INTERNATIONAL TRADE POLICY

- **Free trade** occurs when governments do not attempt to restrict what its citizens can buy from another country or what they can sell to another country

- While many nations are nominally committed to free trade, they tend to intervene in international trade to protect the interests of politically important groups

Types of Trade Policy

1. Tariff
2. Export Subsidy
3. Import quota
4. Voluntary Export Restraint
5. Local Content Requirement
6. Other trade policy
   - Export credit subsidies
   - Government procurement
   - Bureaucratic regulations

1. Types of Tariffs

- A **specific tariff** is levied as a fixed charge for each unit of imported goods.
  a. For example, $1 per kg of cheese
- An **ad valorem tariff** is levied as a fraction of the value of imported goods.
  b. For example, 25% tariff on the value of imported cars.

2. **Export Subsidy**
   - ➢ An export subsidy can also be *specific* or *ad valorem*
     - A specific subsidy is a payment per unit exported.
     - An ad valorem subsidy is a payment as a proportion of the value exported.
   - ➢ An export subsidy raises the price of a good in the exporting country, decreasing its consumer surplus (making its consumers worse off) and increasing its producer surplus (making its producers better off).
   - ➢ Also, government revenue will decrease.
   - ➢ An export subsidy raises the price of a good in the exporting country, while lowering it in foreign countries.
   - ➢ In contrast to a tariff, an export subsidy worsens the terms of trade by lowering the price of domestic products in world markets.

3. **Import Quota**

- An import quota is a restriction on the quantity of a good that may be imported.
- This restriction is usually enforced by issuing licenses to domestic firms that import, or in some cases to foreign governments of exporting countries.
- A binding import quota will push up the price of the import because the quantity demanded will exceed the quantity supplied by domestic producers and from imports.
- When a quota instead of a tariff is used to restrict imports, the government receives no revenue.
  - o Instead, the revenue from selling imports at high prices goes to quota license holders: either domestic firms or foreign governments.