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The question of the removal of international trade barriers to encourage financial growth

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Definition of Key Terms

Trade Barriers

Government regulation to restrict the flow of international goods or services going in or out of a country. This could be in the form of tariffs, quotas, embargos, subsidies to domestic producers and other methods. However, trade barriers such as embargos may be imposed by a nation due to international disputes.

Embargo

A complete ban on trade of a certain good or service from a specific country.

Subsidy

A sum paid by a government to domestic firms to cut their cost of production, resulting in lower costs for consumers. By doing so, this increases its affordability and therefore causes the demand for that good or service to rise.

Protectionism

The economic policy to restrain imports from foreign nations, through the use of tariffs, embargoes, quotas as well as Health and Safety standards and Environmental Standards.

Quota

A government established limit on the number of imports or exports transferred during a certain time period.

Dumping

When a country exports a good or service set at a price that is cheaper in the foreign importing market than in the domestic market. This would lead to driving foreign companies out of businesses as they would not be able to compete. Therefore, increasing the exporting firm's market share in that foreign country. The World Trade Organisation (WTO) does not prohibit the practicing of dumping, unless it is threatening and damaging to the economy the export is entering.

World Trade Organisation (WTO)

Founded in 1995, the WTO is an intergovernmental organisation that is set up to monitor and control regulations for international trade. Its main concern is smooth and free trading between countries. With 164 member nations, they are responsible for 95% of international trade. The World Trade Organisation manages trade regulations and sets standards that countries have to abide in order to trade with others. For example, to reduce the risk of spreading diseases, health and sanitation standards are established for agricultural goods.

Introduction

The birth of free trade links back to an economic theory, mainly employed between the 16th and 18th century, named Mercantilism: the theory where countries aim to accumulate wealth through the trading of goods internationally. Free trade allows nations to specialise in producing goods or services that they are comparatively best at making. If a country can produce more of a product with a lower opportunity cost than another country, then they have a comparative advantage at making that product.

The removal of trade barriers would allow for complete free trade between nations. As a result, this would boost global competitiveness due to an immense supply of goods from all countries. Thus, providing a larger range of goods and services sold at lower prices which would be extremely beneficial for consumers.

Trade barriers ensure domestic producers have the opportunity to compete with international rivals as well as save jobs, save infant industries and prevent “dumping”. The most famous protectionist policy is tariffs: taxes imposed on imported goods to make them more expensive for consumers to purchase. As the price rises, goods become less competitive and appealing to consumers, making consumers unlikely to buy them. As a result, consumers resort to buying domestic substitute goods that are less expensive.

Additionally, trade barriers prevent overspecialization. Free trade allows countries to specialise in making the goods that they are better at making, by having comparative advantages. Overspecialization occurs when countries over-rely on other nations for specific goods or over-depend on their exports to acquire revenue. Every country will target to maintain some level of self-sufficiency, especially in specific industries such as agriculture.

Infant industries face various challenges when they first enter the market as many of them find it difficult to compete with competitors abroad. Well established international competitors may use pricing or non—pricing strategies that aim to force infant industries out of business. These strategies include, predatory pricing, where international firms set their prices very low when new competitors enter the market. New competitors are not be able to experience economies of scale or sell their product at such a low price at this early stage, thus forcing them to close their business when they cannot compete at these low prices. This can be solved by imposing tariffs on the imports from the international competitors, forcing their prices to rise and become less competitive. As well as tariffs, subsidies to the domestic firms in the infant industry would allow the firms to lower their cost of production and thus sell their goods or service at a cheaper price.

Issues with Trade Barriers

Trade Wars

Enforcing trade barriers can deteriorate international relationships between countries. Currently, the two largest economies in the world, United States of America and China, are engaging in a trade war. In President Trump’s campaign, he promised to rectify China’s “long-time abuse of the broken international system and unfair practices”. Beginning with the US setting a 30% tax on imported solar panels. China, being the largest exporter of solar panels, criticised the charge. As retaliation, China imposed tariffs on as many as 128 American goods: 25% on Aluminium, airplanes, pork, cars and soybean with another 15% on fruit, nuts and steel tubing.

Less Variety of Goods

The higher the price of a good, the less people will demand for it. When tariffs cause the price of products to rise, there will be a contraction in demand. Not only that, embargoes fully ban certain products from entering the domestic market. The lack of variety due to the lowered quantity of goods being imported into the country disadvantages domestic consumers. As every country specialises in products that they have a comparative advantage in, each country may not produce certain products due to the absence of resources or technology.

Higher costs for Domestic consumers

Tariffs imposed on products are at the expense of domestic consumers. When tariffs are set on a certain good, international producers pass on the tariff for the consumers to pay more to cover the costs. Low income households that require necessary imports are majorly affected by these tariffs. Although these tariffs do generate more tax revenue and reduce trade deficits, not all governments use the revenue to improve their economic welfare.

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