demand : 50X
- supply : 20X - import : 30X

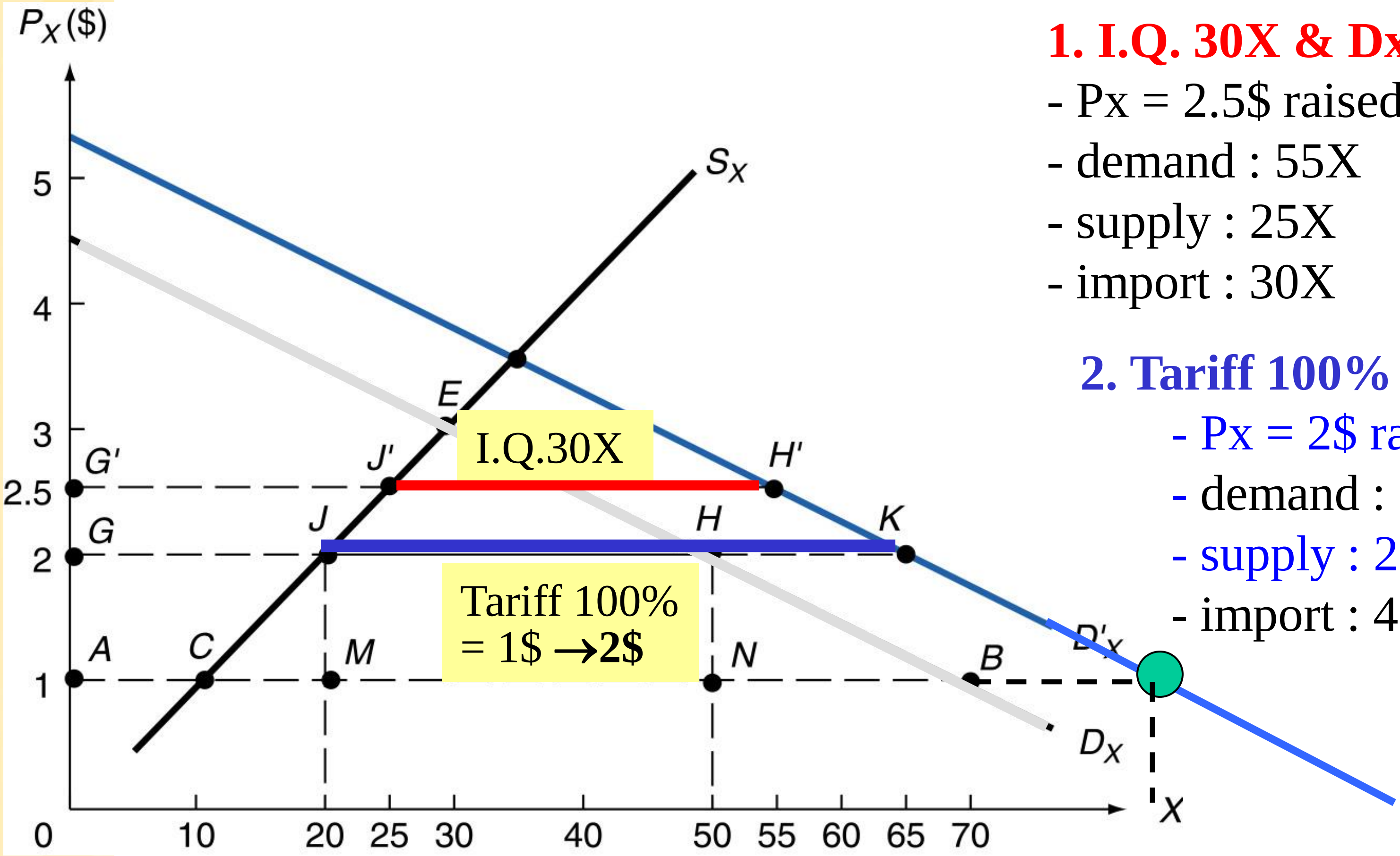
(3) Import Quota : 30X

- Px = 2$ raised
- demand : 50X
- supply : 20X
- import : 30X

Tariff 100% = I.Q. 30X
Govt. Revenue = bidder

FIGURE 9-1 Partial Equilibrium Effects of an Import Quota.

9.2 Import Quotas – Raised Demand

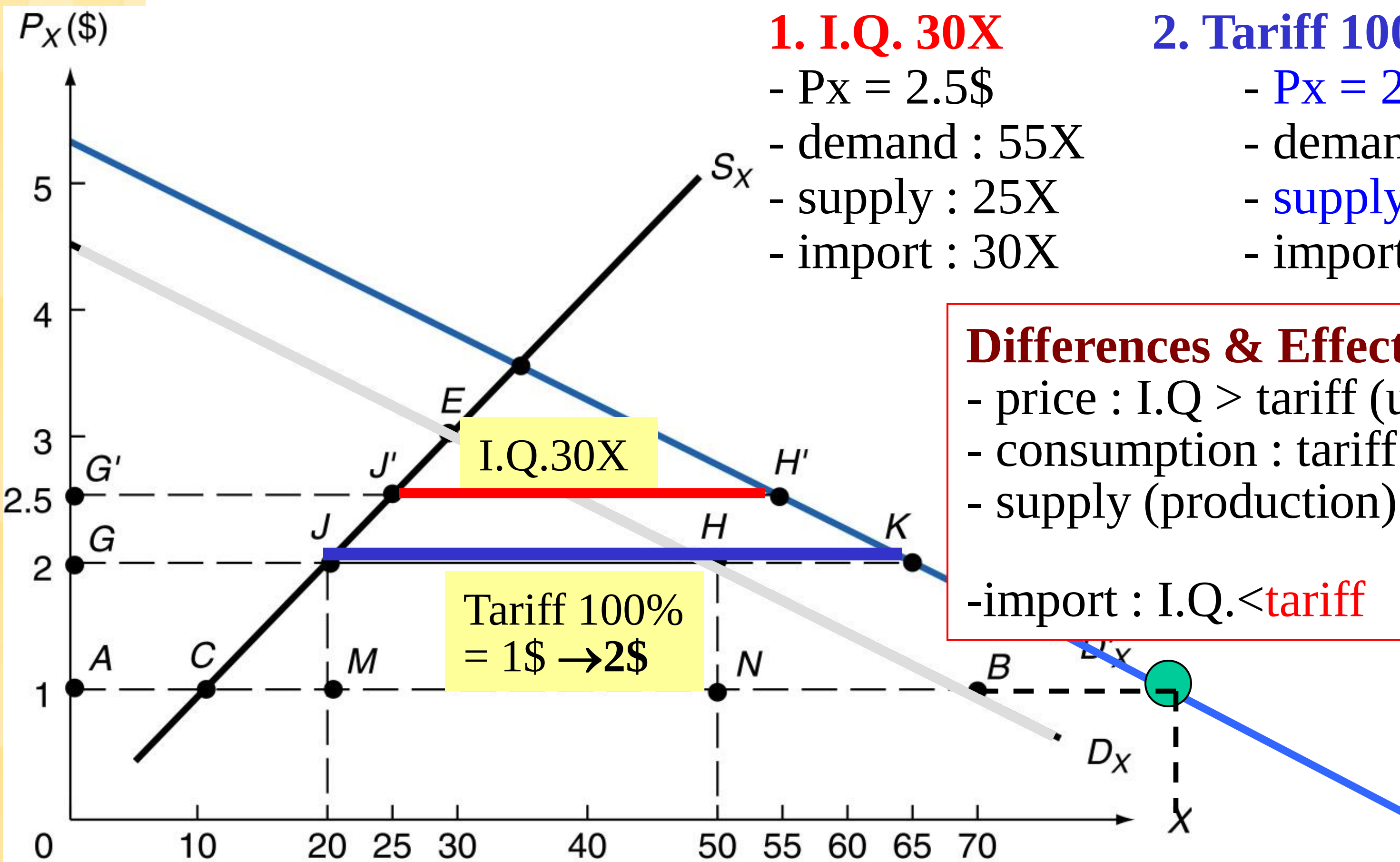


1. I.Q. 30X & Dx →D´x
- Px = 2.5$ raised
- demand : 55X
- supply : 25X
- import : 30X

2. Tariff 100% & Dx →D´x
- Px = 2$ raised
- demand : 65X
- supply : 20X
- import : 45X

FIGURE 9-1 Partial Equilibrium Effects of an Import Quota.

9.2 Import Quotas – Raised Demand



1. I.Q. 30X
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2. Tariff 100%
- Px = 2$
- demand : 65X
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Differences & Effects
- price : I.Q > tariff (unchanged)
- consumption : tariff : I.Q.<tariff
- supply (production) : I.Q > tariff (unchanged)
-import : I.Q.<tariff

FIGURE 9-1 Partial Equilibrium Effects of an Import Quota.

9.2 Import Quotas

9.2B. Comparison of an Import Quota to an Import Tariff

(1) Effects of an increase in domestic demand

- Tariff: an increase in demand will leave the domestic price and domestic production unchanged, but will result in higher consumption and imports.
- Quota: an increase in demand will leave imports unchanged, but will result in a higher domestic price and greater domestic production.

(2) Revenue effect

- Tariff: the government will receive tax revenue.
- Quota: Revenue goes to the licensed firms unless licenses are auctioned off in a competitive market.

(3) Trade effect

- Tariff: the trade effect may be uncertain.
- Quota: the trade effect is certain. It limits imports to the specified level with certainty.

9.3 Other Nontariff Barriers and the New Protectionism

9.3A. Voluntary Export Restraints (VERs)

- The case where an importing country induces another nation to reduce its exports of a commodity “voluntarily,” under the threat of higher all-round trade restrictions.

- “Orderly market arrangements”

-Effects of VERs: they have all the economic effects of equivalent import quotas, except that the revenue effect or rents are captured by foreign exporters.

- Less effective in limiting imports than import quotas because the exporting nations agree only reluctantly to curb their export.

9.3 Other Nontariff Barriers and the New Protectionism

9.3B. Technical, Administrative, and Other Regulations

- Safety regulations & Health regulations
- Labeling requirements
- Government procurement policies
- International commodity agreements & Multiple exchange rates

9.3C. International Cartels

- International cartel: an organization of suppliers of commodity located in different nations that agrees to restrict output and exports of the commodity with the aim of maximizing or increasing the total profits of the organizations.
- e.g., OPEC (Organization of Petroleum Exporting Countries)

9.3 Other Nontariff Barriers and the New Protectionism

9.3D Dumping and Antidumping duties

- **Dumping**: the export of a commodity at below cost or at least the sale of a commodity at a lower price abroad than domestically.

  1) **Persistent dumping**: the *continuous* tendency of a domestic monopolist to maximize total profits by selling the commodity at a higher price in the domestic market than internationally (where it must meet the competition of foreign producers).
  2) **Predatory dumping**: the *temporary* sale of a commodity at below cost or at a lower price abroad in order to drive foreign producers out of business, after which prices are raised to take advantage of the newly acquired monopoly power abroad.
  3) **Sporadic dumping**: the *occasional* sale of a commodity at below cost or at a lower price abroad in order to unload an unforeseen and temporary surplus of the commodity without having to reduce domestic prices.

9.3 Other Nontariff Barriers and the New Protectionism

9.3D Dumping and Antidumping duties

- Trade restrictions to counteract *predatory dumping* are justified and allowed to protect domestic from unfair competition from abroad.
- These restrictions usually take the form of antidumping duties to offset price differentials, or the threat to impose such duties.
- However, it is often difficult to determine the type of dumping, and domestic producers invariably demand protection against any form of dumping.

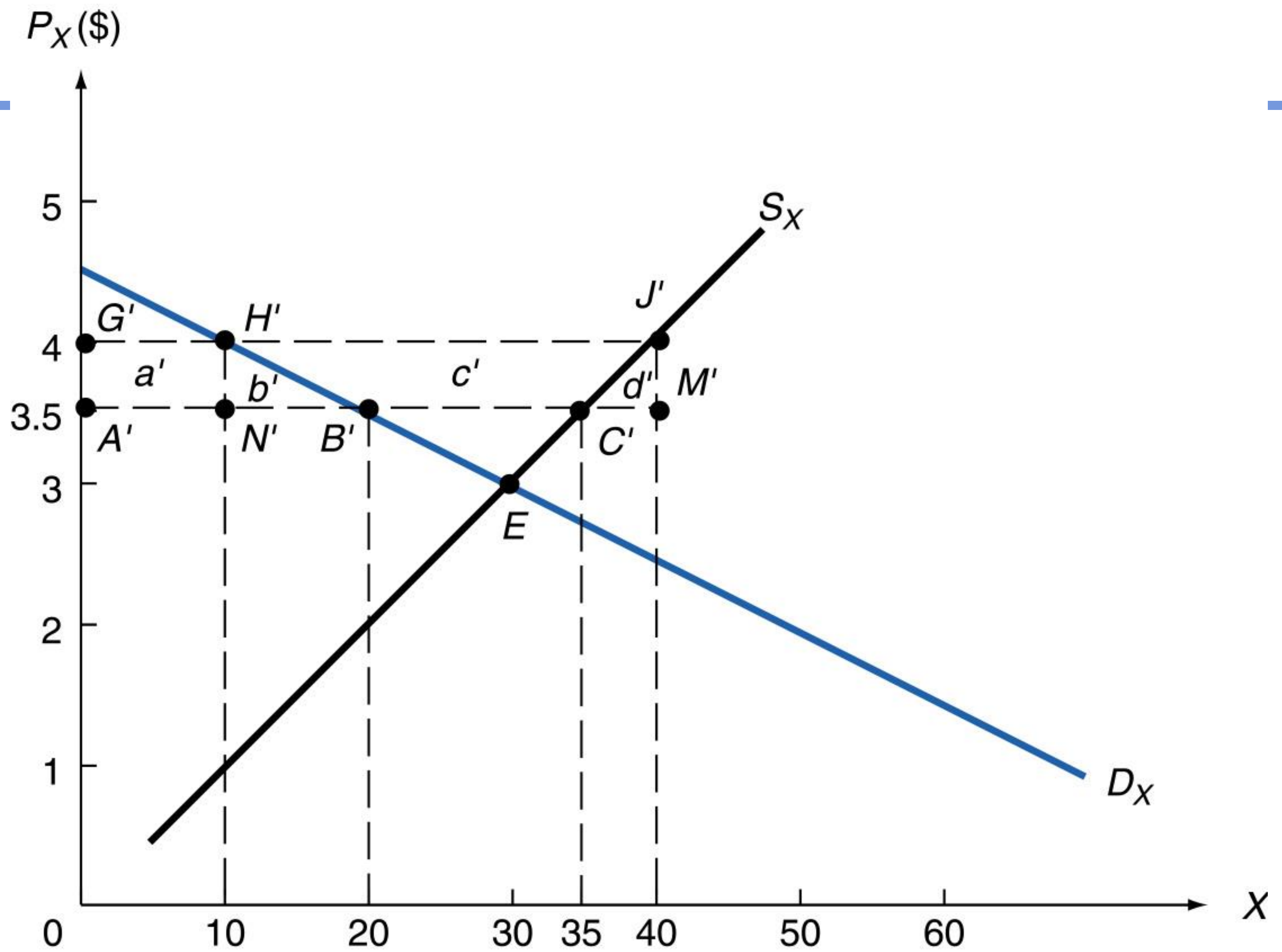

FIGURE 9-2 Partial Equilibrium Effect of an Export Subsidy.

9.4 The Political Economy of Protection

9.4A. Fallacious and Questionable Arguments for Protection

(1) Argument: Trade restrictions are needed to protect domestic labor against cheap foreign labor.

- This argument is fallacious because …………..

(2) Argument: A tariff needs to be imposed to make the price of imports equal to domestic prices and allow domestic producers to meet foreign competition. (This tariff is called the scientific tariff.)

- This argument is fallacious because …………….

(3) Argument: Protection is needed to reduce domestic unemployment.

- This argument is questionable because …………..

(4) Argument: Protection is needed to cure a deficit in the nation's balance of payments.

- This argument is questionable because …….

9.4 The Political Economy of Protection

9.4B. The Infant-Industry and Other Qualified Arguments for Protection

- **Argument:** A nation may have a potential comparative advantage in a commodity, but because of lack of know-how and the initial small level of output, the industry will not be able to set up or, if already started, cannot compete successfully with more established foreign firms. Temporary trade protection is then justified to establish and protect the domestic industry during its "infancy" until it can meet foreign competition, achieve economies of scale, and reflect the nation's long-run comparative advantage.

9.4 The Political Economy of Protection

9.4B. The Infant-Industry and Other Qualified Arguments for Protection

- **Qualifications**

1) This argument is more justified for developing nations than for industrial nations.
2) It may be difficult to identify which industry or potential industry qualifies for this treatment. (It is very difficult to choose the industries that will provide large external economies in the future.)
3) Protection, once given, is difficult to remove. (The protected domestic firms are likely to devote a great deal of effort to lobbying and even bribing government officials to keep the protection.)
4) What trade protection can do, an equivalent production subsidy can do better.

9.4 The Political Economy of Protection

9.4C. Who Gets Protected?

- By increasing the commodity price, trade protection benefits producers and harms consumers.
- However, since producers are few and stand to gain a great deal from protection, they have a strong incentive to lobby the government to adopt protectionist measures.
- On the other hand, since the losses are diffused among many consumers, each of whom loses very little from the protection, they are not likely to effectively organize to resist protectionist measures.

9.5 Strategic Trade and Industrial Policies

9.5A. Strategic Trade Policy

- **Argument:** A nation can create a comparative advantage (through temporary trade protection, subsidies, tax benefits, and cooperative government-industry programs) in the high-tech industries, which are subject to high risks, require large-scale production to achieve economies of scale, and give rise to extensive external economies when successful.
- E.g., (1) steel industry in the 1950s and in semiconductors in the 1970s and 1980s in Japan.

9.5 Strategic Trade and Industrial Policies

9.5A. Strategic Trade Policy

- **Qualifications**

1) It is extremely difficult to pick winners (i.e., choose the industries that will provide large external economies in the future.)
2) Since most leading nations undertake strategic trade policies at the same time, their efforts are largely neutralized, so that the potential benefits to each may be small.
3) When a country does achieve substantial success with strategic trade policy, this comes at the expense of other countries (i.e., it is a beggar-thy-neighbor policy) and so other countries are likely to retaliate.