Econ 340
Lecture 6
Nontariff Barriers

Outline: Nontariff Barriers
• What Are NTBs?
• Quotas
  – Effects Equivalent to Tariffs
  – Who Gets the Rents
• Other NTBs
  – Tariff-Rate Quotas
  – Voluntary Export Restraints (VERs)
  – Variable Levies
  – Government Procurement Regulations
  – Customs Procedures
  – Standards
  – Unfair Trade Laws
  – Export taxes
• Subsidies

What Are NTBs?
• What Are They?
  – Any institutional or policy arrangement that interferes with trade, other than tariffs
  – Term NTB is also used more broadly to include policies that artificially expand trade
    • e.g., Export subsidy
  – Sometimes called “Nontariff Measures” (NTMs)
• Main Types of NTB
  – See outline above

Quotas
• Definition: An import quota is a direct restriction on the quantity of an import
  – E.g., US might limit the imports of steel to some number of tons per year
  – Until Jan 1, 2005, US and EU had elaborate import quotas on many textile and apparel products from developing countries
  – We still have quotas on many agricultural products, e.g., sugar, cheddar cheese, dried milk, etc

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Quotas

• Effects of a quota
  – If permitted quantity is above what would be imported anyway, then no effect at all. (True only with perfect competition)
  – Otherwise, quota creates scarcity and raises price
  – Quota raises domestic price above world price
    • For market to clear, domestic price must rise to the point that desired imports equal the quota
    • See this with supply and demand
    • But first note example of US quota on sugar..

Effects of a Quota: Small Country

\[ \text{Suppose quota limits imports to this amount} \]

Quota

Thus price is…

"Tariff Equivalent"

Note that US price stayed mostly above the world price, and was more stable

But when world price spiked, then US price was
  – just equal to the world price,
  – not above as it would have been with a tariff

http://public.wsu.edu/~hallagan/Econ3327/week5/week5/Sugar/Sugarquota301.html
Effects of a Quota: Small Country

• Results
  – Suppliers gain area $+a$
  – Demanders lose area $-(a+b+c+d)$
  – Somebody gets area $c$, but who?
• Area $c$ is called “quota rents”
  – It is the profit from buying at world price, $P_W$, and selling at higher domestic price, $P_D$

Effects of a Quota: Rent Seeking

• “Rent Seeking”
  – Defined as the use of resources in effort to get rents
  – Examples
    • Faster (thus more costly) transport to win race to border for 1st-come-1st-served quota
    • Lobbying legislators to get quota allocations
    • Inefficient production intended to get quota allocations based on market shares

Effects of a Quota

• Effects of quota compared to tariff
  – Effects on price and quantity at a given time are the same
    • Hence “tariff equivalent”
  – Effect on welfare is different if quota rents are lost to rent seeking and/or accrue to foreigners:
    • In that case, importing country loses more from quota than from equivalent tariff
• What if country is large?
  – Picture is also same as for tariff
  – But if quota rent is lost or goes to foreigners, importing country cannot gain
Effects of Quota: Large Country (if Rent given to foreigners)

Summary:
- Domestic Country:
  - Suppliers gain $a'$
  - Demanders lose $-(a' + b' + c' + d')$
  - Net effect on country $= -(b' + c' + d')$
- Foreign Country:
  - License holders gain $(c' + e')$
  - (Suppliers/Demanders also lose)

Effects of a Quota

- Other effects of a quota
  - Quality upgrading
    - Limited to a fixed quantity, foreign exporters seek higher value by improving quality and charging higher price
  - Like a tariff, quota may induce foreign firms to produce here
  - Unlike a tariff, the quota becomes more restrictive if foreign supply increases or world price drops

Effects of a Fall in World Price

- Many things do not change:
  - Domestic price
  - Domestic quantity supplied
  - Domestic quantity demanded
  - Quantity of imports (fixed by quota)
- What does change?
  - Tariff equivalent increases
  - Rents from quota increase

Effects of a Rise in World Price

- If the rise is small, this is just the reverse of what happened with a fall in world price
- But if the rise in world price is large enough, then
  - The quota ceases to be binding
  - Tariff equivalent of quota becomes, and stays, zero
  - Domestic price becomes
    - Equal to world price, and
    - Rises with it
  - This last is what we saw in the graph of the price of sugar

http://public.wsu.edu/~hallagan/Econ3327/weeks/week5/Sugar/Sugarquota301.html
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Effects of a Rise in World Price

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Other NTBs:
Tariff-Rate Quota (TRQ)

• This is two tariffs, separated by a quota
  – Low (or zero) tariff applies to imports below the quota
  – High tariff applies to imports above the quota
• Used by US on many agricultural products
• Effect is like
  – a low tariff,
  – a quota,
  – or a high tariff,
  depending on levels of supply and demand

Other NTBs:
Voluntary Export Restraint (VER)

• Restriction of exports
  – At request of importing country
  – Usually specified as maximum quantity
• This was the major form of protection for the US auto industry in the 1980s: US persuaded Japan to limit exports of cars to US
• Illegal since 1995 under WTO rules
  – But how to enforce
  – There were examples in 2012 that look like VERs
  – Now the US has gotten S. Korea to limit its exports of steel
  – It look like VERs are back, but may not be called that
• Effect is exactly like a quota allocated to foreigners

Other NTBs:
Variable Levies

• A tariff that is changed as necessary to keep domestic price at a specified level
• These are used extensively by the European Union as part of its Common Agricultural Policy (CAP)
• Effects are same as a tariff, except for behavior over time

Other NTBs:
Tariff-Rate Quota (TRQ)

• This is what Trump used against imports of solar panels and washing machines
Other NTBs: Government Procurement Regulations

- Government favors domestic suppliers in buying goods and services
  - Buys only from domestic firms,
  - Buys from domestic firms unless imports are, say, 10% cheaper
- US used to have a “Buy American” law
  - Some say we need it again, but would violate WTO
- Effect is like a tariff, except that loss to demander is now loss to government and thus taxpayer

Other NTBs: Government Procurement Regulations

- “Buy American” was part of the Stimulus Package of the US in 2009
  - Congress would have imposed broad restrictions
  - Obama got them to restrict only when not contrary to US commitments under trade agreements
  - Even so, result was broadly restrictive, because purchasers were not sure of rules, so avoided imports
  - Result was also that other countries included similar provisions in their stimulus packages
  - See reading by Hufbauer and Schott.
- “Buy American” was said in President Trump’s Inauguration Speech, Jan 20, 2017

Other NTBs: Government Procurement Regulations

- Not just in US. There is an increasing use of “Buy Local” requirements by US and other governments
  - See Economist, “Buying local is more expensive than it looks”
  - The share of imports covered by buy-local requirements has increased five-fold since 2009
  - But... they increases costs, just like tariffs, without any tariff revenue

Other NTBs: Customs Procedures

- All countries have customs procedures for maintaining border security and collecting tariffs
- They become NTBs when
  - Excessive difficulty, or red tape, limits imports
  - Rules impose artificially high valuation for ad valorem tariffs

Other NTBs: Standards

- All countries also have standards, for
  - Health and safety (e.g., no lead paint)
  - Compatibility (e.g., 110 volt appliances)
- They become NTBs when biased against imports in
  - Substance of the requirement
  - Procedures for certifying compliance

Other NTBs: Unfair Trade Laws

- The (legal) threat and use of
  - Anti-Dumping Duties
  - Countervailing Duties
- We’ll say more about this later, in lecture about U.S. Trade Policies
- These are NTBs if
  - “Unfair trade” is actually normal trade (it usually is)
  - The threat of action discourages trade, even when duties are not levied (the “chilling effect”)
Other NTBs: Unfair Trade Laws

- Use of these laws is increasing rapidly by other countries. See Lindsey and Ikenson
  - In 1990s, antidumping use increased 50% over the '80s.
  - Developing country AD cases:
    - 7 in 1980-87
    - Over 700 in 1995-2000
    - US (323), EU (143) (out of 976 total)
  - Targets of AD cases (1995-2000, per year):
    - Leading: China (179), Japan (78), US (65)
    - Developed countries 355; Developing countries 656

Other NTBs: Temporary Trade Barriers (AD, CVD, etc.)

- Use of Temporary Trade Barriers, 1997-2013

Other NTBs: Export Taxes

- Simply a tax on exports, analogous to tariff on imports
  - Effects are similar
  - Not common, until recently, because countries think exports are good
  - Became common in mid-2008, as high world prices for agriculture led food exporters to protect their own consumers
  - Also used recently by China on certain minerals used in high-tech devices

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Subsidies

- Government assistance to producers
  - Export subsidy: paid only for exports
  - Domestic subsidy: paid for all production (but still increases exports or reduces imports)

- Effect on the subsidizing country
  - In competitive industries, country loses
  - Subsidies usually are intended to benefit producers, not country
  - In non-competitive industries, result may be different (recall Boeing-Airbus example)

Effects of a Subsidy on Foreign Countries

- Effect, if country is large, is to reduce the world price of the exported good
- Subsidy expands supply in subsidizing country (which is part of $S_W^0$)

In both cases
- Foreign suppliers lose
- Foreign demanders gain
- Net effect on countries depends on
  - Whether they are net importers or exporters
  - Thus whether price change is improvement or worsening of their terms of trade

Optimal policy response for foreign countries
- Importers: Write "thank-you note" (Krugman)
- Exporters: Not much they can do
Subsidies: Are They Used?

• YES!!
• US, EU, Japan all have large subsidies on many agricultural products
• These reduce world prices and hurt producers of these products in developing countries
• Examples of US subsidies and whom they hurt:
  – Corn: Mexico
  – Sugar: Caribbean countries
  – Cotton: Certain African countries

Next Time

• Reasons for Protection
  If tariffs are such a bad idea, why are they used?