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1. Learning Outcomes

After studying this module, you shall be able to

- Understand the meaning of NTB's
- Classify the types of NTB's
- To study the welfare effects of export subsidies
- Differentiate between Quota and Tariff
- Significance of technical barriers to trade

2. Introduction

International trade enables domestic consumers to choose from a large number of goods, reduce the cost of those goods which are produced with increased competition, and allows domestic industries to send their products to international markets. While all of these pretends to be beneficial, but free trade is not widely accepted and is not beneficial to all the parties. Tariffs have historically been the most important form of trade restriction which we studied in detail in our previous module. The General Agreement on Tariffs and Trade (GATT) strides to lower the overall tariffs levels in US and all over the world. Since GATT members had multilateral agreed to phase out many tariffs, and these countries came up with more inventive ways to cut down imports and protect domestic industries. These inventive measures are called Non-tariff Trade Barriers

3. Non-Tariff Barriers

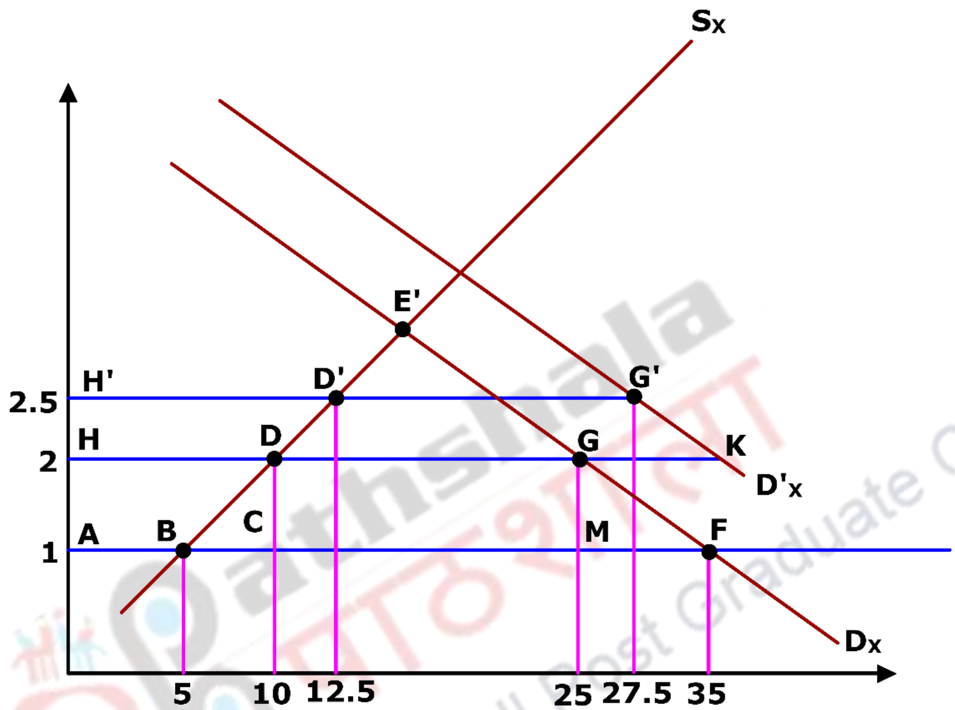
Non-tariff barriers are the government policies other than tariff that tend to distort trade. These refer to the restrictions resulting from prohibition conditions or specific market requirement that make product imports and exports difficult or costly

4. Types of Non-Tariff Barriers

Various types of Non-tariff Barriers are
1 .Import Quotas
2. Voluntary export restraints
3 .Export subsidies
4 .Dumping
5. Technical barriers to trade

4.1 Quotas

One of the most restrictive forms of protectionism is the quota. Quotas involve restriction of imports of a good to a definite quantitative level. In practice, this means that a country imposing a quota imports only a certain number of units of the good on an annual basis. The partial equilibrium effects of import quota can be explained through fig 1



In fig 1 , Dx is the demand curve and Sx is the supply curve of commodity X for nation 1. With free trade at the world price of Px = 1, the nation consumes 35 (X) AF, of which 5X (AB) is produced domestically and the remainder of 30X (BF) is imported.

An import quota of 15X(DG) will raise the domestic price of X to Px = 2 which is the same as if 100 percent ad valorem import tariff on commodity X is charged. At Px = 2, the quantity demanded of 25 X (HG) equals 10X (HD) produced domestically plus the 15X (DG) allowed by import quota. Thus consumption is reduced by FM and domestic production is increased by 5X (BC) with an import quota of 15X (DG).

With an upward shift of Dx to D'x , the given import quota of 15X(D'G') would result in domestic price of X rising to Px = 2.50, and domestic production rising to H'D' (12.5X) and domestic consumption to H'G'.

On the other hand if demand is increased from Dx to D'x and with given 100% import tariff, price of X would not have been changed and domestic production would also be the same ie 10X (HD) but domestic consumption would have increased to HK and imports to DK.

4.2 Voluntary Export restraints

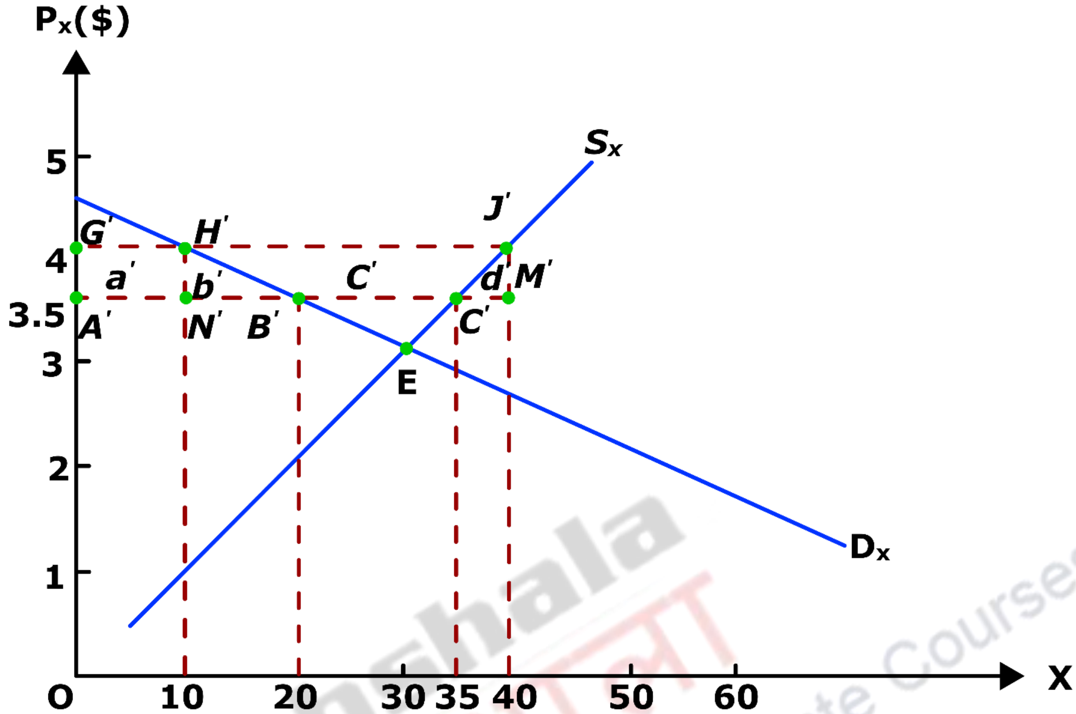
The other important Non-tariff trade barriers or NTB's is voluntary export restraints (VERs). These refer to the case where an importing country induces another nation to reduce its exports of a commodity "voluntarily", under the threat of all round restrictions, when these exports threaten an entire domestic industry.

- VERs are often created because an exporting nation might agree to voluntarily comply because it may want to avoid damaging its relationship with a foreign government and country's consumers.
- VERs are generally imposed at the request of importer for providing a protection measure for its domestic businesses producing substitute goods.
- VERs is indeed like import quota where the licenses are authorized to foreign governments and therefore is very expensive for the importing country.
- The most remarkable example of VERs is when Japan levied a VER on its auto exports into the U.S. resulting from 1980s American pressure. The VER finally gave the U.S. auto industry some protection against a high foreign competition.

4.3 Subsidies

Export subsidies are a payment to a firm or an individual that ships the good abroad. These are the direct payments or granting of tax relief or the subsidized loans to the nation exporters to spur the nation exports. Like a tariff, an export subsidy can either be specific or ad valorem. As the government provides the export subsidy, shippers export the good till the point where the domestic price exceeds the foreign price by the amount of the subsidy.

The effects of subsidy is explained with the help of fig2



In the fig2 Dx and Sx represent Nations 2 demand and supply curves of commodity X. At the free trade price of Px , small Nation2 produces (A'C'), consumes (A'B'), and exports(B'C'). With the subsidy of Px-Pxs on each unit of commodity X exported, Px rises to Pxs for domestic producers and consumers.. At Pxs, Nation produces G'J', consumes G'H' and exports H'J'.
Domestic Consumers lose = a'+ b'
Domestic producers gain = a' + b' + c'
Government subsidy = b' + c'+ d'
Dead weight loss = area (B'H'N') + area (C'J'M')
Although export subsidies may benefit industries and workers in a subsidized industry by increasing sales and employment, the benefits may be offset by certain cost that fall on the society as a whole. Consumers in the exporting nations suffer as the international terms of trade moves against them. Also the taxes are required to finance the export subsidies, so the burden falls on the consumers.

4.4 Local Content Requirements

- Local Content requirement is a regulation in which some definite fraction of a final good should be produced domestically.
- It may be specified in value terms, by requiring that some minimum share of the value of a good represent domestic value added or in physical units.

- The developing countries have widely used Local content laws which are trying to shift their manufacturing base from assembly back in to intermediate goods.
- From the view point domestic producer of inputs, a local content requirement provide the protection in the same way as an import quota does
- Local content does not place a strict limit on imports. Rather it allows the firms to import more, provided that they also buy more goods domestically

4.4 Dumping

Trade barriers may also result from dumping. Dumping is recognized as a form of international price discrimination. It happens when foreign buyers are charged reduced prices as compared to domestic buyers for a same product after taking into account the transportation cost and tariff duties.

Forms of Dumping

a) Sporadic Dumping – Sporadic dumping is the occasional sale of a commodity at below cost or at a lower price abroad than domestically in order to discharge an unanticipated and temporary surplus of the commodity without having to reduce the domestic prices.

b) Predatory Dumping – Predatory Dumping is the temporary sale of a commodity at below cost or at a lower price abroad to knock out foreign producers out of the market, post which prices are increased so as to reap the fruits of the newly acquired monopoly abroad.

c) Persistent Dumping – Persistent Dumping is a continuous tendency of a domestic monopolist to maximize total profits by selling the commodity at a higher price in the domestic market than the international market.

Causes of Dumping

Dumping usually occurs due to the following reasons

- Producers in one country are trying to be in competition with the producers in the other country.
- Producers are trying to clear off excess stuff which they are not able to sell in their own country.
- Producers can make profit by dividing sales in to domestic and foreign markets and then charging each market whatever price the buyers are willing to pay.

5. Import Quota Vs. Import tariff

Import quotas and tariffs have the same objectives that is to reduce the level of imports so as to protect the domestic industries, correct balance of payment deficit, expand domestic employment and economic activities. Still they are distinguished on the basis of following points –

- **The revenue effect** – The tariff brings revenue to the government whereas quotas do not. When quota instead of tariff is used to restrict imports, the sum of money that would have appeared as government revenue with a tariff is collected by the one who receives import license. License holders are able to buy imports and resell them at a higher price in the domestic market.
- **Corruption and bribery –** Distribution of import licenses may give rise to corruption and bribery on the part of government officials. Import tariffs do not create such evils of government corruption, political favoritism etc.
- **Monopoly profit –** Quotas creates a monopoly profit for those who have import licenses. This means that consumer surplus is converted into monopoly profits. Thus, quotas are likely to lead to a greater loss of consumer welfare. Where as if a tariff is imposed domestic price will be equal to import price plus tariff.
- **Nature of protectionism** – In its protective effect, trade shelters the domestic market from competition by foreign firms, while import quota offers protection to old inefficient firms as import licenses are generally offered to them.
- **Price Differential** – Tariffs and Quota also differ in price differentials between domestic price and the world price, in the case of a tariff, the domestic price differs from the world price by the amount of a tariff duty. But under quota domestic price would exceed the tariffs, because when the quantity imported is fixed, instability in demand and supply conditions in the domestic and world markets have to be adjusted not through changing import quantities but through altered prices.
- **Stability** - An import quota is unstable because it can be changed at the discretion of the bureaucracy, while a tariff is stable because any change in tariff policy requires legislative approval.
- **Preventing Recession** – Quotas may also be used as a device to prevent the international transmission of severe recession. Recession generally causes a fall in prices and this may encourage exports. A country may make use of quotas to safeguard their interest against such recession

The following example illustrates how during the periods of growing demand, an import quota inhibit the volume of imports by a large amount than does an equivalent import tariff

Fig 3 represents the hypothetical trade situation of the Nation 1 in commodity X. The nation 1 supply and demand schedule is given by S_{nat1} and D_{nat1} and S_{nat2} represents thae nation 2 supply schedule. Suppose the Nation 1 has the option of levying a tariff or quota on commodity X imports to protect Nation 1 companies from foreign competition.

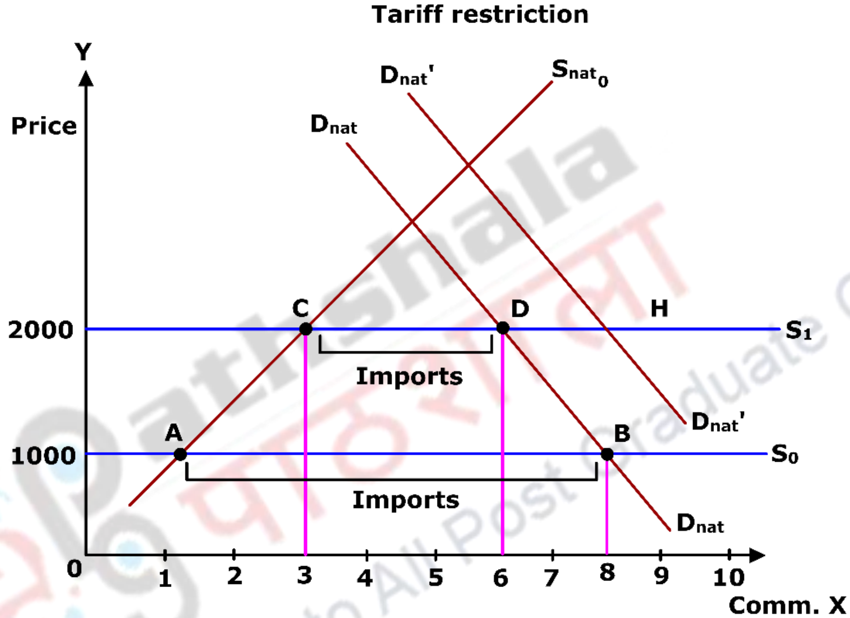


Figure: 3A

Quota Restriction

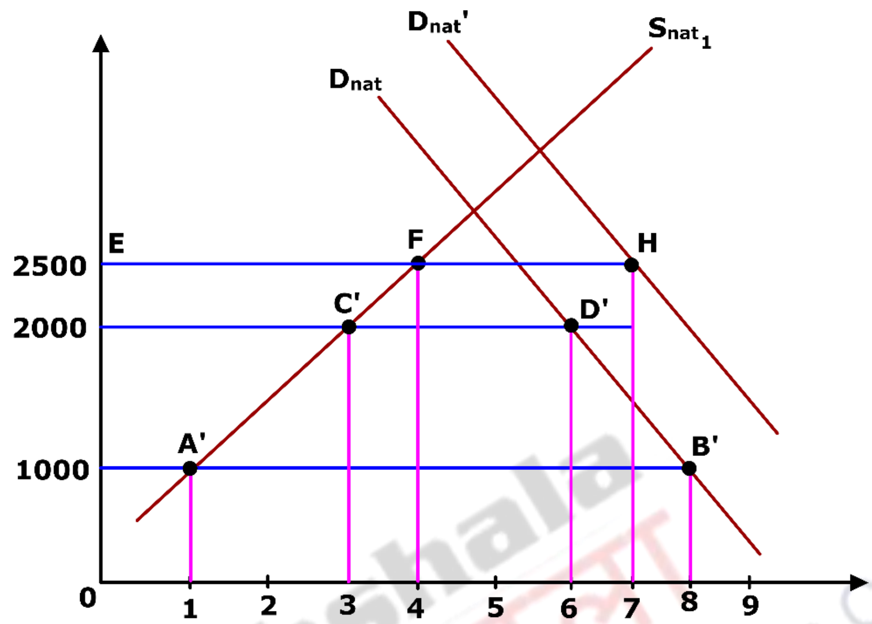


Figure: 3B

In fig3 (a) a tariff of \$ 1000 would raise the commodity X from \$1000 to \$2000. And so commodity X imports will fall from 7 lakh units (AB) to 3 lakh units (CD). **In fig 3 (B)** an import quota of 3 lakh units would put nation 1 in a trade position identical to that which occurs under tariff and the rise in price is the same ie from \$1000 to \$2000. So far it appears that the tariff and the quota are equivalent with respect to their restrictive impact on the volume of trade.

Now suppose the Nation 1 demand for Commodity X rises from D_{nat} to D'_{nat}. Despite the increased demand, the price of commodity X remains at \$2000. This is because the Nation 1 price cannot differ from the Nation 2 Price by an amount exceeding the tariff duty. Commodity X imports rises from 3 lakh units (CD) to 5 (CH) lakh units. So under an import tariff prices were not increased further.

In fig 2 (b) an identical increase in demand induces a rise in domestic auto prices. With increase in the demand from D_{nat} to D'_{nat} forces commodity x prices up from \$2000 to \$2500. At this new price the domestic production equals 4 lakh units (EF) and domestic consumption equals 7 lakh units (EH). So the adjustment is occurred in the prices rather than the quantity of commodity X imported.

So during the period of growing demand, an import quota is more restrictive trade barrier than an equivalent import tariff.

6. Technical Barriers to trade

Technical barriers refer to a country's national standards for health, safety, and product labeling. Even when these regulations are designed solely for the protection of domestic population, they can distort international trade. For example most firms produce products primarily for domestic consumption and the exportation of the product provides a secondary source of demand. However when a firm decides to export its product, it will have to change the product label. In most cases, the new label will have to confirm to the importing country's product labeling and standards and to be printed in the country's official language.

In addition to the labeling changes, many domestic products that are exported are also modified to meet government technical standards. For example if Japan firm is to sell car in India, the steering wheel and other driver related components have to be moved from the left side of the car to the right side of the car.

The WTO Agreement on Technical Barriers to Trade ("TBT Agreement"), entered into force in 1995, is the multilateral successor to the Standards Code, signed by 32 GATT contracting parties at the conclusion of the 1979 Tokyo Round of Trade Negotiations. The purposes of the TBT Agreement can be broadly described as: (1) assuring that technical regulations, standards and conformity assessment procedures, do not create unnecessary obstacles to international trade, while (2) leaving Members adequate regulatory discretion to protect human, animal and plant life and health, national security, the environment, consumers, and other policy interests

The TBT agreement says the procedures used to decide whether a product conforms with relevant standards have to be fair and equitable. It discourages any methods that would give domestically produced goods an unfair advantage. The agreement also encourages countries to recognize each other's procedures for assessing whether a product meet their standards. Without recognition, products might have to be tested twice, first by the exporting country and then by the importing country. Manufacturers and exporters need to know what the latest standards are in their prospective markets. To help ensure that this information is made available conveniently, all WTO member governments are required to establish national enquiry points and to keep each other informed through the WTO. The Technical Barriers to Trade Committee is the major clearing house for members to share the information and the major forum to discuss concerns about the regulations and their implementation.

7 Summary

Industrialized countries have moved from tariffs to NTBs due to the fact that developed countries have sources of income other than tariffs. Tariffs for goods production were reduced during the eight rounds of negotiations in the WTO and the General Agreement on Tariffs and Trade (GATT). After lowering of tariffs, the principle of protectionism demanded the introduction of new NTBs such as technical barriers to trade (TBT). Increasing consumer demand for safe and environment friendly products also have had their impact on increasing popularity of TBT. Many NTBs are governed by WTO agreements, which originated in the Uruguay Round (the TBT Agreement, SPS Measures Agreement, the Agreement on Textiles and Clothing), as well as GATT articles. NTBs in the field of services have become as important as in the field of usual trade. Thus, NTBs can be referred as a new of protection which has replaced tariffs as an old form of protection.