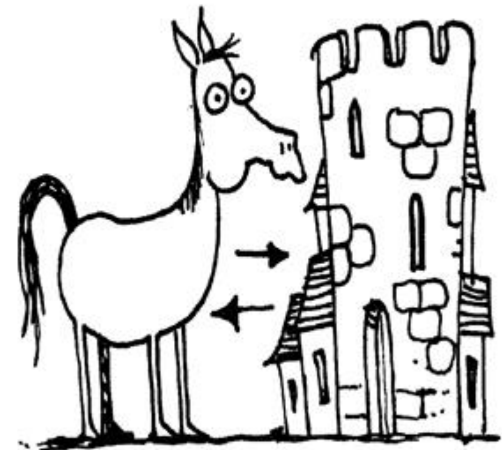
INTERNATIONAL TRADE

What is International Trade?

- International trade is the exchange of goods and services between countries.
- This type of trade gives rise to a world economy, in which prices, or supply and demand, affect and are affected by global events.
- IT gives consumers and countries an opportunity to be exposed to goods and services not available in their own countries.



Sometimes you can trade a horse for a kingdom.

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Why International Trade?

- By virtue of International Trade consumers gets an opportunity to consume a large variety of goods produced by different countries. This improves the quality of life.
- International trade enables every country to dispose off their surplus production. Some countries produce more than their own requirement. They sell this surplus production in other countries and avoid the occurrence of deflationary pressures in the domestic economy.
- It widens the extent of market. Every country makes an attempt to produce different goods in large quantity. This induces production on large scale and thereby generates economies of scale.
- International Trade stimulates the spirit of competition among the entrepreneurs. Novel techniques of production are devised to produce quality goods at low cost. Advancement of technology is the key to economic development.
- International Trade promotes mutual cooperation among different countries. It creates an atmosphere of goodwill and friendship among the trading countries.

Summary: The Welfare Effects of Trade

	PD < PW	PD > PW
Direction of Trade	Exports	Imports
Consumer Surplus	Falls	Rises
Producer Surplus	Rises	Falls
Total Surplus	Rises	Rises

Whether a good is imported or exported, trade creates winners and losers.
But the gains exceed the losses.

Restrictions on International Trade

- **Unemployment**

Trade destroys jobs in the industries that compete against imports.

- **National Security**

An industry vital to national security should be protected from foreign competition, to prevent dependence on imports that could be disrupted during wartime

- **Infant Industry**

A new industry argues for temporary protection until it is mature and can compete with foreign firms.

- **Unfair Competition**

Producers argue their competitors in another country have an unfair advantage, e.g. due to Govt subsidies.

- **The protection-as-bargaining-chip argument**

Example: The U.S. can threaten to limit imports of French wine unless France lifts their quotas on American beef.

Tariff: An Example of a Trade Restriction

- A tariff is a tax on imports or exports. Money collected under a tariff is called a duty or customs duty. Tariffs are used by governments to generate revenue or to protect domestic industries from competition.
- There are generally two types of tariffs. **Ad valorem tariffs** are calculated as a **fixed percentage of the value of the imported good.** When the international price of a good rises or falls, so does the tariff. A **specific tariff** is a **fixed amount of money that does not vary with the price of the good.** In some cases, both the ad valorem and specific tariffs are levied on the same product.
- For example, Company XYZ produces cheese in Scotland and exports the cheese, which costs $100 per pound, to the United States. A 20% ad valorem tariff would require Company XYZ to pay the U.S. government $20 to export the cheese. A specific tax would involve charging $30 dollars per pound of cheese whether cheese sold for $100 or $200 per pound.

Is it good or bad?

- Import and export taxes make it more expensive for users of foreign goods, causing a decline in imports, a decline in the supply of the good, and a resulting increase in the price of the good. The price increase usually motivates domestic producers to increase their output of the product. Some economists argue that the resulting higher consumer prices, higher producer revenues and profits, and higher government revenues make **tariffs a way to effectively transfer money from consumers to government treasuries**.

- Some economists also argue that **tariffs interfere with free market ideals** by diverting resources to domestic industries that are less efficient than foreign producers.

Import Quotas: Another Way to Restrict Trade

- An import quota is a quantitative limit on imports of a good.
- Mostly has the same effects as a tariff:
  1. Raises price, reduces quantity of imports.
  2. Reduces buyers' welfare.
  3. Increases sellers' welfare.
- A tariff creates revenue for the Govt. A quota creates profits for the foreign producers of the imported goods, who can sell them at higher price.
- Or, Govt could auction licenses to import to capture this profit as revenue. Usually it does not.

US – China Trade War

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- US imposed 25% tariffs on $34 billion of Chinese imports in July and $16 billion in August. To which China reciprocated with tariffs on $50 billion of goods. This is known as **Retaliatory Tariffs**
- It further imposed an extra 10% tariffs on $200 billion worth of Chinese imports.
- If all planned tariffs go into effect, US imports from China will fall by nearly $70 billion, which would amount to 14% of the imports from China.

Impact on Various Stakeholders

- 10% increase in tariffs on imported goods would cost the poorest 20% of earners in the US, whose average earning is $13,000, $300 a year.
- In China, official PMI fell to 50.2 in October, the lowest since July 2016 and down from 50.8 in September.
- Even if 25% tariffs were to be imposed on all the US imports from China, that will only reduce Chinese growth by 0.5%.
- Investment across borders is likely to get impacted, which will impact Indian Economy as well.

Thank You!!