

Topics in International Trade

- WTO (Chapter 8-sec 1, Chapter 10-sec 1, and lecture notes)
- Anti-Dumping duties (Chapter 9, section 4 including application)
- Export subsidies (Chapter 10, sections 1, 2, 3. All applications and headlines included)
- Agricultural Production Subsidies (Chapter 10, section 4. All applications and headlines included)

Historical Perspective

- Need for global institutions arose out of wars
- 19th century: world dominated by a few countries, industrialization spreading
- Colonialism still important – Germany's attempt to get some colonies one of causes of WWI
- After WW I (1914-18) – some attempt to create global institutions
 - US isolationist
 - France, UK disagree
 - Germany outsider
 - Attempt fails
- Between wars – world depression.
 - Growing interdependence
- After WW II, US takes lead
 - Cold war – need to win allies
 - Rise of outward oriented industries – aircraft, shipbuilding
 - Dollar is world currency
- Reasoning: International economy viewed as one of reasons for war

- **Post-war Period**
- *1950-70: golden era of the “Bretton Woods” system*
 - 1950-70 annual GNP growth
 - Europe 4.6%
 - US 3.7%
 - Japan 10%
 - Growth of international trade 9% per year
- *Harder times from 80’s onwards*
 - relative decline of US and UK
 - other strong economies
 - Germany, Japan, France, etc
 - more countries 1950-1990
 - decolonization 1948-1965
 - China opens 1978
 - 1990's Russia, etc
 - More issues 1980-2000+
 - increase in world trade, capital flows
 - services, agriculture, investment
 - development, democracy, environment, etc

GATT/WTO

- GATT 1947-1994
 - 23 members originally, 110 at end
 - Uruguay round - GATT becomes WTO
- WTO 1995-
 - now 146 members and 20 applicants
 - unified GATT agreements
 - continuation and strengthening of GATT
 - permanent organization
 - extended GATT to other areas e.g. Services
- Objectives
 - substantial reductions in trade barriers
 - elimination of discrimination in trade policy

- Tools

- MFN: most favored nation status – advantages to one apply to all
- National treatment: treat import like domestic goods
- Tariff Binding: can not raise, once lowered

- How? Rounds of negotiation

- Kennedy round 1964-7, very large tariff cuts
- Tokyo round 1973-79, attacking non-tariff barriers
- Uruguay round – 1986-1993 – WTO born
- Doha round – going on right now, need to tackle agricultural quotas in D.C.s, contentious issue

- WTO
 - Follows basic principles of GATT
 - One country, one vote
 - Permanent organization but weak – little enforcement power
 - Dispute settlement: 3 judges, 20 months for decisions, allows retaliation by winner

- Additional Provisions
 - Bans VERs
 - Safeguard clause: allows stronger justification for escape clauses
 - Anti-dumping punitive tariffs allowed
 - Allows regional trade agreements

- Aims and Results of WTO
 - Trade liberalization
 - Agriculture
 - banning quotas (convert to tariffs)
 - reduction in tariffs
 - reducing subsidies
 - Textiles
 - phasing out of quotas
 - reductions of tariffs
- "tariff-bindings" now apply to 99% of imports
- GATS General Agreement on Trade in Services
 - service trade previously not covered by GATT
 - GATT-type rules now apply to services
- TRIPS - trade-related aspects of intellectual property
 - obligations for protection and enforcement of intellectual property rules (patents, copyright, etc)
 - forces countries to use domestic sanctions
 - WTO handles violations

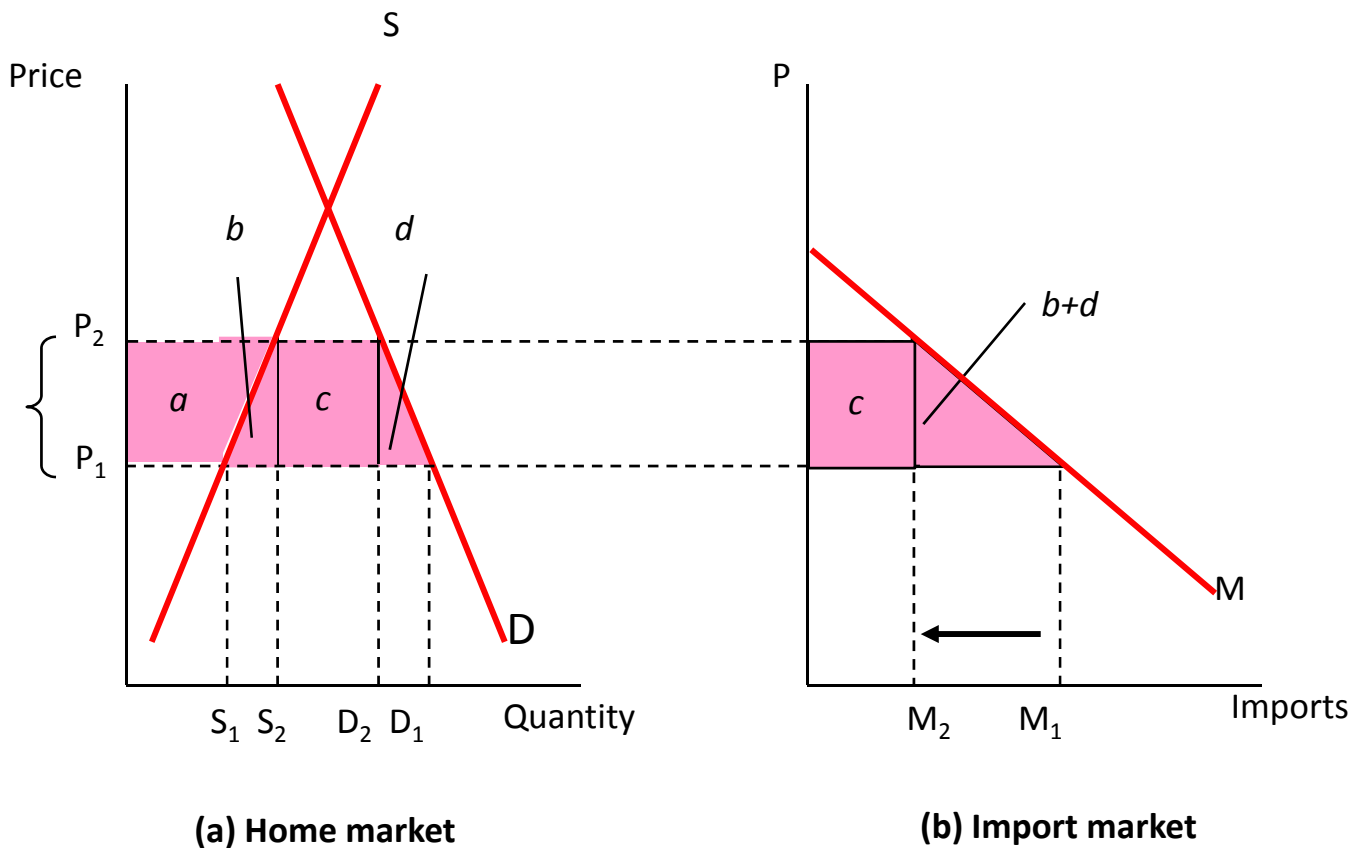
- Critique of WTO
- Success
 - huge growth in world trade
 - increasing membership
 - absence of trade wars
- Criticism
 - National sovereignty loss
 - Domination by richer countries
 - Need for stronger enforcement
 - No progress on agriculture: single most important economic way to help poor countries
- Status: Deadlock in Doha Round
 - Cancun meeting (Sept 2003): walk out by developing countries (G21)
 - Main issue: removal of agricultural subsidies and quotas
 - G21 against US/EU, EU against US

- **Since then.....**
- Geneva 2004: *Talks achieved framework agreement. US, EU, Japan, Brazil agree to lower/end export subsidies, reduce agricultural subsidies. Developing countries agree to lower manufacturing tariffs.*
- Paris 2005: *France protests moves to cut subsidies to farmers. The U.S., Australia, the EU, Brazil and India fail to agree on issues relating to chicken, beef and rice.*
- Hong Kong 2005: *6th WTO Ministerial Conference. Deal that sets a deadline for eliminating subsidies of agricultural exports by 2013. Fresh impetus for negotiators to try to finish a comprehensive set of global free trade rules by the end of 2006.*
- Geneva 2006: *Failure to reach agreement on reducing farm subsidies and lowering import taxes.*
- Another complication: *Fast track authority to Pres. Bush expired in 2007. After that any trade pact will have to go through the Congress with possibility of amendments. Reduces US bargaining power, reduces other countries willingness to participate.*

Anti-Dumping Clause and its uses

- Dumping = when firm is exporting goods at a price that is below the price in its local market, or below its average cost of production
- If the exporter's local price is not available then compare the import price to
 - i. A price charged for the product in a third market, or
 - ii. The exporter's average costs of production
- Amount of the antidumping duty = difference between the exporter's local price and the "dumped" price in the importing country
 - Incentive problem for foreign producers?

- Foreign firms can & do change their prices, and increase the price charged in the importing country even before an antidumping tariff is applied
 - Not so with safeguard tariff
 - For example, if the local price is \$10 and the export price to Home is \$6, the antidumping duty is \$4
 - If they charge an export price of \$8 instead of \$6 but keep the local price at \$10, the duty is now only \$2
 - Incentive for the Foreign firm to *raise* its export price even before the tariff is applied so the duty will be lower => Greater consumer surplus loss



Home Loss Due to Threat of Duty

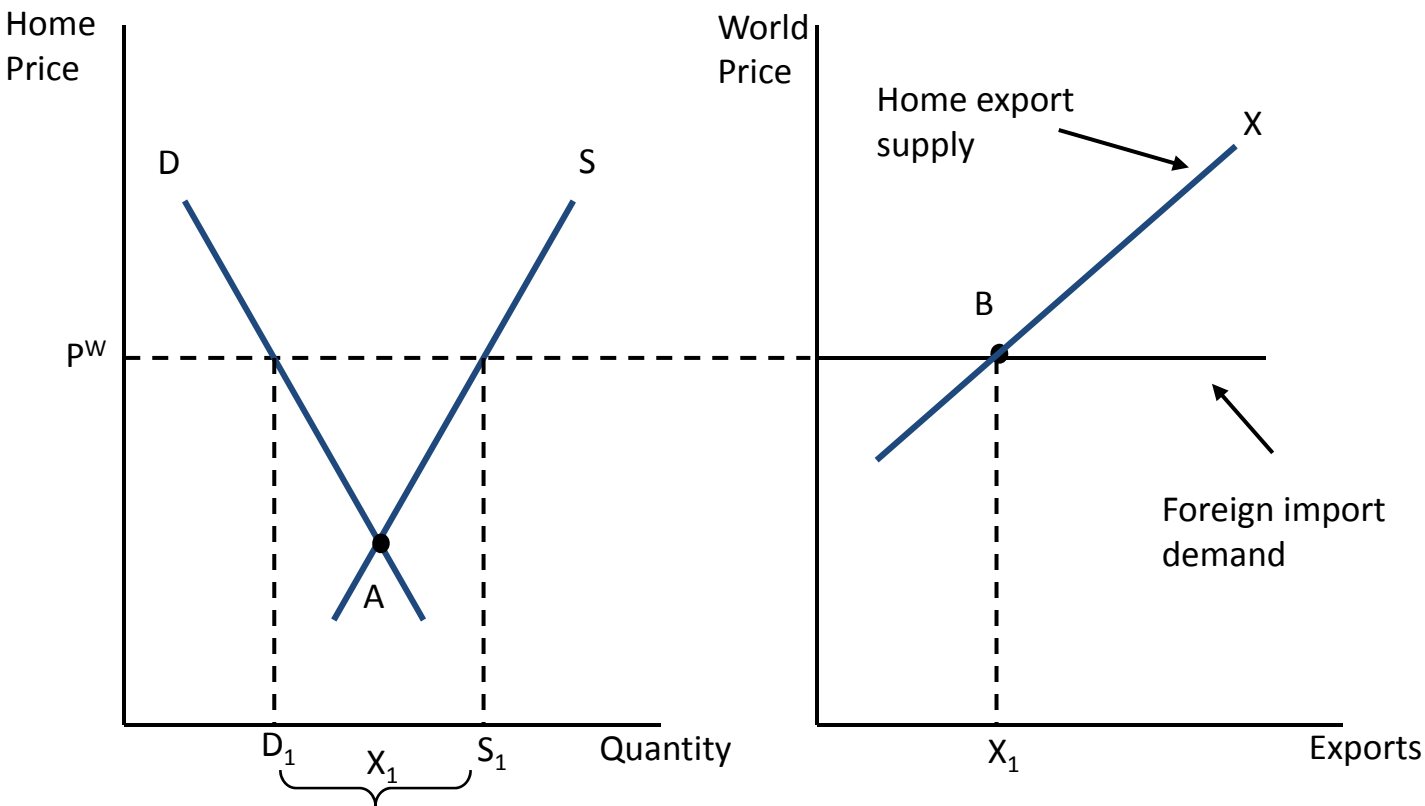
- A charge of dumping => Foreign firms to increase their prices
- Just the *threat* of anti-dumping duty is enough
- Loss for Home consumers ($a + b + c + d$)
- Gain for Home producers (a)
- Net loss for the Home country is area ($b + c + d$).
- *Incentives for Home firms to file dumping claim even when none has occurred!*

- Over-use of Anti-Dumping laws?
 - Seen empirically – vastly greater # of dumping cases files (compared to cases calling for safeguard tariff)
 - Reason 1: just the threat of case is enough to get Foreign firm to raise price => Home firm gets protection
 - Reason 2: US anti-dumping law allows Home firms to withdraw cases and settle with Foreign firms!!! Collusion?
 - Reason 3: Nature of filing process in WTO – very expensive, time consuming. Puts developing countries at disadvantage.

Export Subsidies & WTO

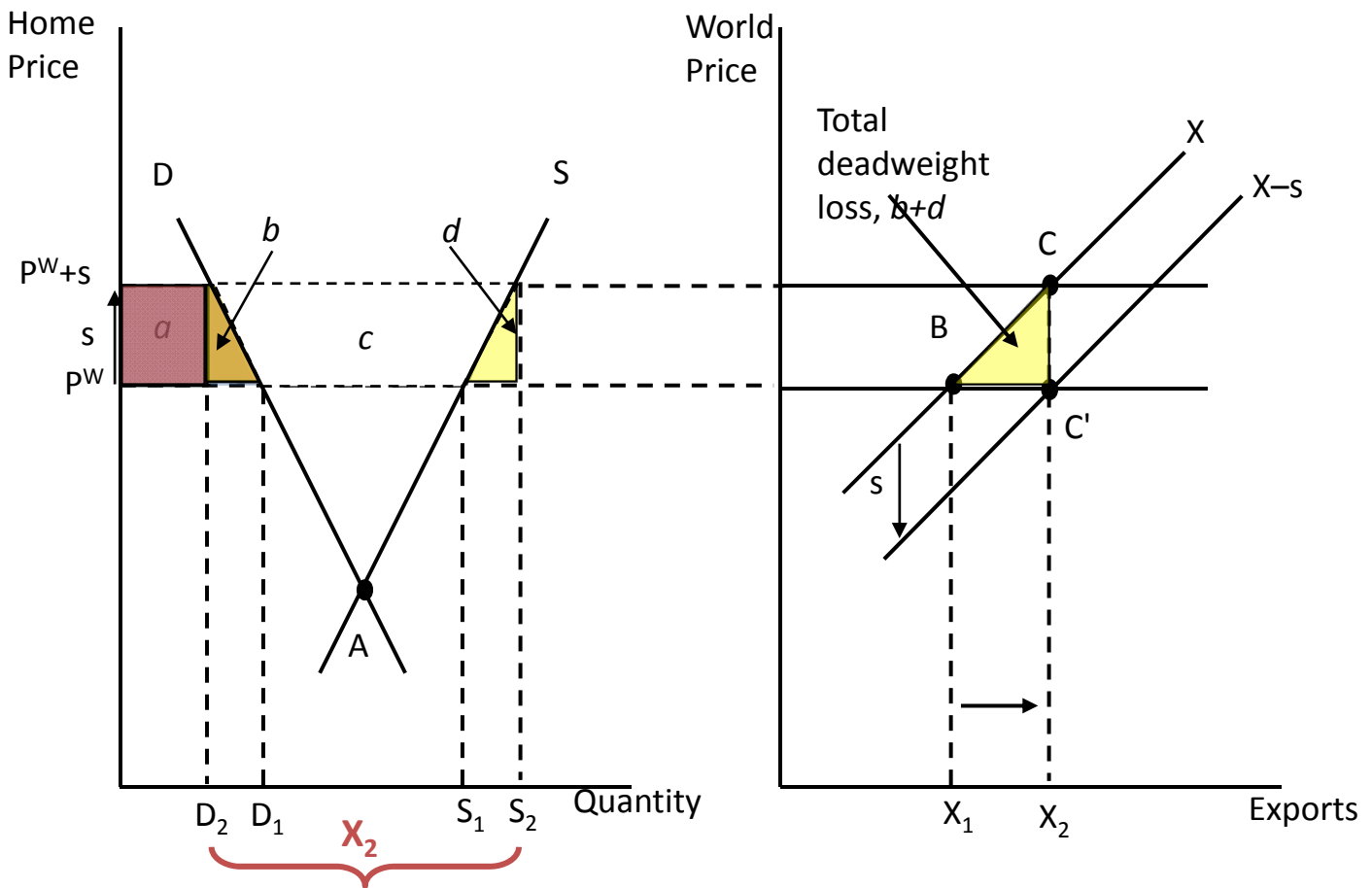
- Dec 2005, WTO Meeting in Hong Kong
- Focus on Agricultural trade
 - Lower world prices hurt farmers in land-rich developing countries like Brazil, India and China
 - But lower world prices benefit land-poor developing countries that import agricultural products
- Agricultural Export Subsidies
 - An **export subsidy** is a payment to a firm for every unit exported
 - A fixed amount or a fraction of the sales price
 - Governments give subsidies to encourage domestic firms to increase production in particular industries

- Home – small, exports sugar
- Free trade situation



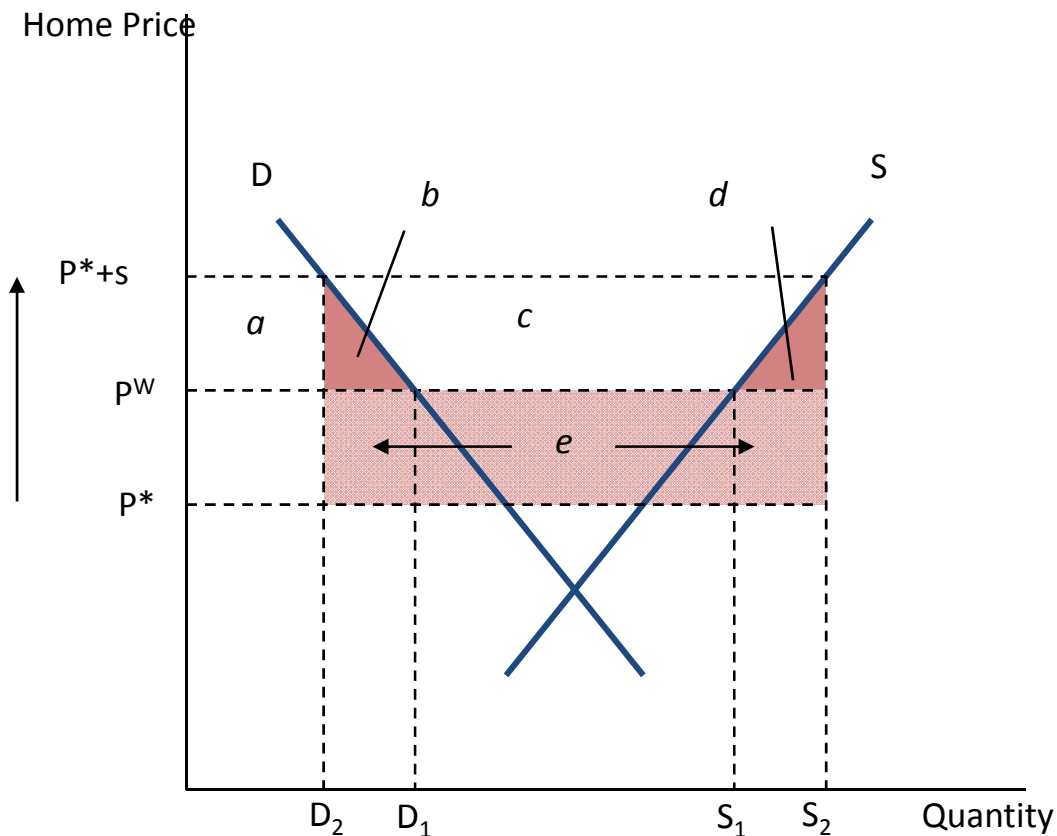
Impact of an Export Subsidy: Each ton of sugar exported receives a subsidy, s
 \Rightarrow Exporters will receive $P^W + s$ for each ton exported
 \Rightarrow Home price goes up to $P^W + s$ too!

- Impact: Home Export Supply Curve shifts Down by \$s.



- Change in CS = $-(a+b)$
- Change in PS = $(a+b+c)$
- Change in Govt Rev = $-(b+c+d)$
- DWL = $-(b+c+d)$

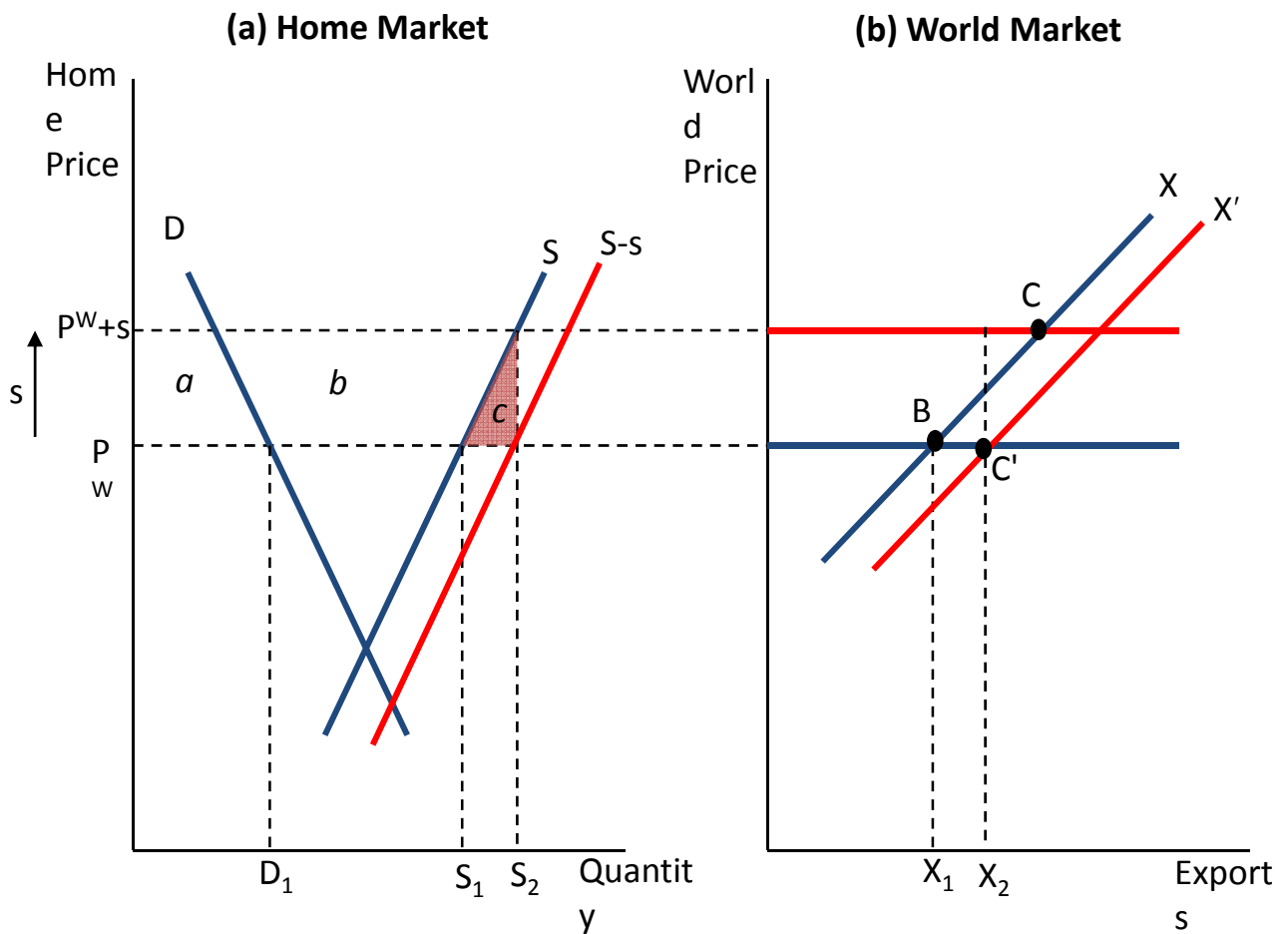
- Home – large, exporter, imposes export subsidies



- Even greater DWL than small country!
- Area e = Terms-of-trade loss! Your export commodity is getting cheaper!
- This benefits foreign consumers

Agricultural Production Subsidies

- A **production subsidy** is when the government provides a subsidy of s dollars for *every unit* (ton of sugar for example) that a Home firm produces
 - It is a subsidy to every unit produced, not just to units exported
- Small country: Production subsidy shifts domestic supply curve down
 - Cheaper to produce each quantity
- No change in domestic consumption!
 - Consumers pay world price
 - Just that producers receive $P_w + s$



- PS = rises by $(a+b)$
- Govt revenue = falls by $(a+b+c)$
- *No change in CS*
- \Rightarrow lower DWL than export subsidies

- Targeting Principle
 - Since the deadweight loss is lower for this subsidy than for the export subsidy, it makes a better policy instrument than the export subsidy to increase Home supply
 - This is an example of the **targeting principle**
 - To achieve some objective, it is best to use the policy instrument that achieves the objective most directly
 - We have many examples of using a targeting principle in economics:
 - Tax on cigarettes, tax on gasoline
 - To use an example from this book, it is better to provide trade adjustment assistance directly to those affected, than to impose a tariff or quota