INTERNATIONAL TRADE

Objectives

After studying this chapter, you will be able to:

- Explain how a country can gain from international trade
- Explain how markets enable us to reap the gains from international trade and identify its winners and losers
- Explain the effects of international trade barriers
- Explain the arguments used to justify trade

The Gains from International Trade

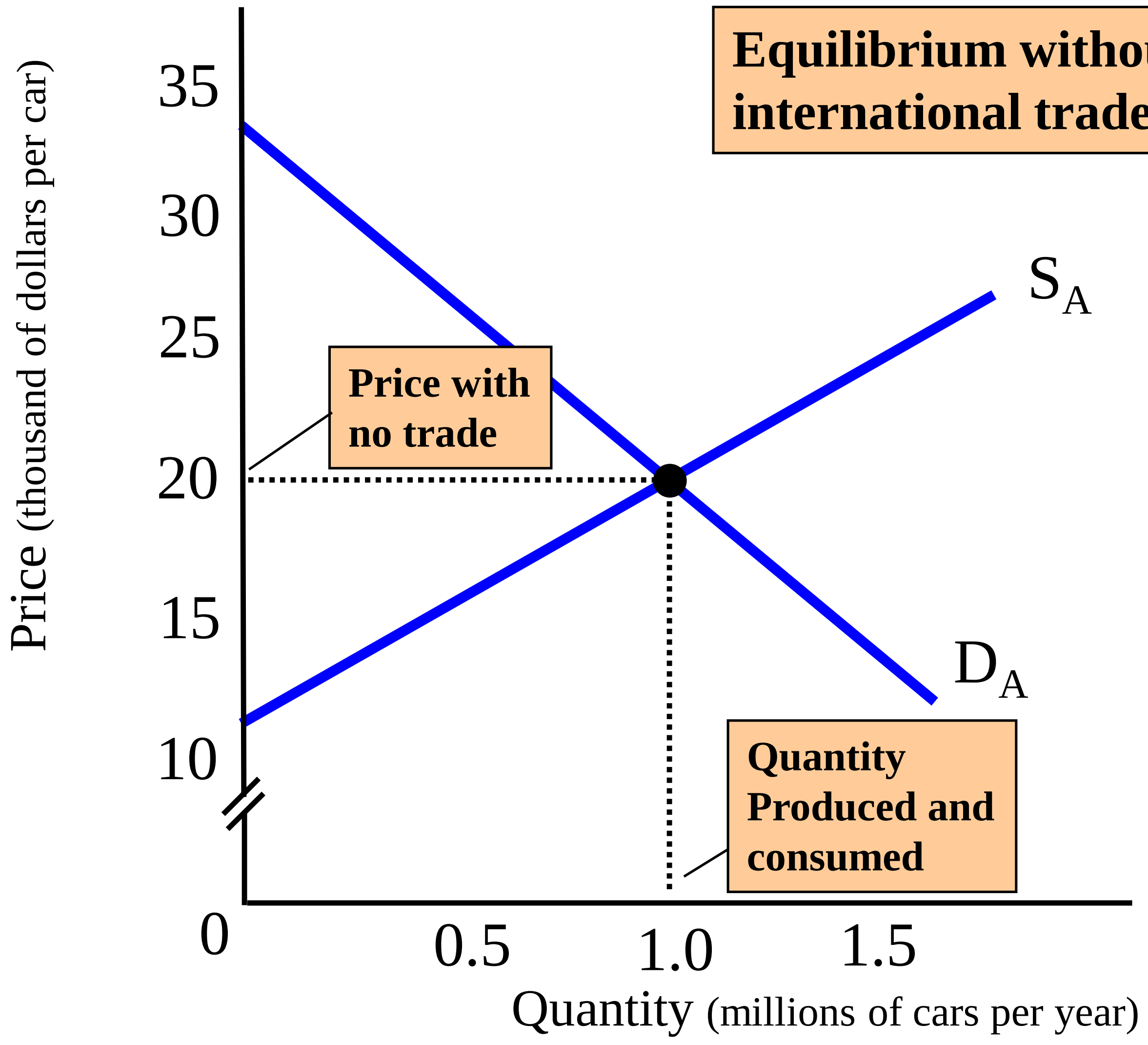
- **Imports** are the goods and services that we buy from people in other countries.
- **Exports** are the goods and services we sell to people in other countries.

Markets and the Distribution of Gains and Losses

- An import
  - Australia is an importer in the market for cars
  - The market for cars without international trade is illustrated in figure 7.3(a)
  - The market for cars with international trade is illustrated in figure 7.3(b)

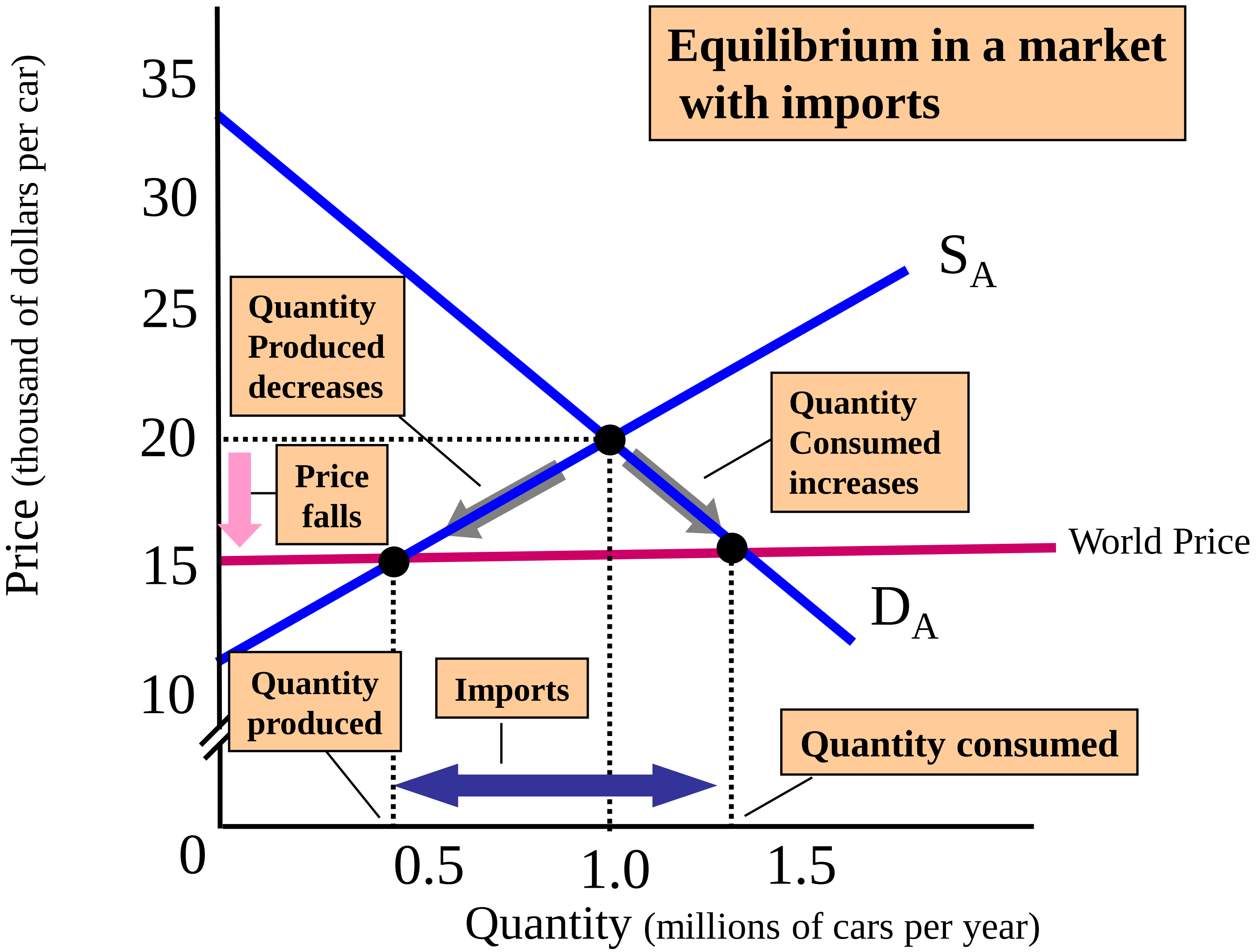
A Market With Imports

Figure 7.3(a)

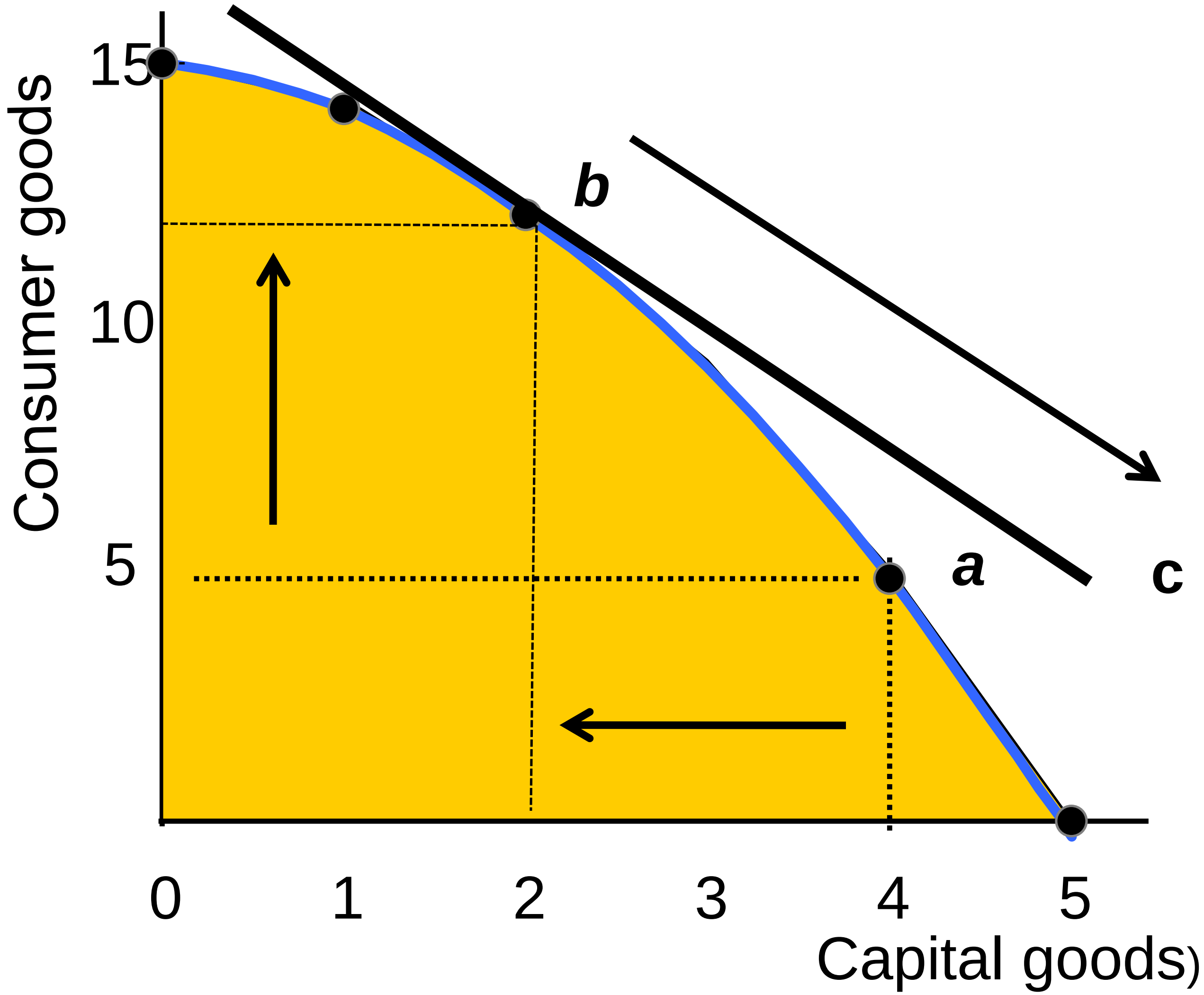


A Market With Imports

Figure 7.3(b)



Benefits of trade

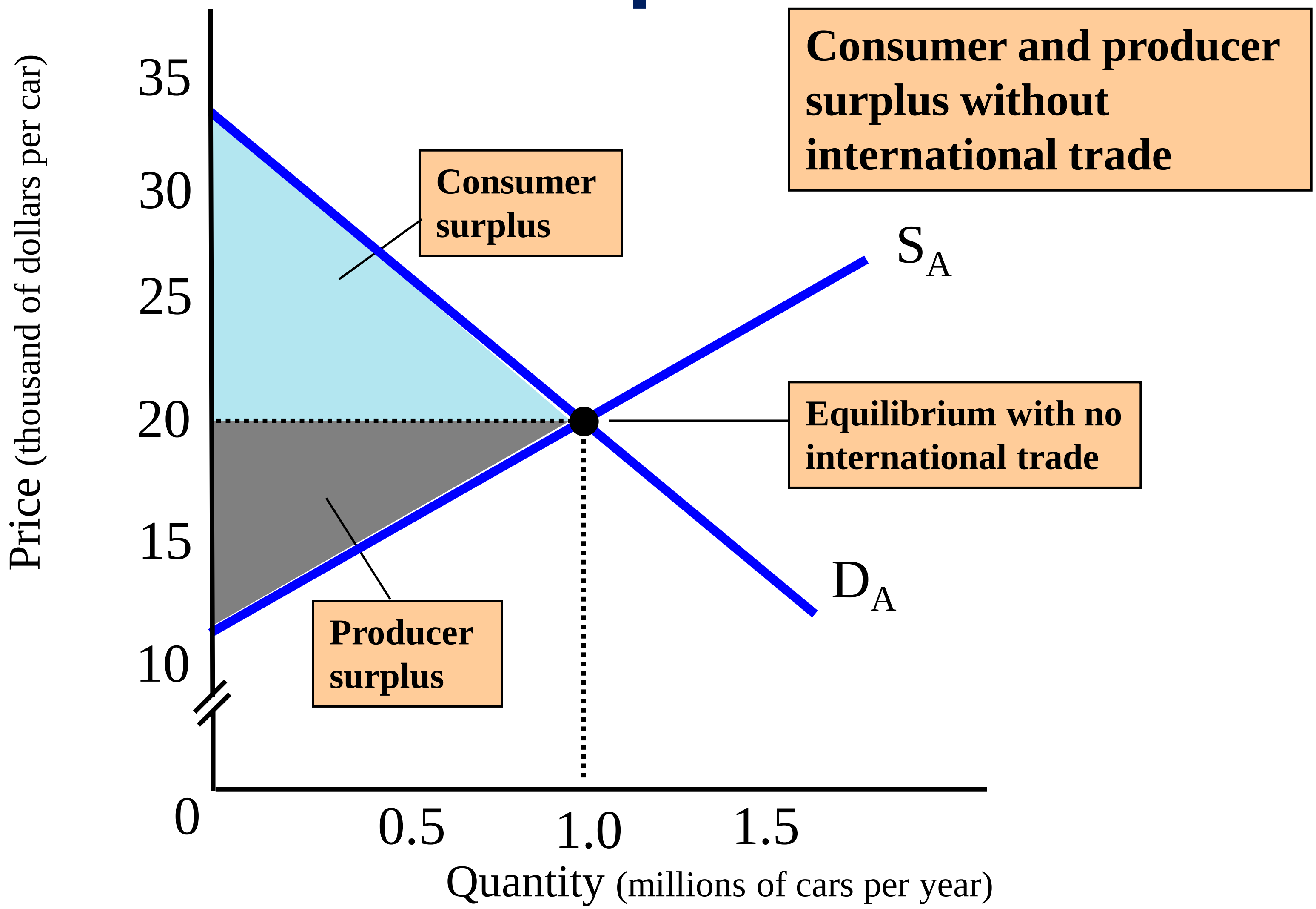


Markets and the Distribution of Gains and Losses

- Winners and losers in an import market
  - By comparing consumer surplus and producer surplus with imports and without imports, consumers gain and producers lose

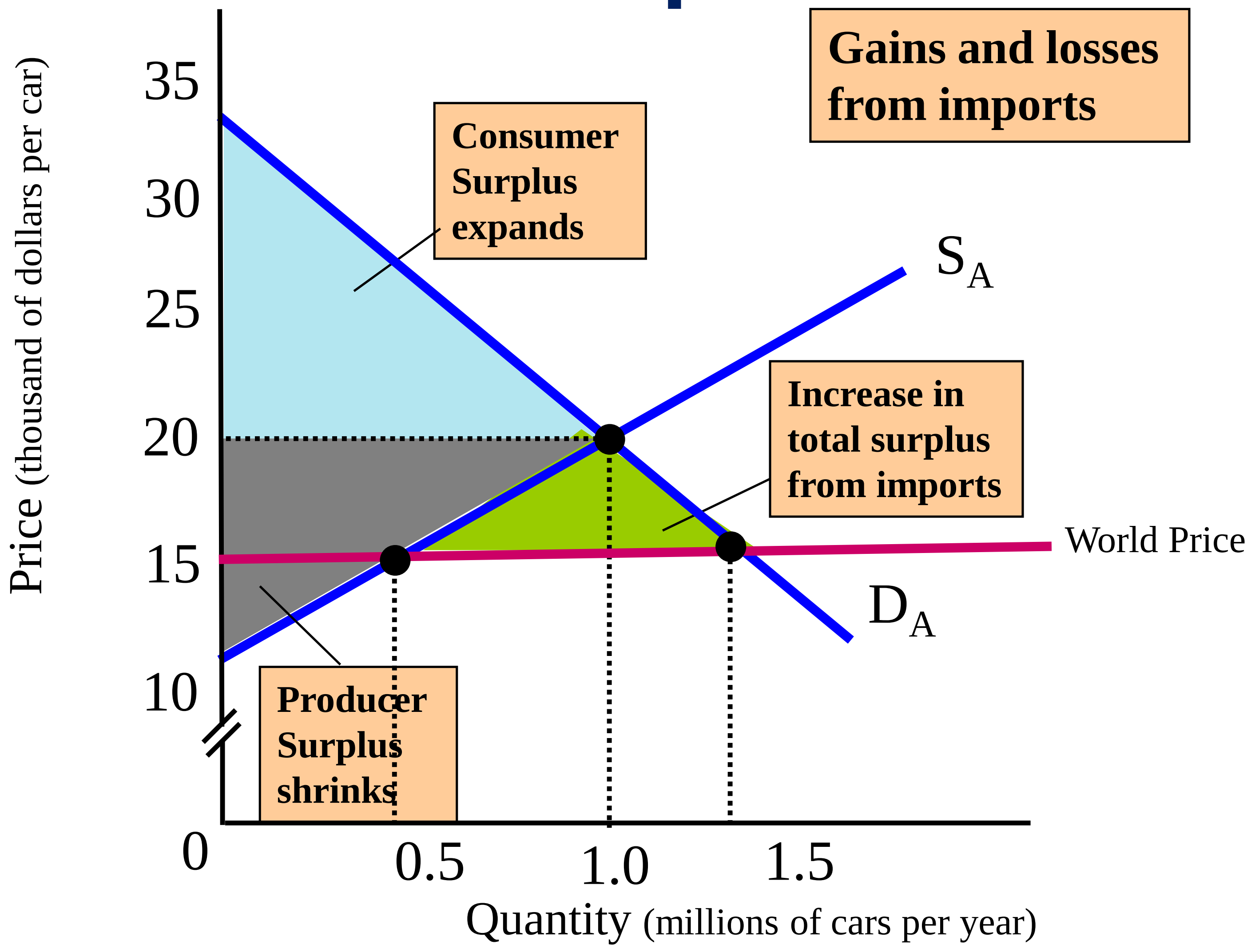
Gains and Losses in a Market With Imports

Figure 7.4(a)



Gains and losses in a Market With Imports

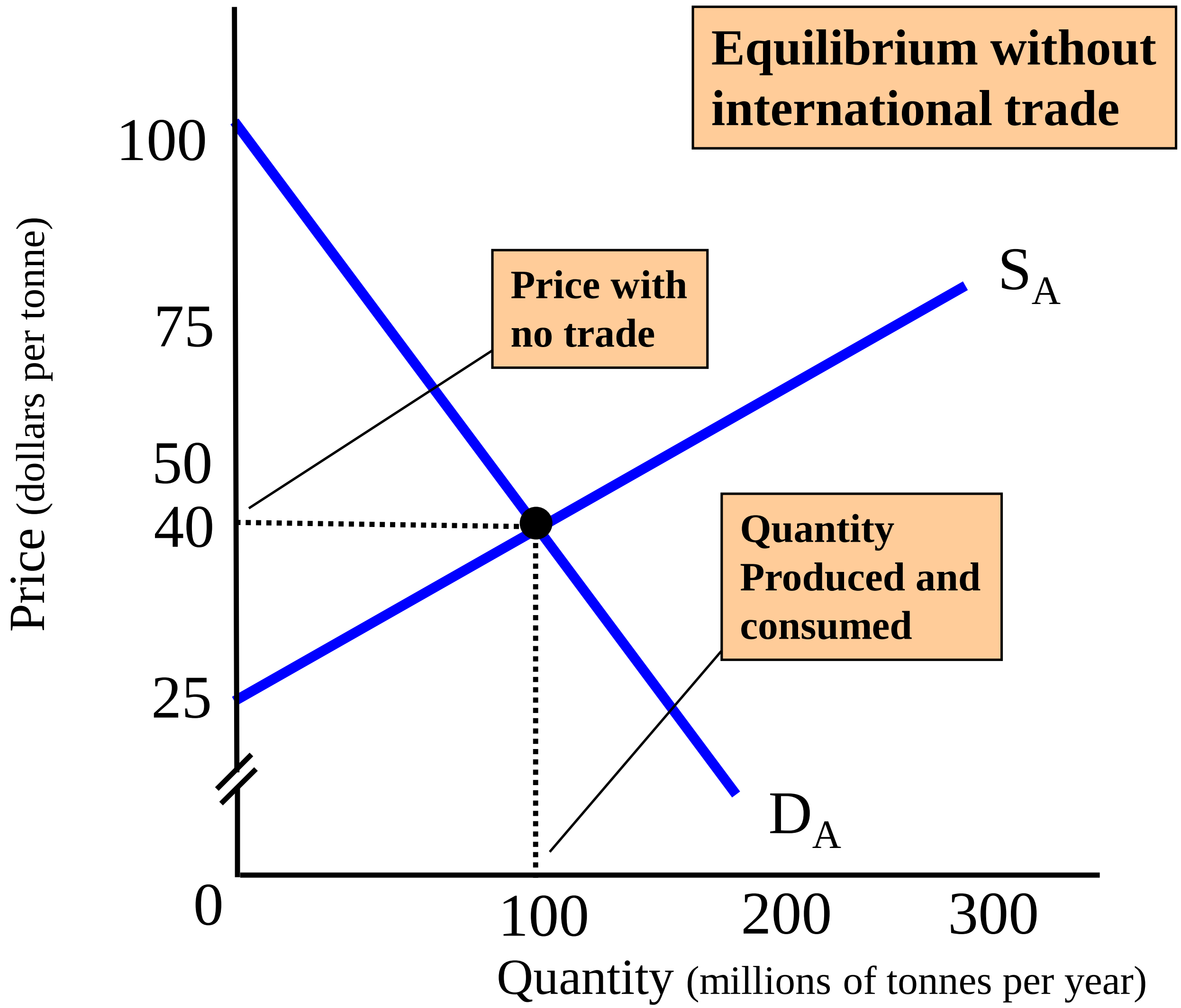
Figure 7.4(b)



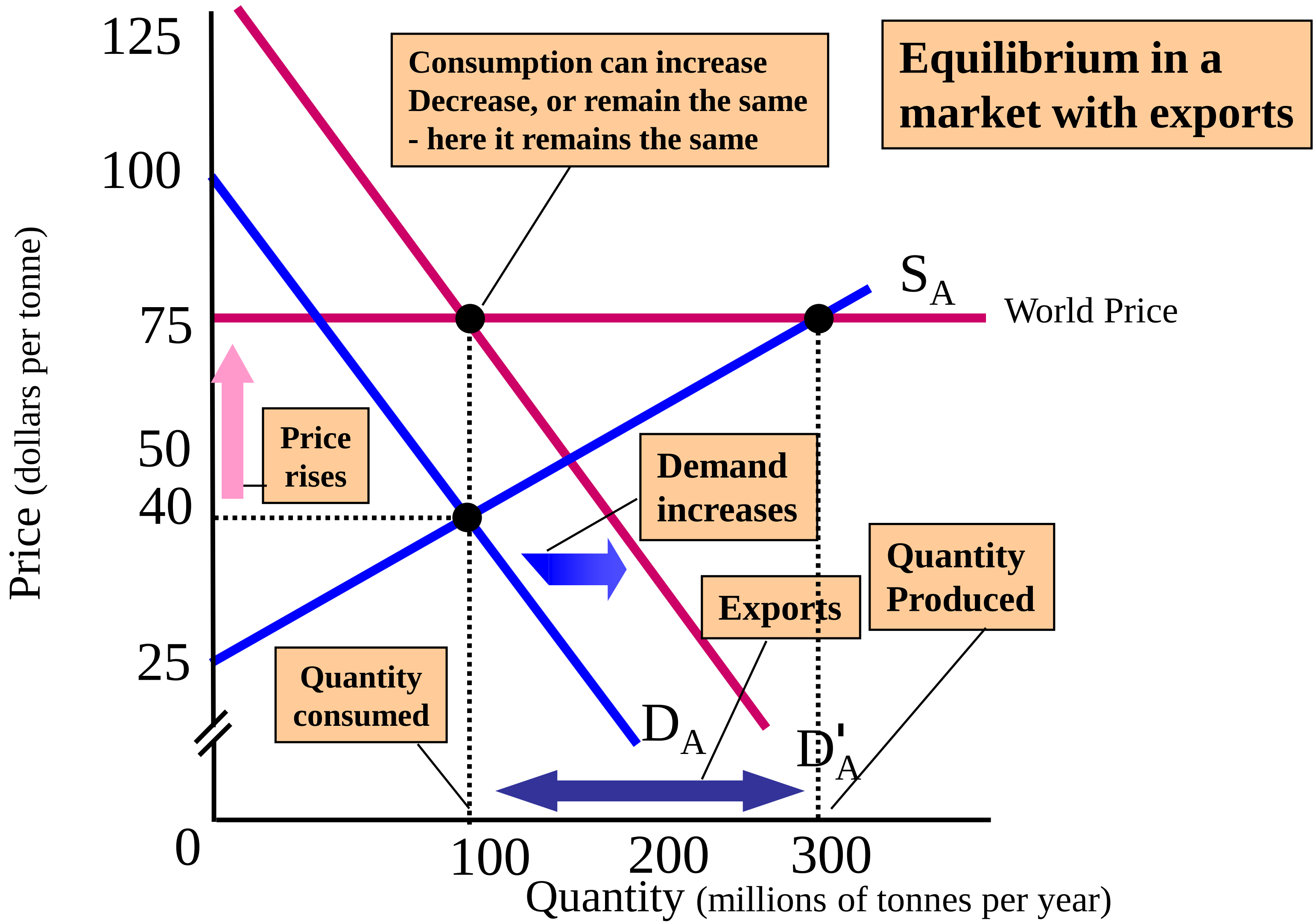
Markets and the Distribution of Gains and Losses

- An Export
  - Australia is an exporter in the market for coal because our costs of production are lower that the world price.
  - Equilibrium without international trade is illustrated in figure 7.5(a)
  - Equilibrium with international trade is illustrated in figure 7.5(b)

A Market With Exports



A Market With Exports

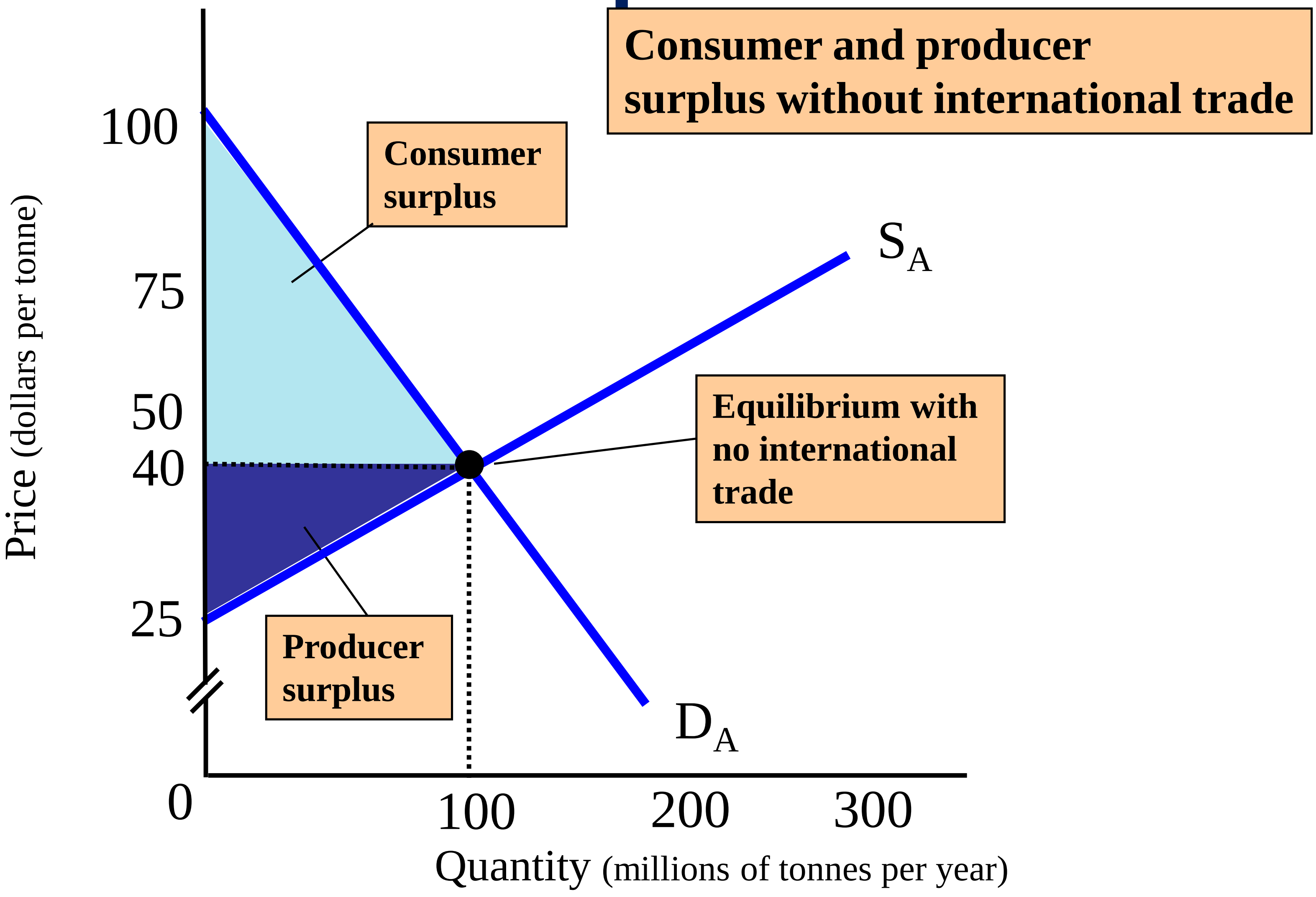


Markets and the Distribution of Gains and Losses

- Winners and losers in an export market
  - We can see who gains and who loses by looking at the changes to consumer surplus and producer surplus
  - Consumer surplus remains the same while producer surplus increases
  - Producers gain because they receive higher price, sell more and receive a larger producer surplus

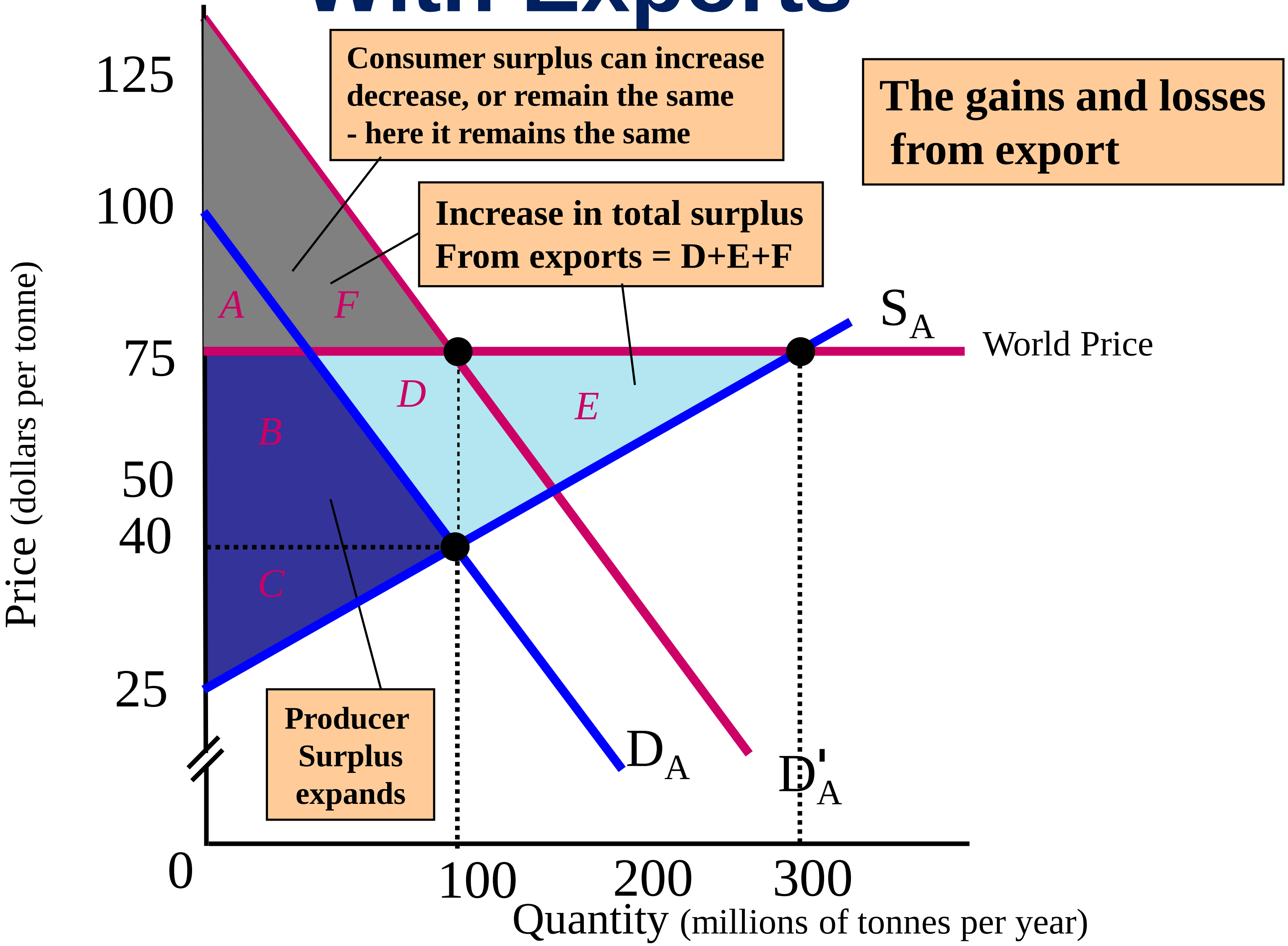
Gains and Losses in a Market With Exports

Figure 7.6(a)



Gains and Losses in a Market With Exports

Figure 7.6(b)



International Trade Restrictions

– Governments restrict international trade to protect domestic producers from competition by using three main tools:

1. Tariffs
2. Subsidies
3. Quotas

International Trade Restrictions

- A **tariff** is a tax that is imposed by the importing country when an imported good crosses its international boundary.
- A **subsidy** is a payment made by a government to a domestic producer based on the quantity produced
- A **quota** is a limit on the quantity of a good that may be imported
- Today we will explore tariffs and quotas

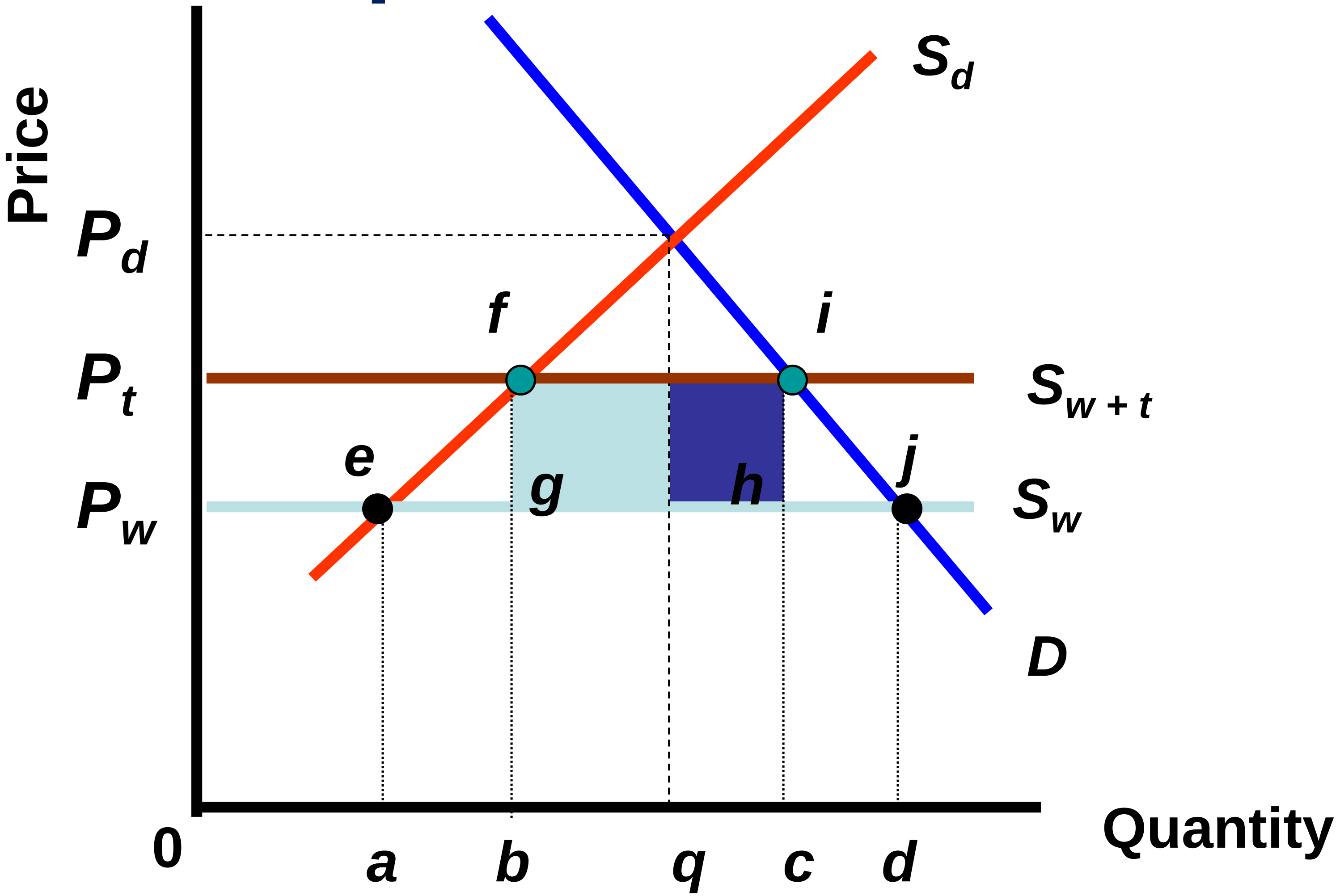
International Trade Restrictions

- When Australia imposes a tariff on car imports:
  - The price of a car in rises.
  - The quantity of cars imported decreases.
  - The government collects the tariff revenue.
  - Producer surplus increases.
  - Consumer surplus decreases.
  - Total surplus decreases – a deadweight loss

International Trade Restrictions

- How subsidies work
  - A subsidy works just like a tax, but in the opposite direction.
  - A subsidy shifts the supply curve rightward, lowers the price, increase the quantity, and creates a deadweight loss from overproduction
  - If a subsidy is granted on an export or an import it changes the amount of international trade

Impact of Tariffs



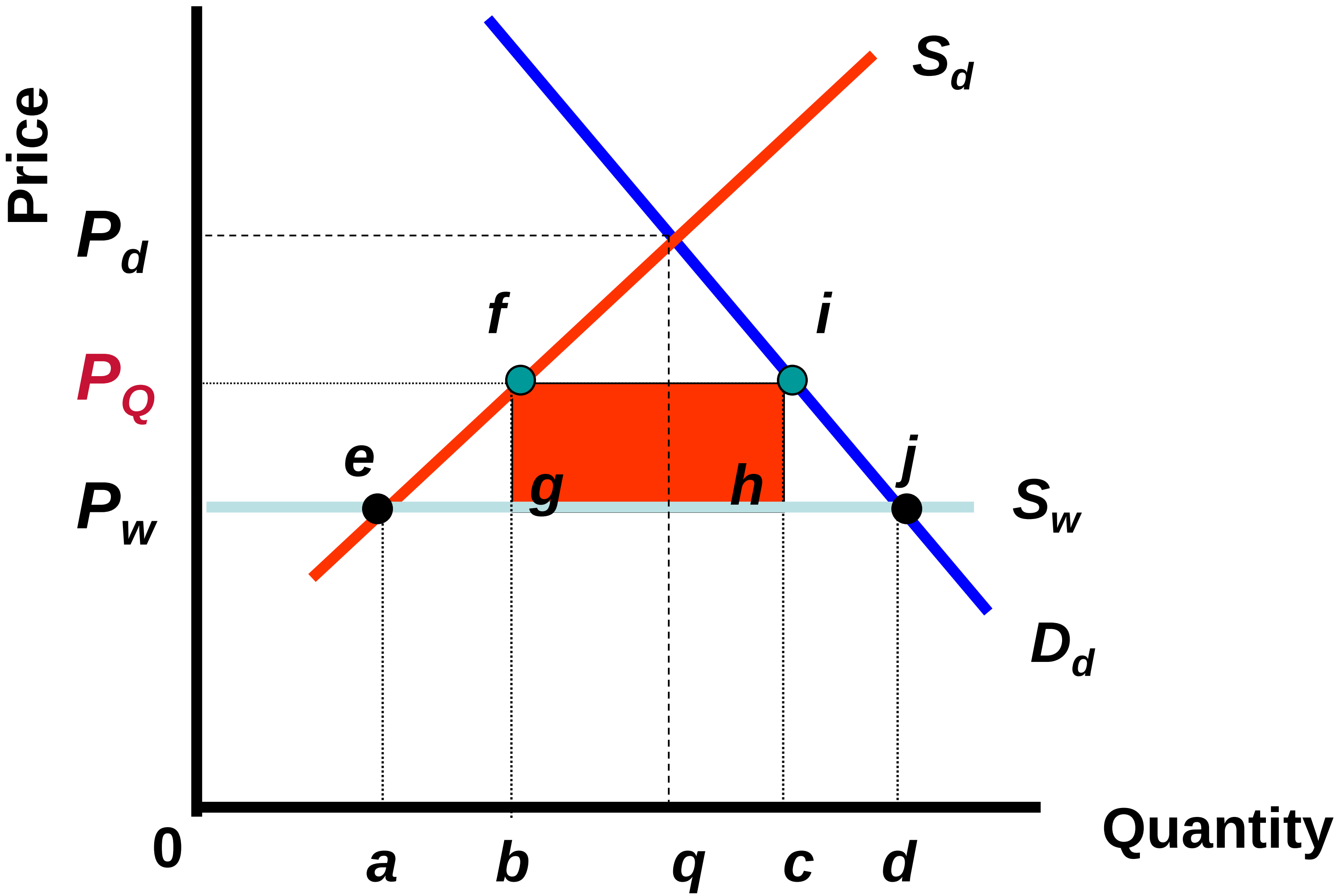
Impact of Tariffs (cont.)

- Consumption loss
  - a measure of the benefit lost to consumers that is not captured by other elements in society
- Production loss
  - the value of production lost to society
- Deadweight loss
  - the reduction in the total level of welfare (or real incomes) across society due to tariff protection

Impact of Tariffs (cont.)

- Effects on foreign producers
  - income of foreign producers will fall
- Government revenue
  - the government gains by obtaining tariff revenue
  - tariff revenue is essentially a transfer of income from consumers to government and does not represent any net change in the nation's economic wellbeing

Impact of Quotas



Arguments for Protection

- Military self-sufficiency argument
- Increase domestic employment
- Diversification for stability
- Infant-industry argument
- Cheap foreign labour argument
- Anti-dumping
- To counter lax environmental standards