

TRADE POLICIES IN ADVANCED INDUSTRIALIZED COUNTRIES

GENERAL FEATURES

- Low tariffs negotiated in GATT/WTO, average under 5%
- Non-tariff barriers remain; negotiations to liberalize; tariffication
- High barriers in selective sectors, mostly agriculture and declining industries
- High barriers imposed temporarily:
 - (a) “safeguard” or “escape clause” protection is permitted by WTO when import surge causes serious injury to domestic industry
 - (b) anti-dumping duties and “countervailing” duties against foreign subsidies
These are often misused by domestic industries and politicized bureaucracies
- Regional preferential trade agreements: EU, NAFTA
- Pressure LDCs to liberalize sectors where advanced countries have advantage
- Resist liberalization of own sectors where LDCs have advantage

UNITED STATES

Mostly low tariff and non-tariff barriers

A few sectors still heavily protected:

sugar, textiles (until recently), steel (occasionally)

Sugar quota

- US guarantees sugar producers a “break-even” price on their production (the USDA will buy any amount of sugar at this price)
- Even at this price, US demand exceeds output, so US imports some sugar
- But imports are limited by a quota (1.4 million tons)
- Without the quota, the US price would be lower, imports higher
- To make the quota viable in international politics and the WTO, US lets foreign governments administer the quota and retain the rents
- Over the past 25 years, the US price of sugar has been 2-3 times the world price, sometimes even more
- Calc's on the following page imply low elasticities: 0.05 demand, 0.3 supply
- Other complications not taken into account: preferential agreements, interaction with other sweeteners, esp. high-fructose corn syrup, endogenous world price of sugar (US monopsony power, optimal tariff)

Welfare effect calculations for 2002:

Consumer surplus loss
(areas 1+2+3+4)
= \$2,468 million

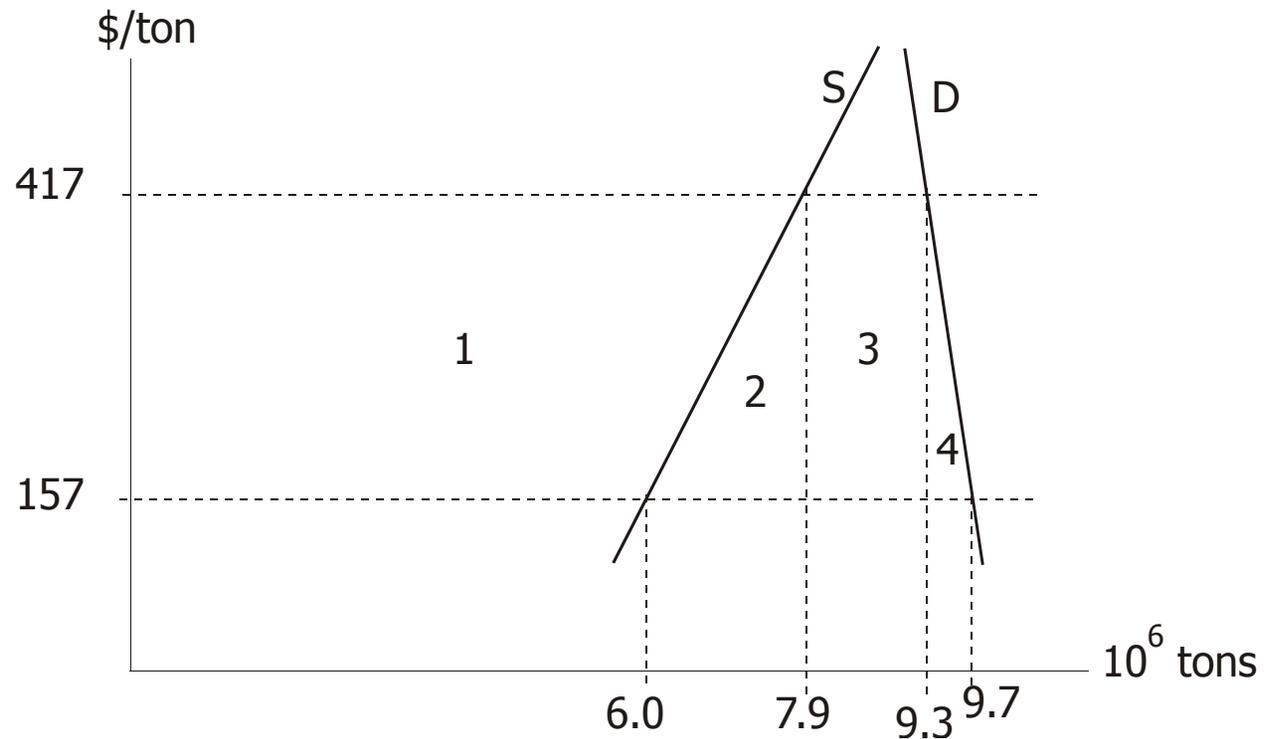
Producer surplus
gain (area 1)
= \$1,806 million

Quota rent (area 3)
= \$364 million

Consumption-side
DWL (area 4)
= \$52 million

Production-side DWL (area 2) = \$247 million

Total loss to US economy (areas 2+3+4) = \$662 million



[1] Consumption-side DWL is small, but consumer surplus loss is large

[2] Main part of social welfare loss is the loss of quota rent to foreigners

[3] Main effect of quota is redistribution from consumers to producers

Political economy:

- US sugar industry employs approximately 60,000 workers
- Producer surplus gains are about \$30,000 per worker
(although much of this may go to capital and land owners, not workers)
- The quota does increase employment in the industry
Without it, employment would be about 25% lower: 15 thousand jobs
- Each US consumer pays about \$8 per year more for sugar (\$30/family)
as a result of the quota
- Consumer surplus cost is about \$164,000 per job saved in this industry
(Note: worse, the jobs “saved” may be just shifted from other sectors;
aggregate employment is largely determined by monetary & fiscal policies)

- The industry is highly concentrated geographically (Florida; Hawaii, Wisconsin)
- US sugar sales represent 1% of farm receipts & 0.5% of farm employment
but 17% of political contributions from the agricultural sector
- Total political contributions by sugar lobby since 1990 > \$20 million
Fanjul brothers (Flo-Sun) gave \$1 million in political contributions in 2000, 2004
- Lobby can also organize petitions from thousands of workers in key states
- Sugar kept out of many preferential trade agreements with low-cost producers
- In 1996 a phase-out attempt was defeated in the House

Textiles and Garments

Two separate industries: [1] some industrial textile production has high capital, research intensity; US firms can compete

[2] garments very labor-intensive; design in West but production in LDCs

Until recently, protected by complex system of quotas: Multi-Fibre Arrangement

- Allocations specific to garment type and exporting country
- Quotas administered by exporters, rent captured by foreigners
- Some secondary markets in quotas, high prices show value of rent
- Estimated welfare cost to US economy: \$11.8 billion in 2002
(Calculation complicated because multiple products, exporters, ...)
- Political support for quotas from organized labor: ILGWU
- Since 2005, MFA being phased out (but with occasional backsliding)

Other products

Agriculture: US exports many products, but has price supports, subsidies

These affect world trade, creating conflicts in international negotiations

US often sides with EU etc. against "clean" exporters like Canada and Australia

Steel: Occasional imposition of quotas, in recessions, or before elections

Many anti-dumping actions, countervailing duties against alleged foreign subsidies

Export promotion

Major current issue: Consumer demand may remain stagnant as debt reduced
Recovery from recession may depend on (investment and) exports

But unpleasant GDP arithmetic

$$\begin{aligned} \text{GDP} &= C + I + G + (X - M) \\ &= C + S + T \end{aligned}$$

Therefore

$$X - M = (S - I) + (T - G)$$

So increase in $X - M$ requires accompanying

1. increase in S (possible but painful), T (politically difficult)
2. decrease in I (not good in short run or long run),
 G (too much is entitlement spending)

EUROPEAN UNION

Taxonomy of preferential trade agreements:

Free trade area: members' goods have free access to each other's markets but each country chooses its own policy vis-a-vis non-members (This requires complicated specification of "rules of origin")

Customs union: members' goods have free access to each other's markets and all have a common policy vis-a-vis non-members

Economic union: unrestricted access not just for goods, but services including professions, migration, capital flows ...

(On the macro side, fixed exchange rates, common currency, central bank ...)

These are pure cases; in practice there are reserved sectors, phaseouts of existing restrictions in some sectors, ...

EU has progressed through these stages;

most important step was "single-market" act of 1992 that reduced/eliminated border formalities, labor mobility restrictions unified product standards and other regulations

Economic welfare gains of 1992 estimated at approximately 1.8% of EU GDP (But K-O say French have started to buy British white sliced bread!)

Some other policies: support for Airbus and some other high-tech sectors

Common agricultural policy (CAP)

- This program was not originally intended to be an export subsidy.
- It started as a price control to insure farmers against price fluctuations.
- Over time, political power of the agricultural sector grew, and the controlled price was not reduced as productivity increased.
- Starting in the 1970s the program had the effect of a price support, led to large surpluses: by 1985 these grew to 12 million tonnes of wheat, 1.2 m of butter, 780,000 of beef, a “wine lake”, ...
- The EU started selling the surpluses on the world market: implicit export subsidy
- By comparative advantage, EU should be a net importer of these products
- Instead the subsidies are large enough to decrease the world price
- Calculation of economic effects and welfare costs complicated by interaction (general equilibrium) effects, endogenous world price, ...
Budgetary cost of CAP averages around €60 billion (0.6% of EU GDP)
Dead-weight losses around €6 billion (only 0.06% of GDP but large)
- Many attempts to reform, phase out ... but futile due to French intransigence and German acquiescence

Partial equilibrium illustration of effects:

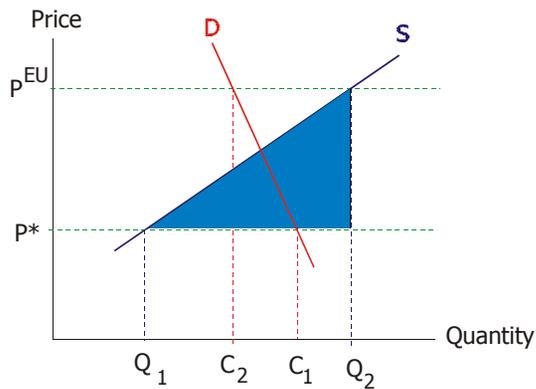
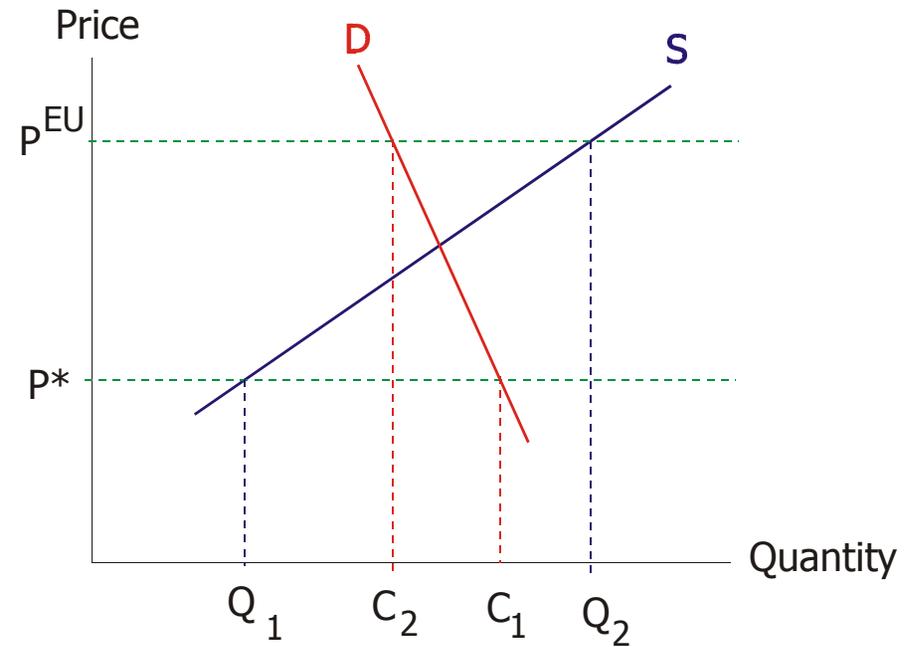
Assume world price constant at P^*

Support price P^{EU} higher than even the EU autarkic price

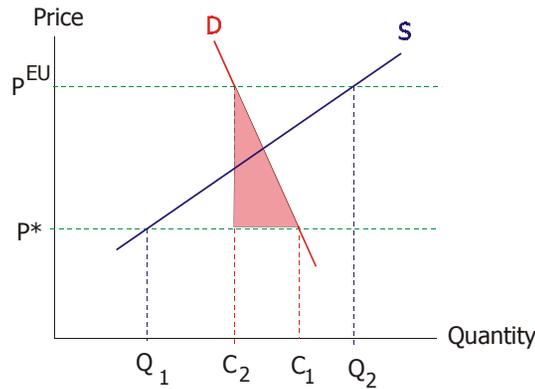
EU output rises from Q_1 to Q_2

EU consumption falls from C_1 to C_2

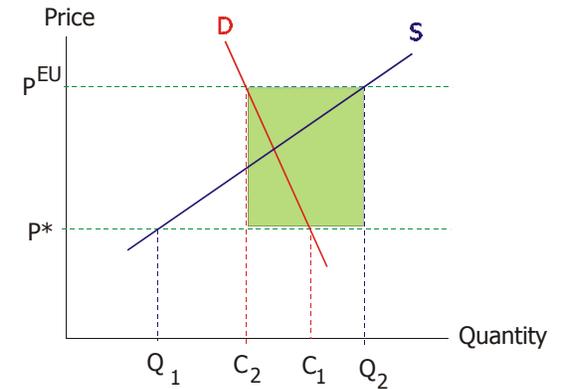
Dead-weight losses and gov. revenue costs shown separately to avoid cluttered diagram.



Production-side DWL



Consumption-side DWL



Budget cost of subsidy

JAPAN

Rice import ban

This was effectively total until 1995

Justified on grounds of national food security, cultural importance of rice

High-cost domestic production includes small urban paddies, "weekend" farms

Minor adjustments, relaxation since then

In 1999, conversion to tariff, import duty around 340 yen/kg

Compare this with domestic support price around 290 yen/kg

In 2004, imports 0.8 million tonne, domestic production 10.9 million tonnes

Difficult to establish world price because different varieties, but

FAO estimates 2002 price in Japan about 14 times price in US

Other import bans now somewhat relaxed

Beef (Justification: Japanese have longer intestines so they can't eat much beef.

But how they can eat higher-cost Japanese beef is not explained!)

Restrictions revived in response to fears of BSE (mad cow disease)

Oranges, ...

Other policies: Various industrial policies, with doubtful effects
even for the sectors, let alone for the whole economy

EFFECT OF ADVANCED-COUNTRY BARRIERS ON LDCs

Barriers keep prices in rest of the world lower than they otherwise would be

This hurts other exporters who would have natural comparative advantage

That includes many LDCs – Thailand and Vietnam (rice),

Brazil, Thailand, Caribbean countries (sugar),

West African and Central Asian countries (cotton) ...

Also includes other rich countries exporting agric. Products: Canada, Australia

And in case of CAP, implicit export subsidy worsens EU's own terms of trade

Estimates of increase in world price if distortions are removed:

Rice: 33% on average, up to 90% on short/medium grain rice

Sugar: 20-40% (exporters to US would lose quota rent so their gains smaller)

Cotton: 10-20%

Very crude calculation of the gains and losses from removing rice distortions:

Gain = value of net exports * 0.33 This implicitly assumes zero elasticities,
so underestimates gains and overestimates losses

Net exporters' gains: Asia minus Japan \$800 million, US \$290 million

Net importers' losses: Europe \$240 million, Africa \$560 million