
CA FOUNDATION JUNE 2024
रामबाण
SUPER REVISION SESSIONS
Chapter – 9
INTERNATIONAL TRADE
Business Economics
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Chapter 9

International Trade → 5 units

Topic: Theories of International Trade

(1) The Mercantilists' View of International Trade → Export ↑

(2) The Theory of Absolute Advantage → Adam Smith

(3) The Theory of Comparative Advantage → Ricardo

(4) The Heckscher-Ohlin Theory of Trade → Factor Endowment

(5) New Trade Theory - An Introduction

① Economies of scale

② Network Effect

X — Specialise — Y

100

50

Same resources

high quantity

Absolute Advantage

14

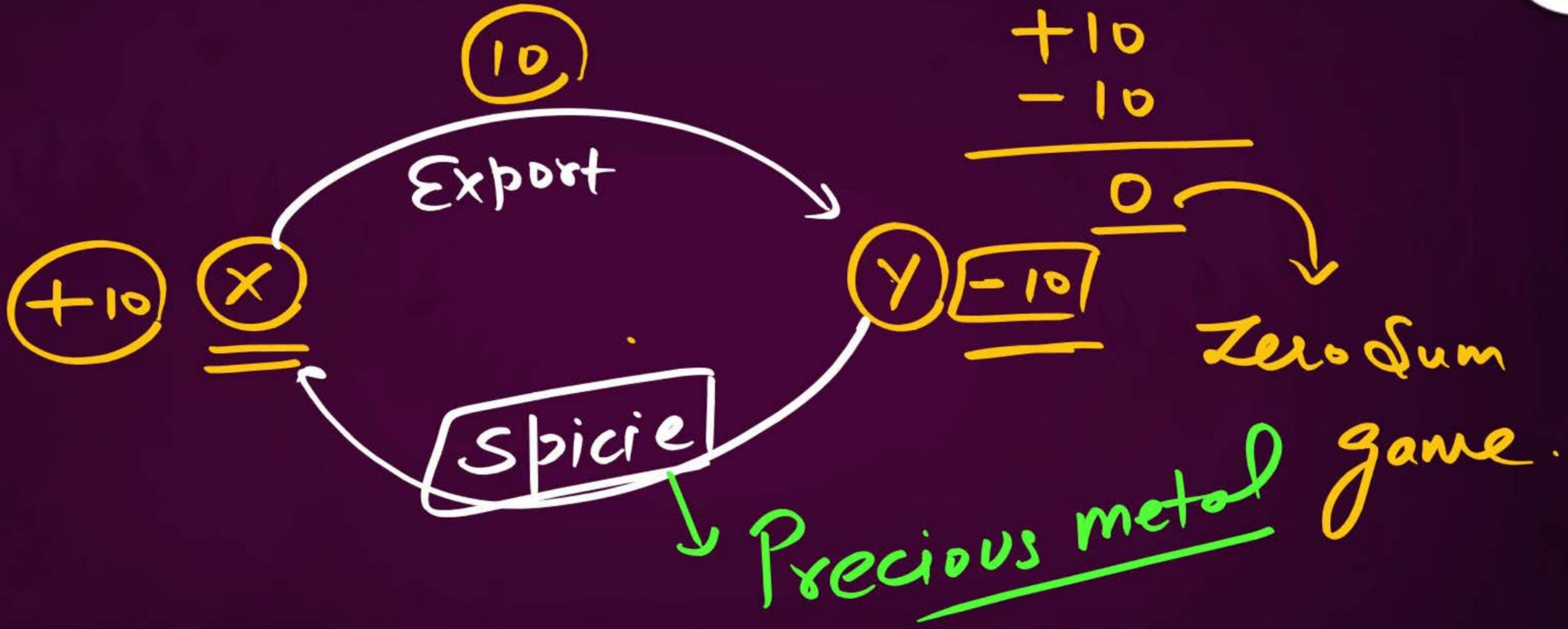
	X	Y
A	$\boxed{10}$	~~4~~
B	~~5~~	6

14

	X	Y
A	10	8
B	15	6

Ricardo

Comparative


10
Export
+10
X
Y
-10
Spicie
Precious metal
+10
-10
0
Zero sum game.

QUESTION

CA

#Q. What was the primary objective of mercantilism?

A Maximizing imports

B Maximizing exports B

C Encouraging free trade → Trade without Tariff

D Minimizing government intervention

QUESTION

CA

#Q. According to mercantilism, trade is viewed as:

A) A cooperative endeavor

B) A zero-sum game

C) Beneficial for all parties involved

D) Irrelevant to economic growth

B

$\boxed{H-O}$

Factor Abundant

$CIT \Longrightarrow \underline{\underline{C\uparrow}} \longrightarrow \underline{\text{Export}}$

$LIT \Longrightarrow L\uparrow \longrightarrow \underline{\underline{\text{Export}}}$

China

mobile

USA

iphone

Similar goods

Tariff

USA

import

$100 + 40 \rightarrow 140$ — Expensive

India

Q=1

X — 100 → per unit fixed Tax ⇒ ₹5/unit

Specific Tariff

Import

% 10% ⇒ ₹10

₹500 → ₹50

Ad-velorom Tariff

17 Types

Topic: Types of Tariffs

(1) **Specific Tariff-** It is **fixed amount of money** per physical unit or according to weight or measurement of commodity imported or exported.

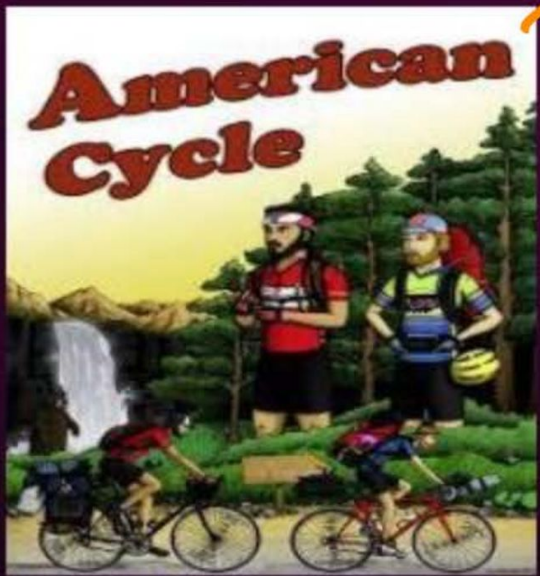
(2) **Ad Valorem Tariff-** When duty is **levied as fixed percentage of value of traded commodity.**

A 30% ad valorem tariff on any American cycle.

This tariff **preserves protective value** of tariff on home producer, but it **gives incentives to deliberately undervalue good's price on invoices** to reduce tax burden.

$\boxed{5000} \rightarrow 20\%$

$\boxed{1000}$



5000

$\boxed{1000}$ — specific Tariff

10% Adveloram

$\boxed{1000}$ — whichever is higher → Mixed Tariff

500

1500 → Compound Tariff

(3) **Mixed Tariffs-** They are expressed **either** on **basis of value** of imported goods (an ad valorem rate) **or** on **basis of a unit of measure** of the imported goods (a specific duty) whichever is higher.

For Eg, duty on American cycle : 10% ad valorem or Rs. 4000 fixed tax, whichever is higher.

1000

$\boxed{10{,}000}$

(4) **Compound Tariff-** It is generally calculated by **adding up a specific duty** to **an ad valorem duty.**

Thus, on an import with quantity q and price p, a compound tariff collects a revenue = $\boxed{t_s q + t_a pq.}$

Cycle → $\boxed{q = 5}$, $\boxed{P = 1000}$, $t_s = 100$, $t_a = 5\%$

Specific tariff $= 100 \times 5 \Rightarrow \boxed{t_s . q}$

$= 500$

750

Ad-veloram $= \boxed{t_a \times p.q.}$

$= 5\% \times 1000 \times 5 = \frac{5}{100} \times 5000 = 250$

(5) **Technical/Other Tariff-** These are calculated on the basis of the **specific contents of imported goods** i.e. **duties are payable by its components** or related items.

For Eg- **Rs. 10000** on **each E-rikshaw** plus **Rs. 100/per kg** on battery.

iphone ⇒ 100 ⇒ ₹5

= 105

Charger → 10 → ₹1

₹6

USA

Liquor

$\boxed{Q=2} \Rightarrow$ No Tariff $\rightarrow$ low

$\boxed{Q=3}$

$\boxed{Q=1} \Rightarrow$ 50%

(6) Tarrif Rate Quota- It combine two policy instruments quotas and tariffs , where Imports entering under specified quota portion are subject to lower or zero tariff rate and Imports above quantitative threshold of quota face a much higher tariff.

↓

Extra quantity

China

5000

\+ 1500

India

6500

import + $\boxed{}$ = domestic cycle

Variable Tariff

(7) **Most-Favoured Nation Tariffs-** Import tariffs which **countries promise to impose on imports from other members of WTO,** MFN rates are the **highest** that **WTO members charge each other.**

(8) **Variable Tariff**- A duty typically fixed to **bring the price of an imported commodity up to level of the domestic support price** for the commodity.

WTO → Geneva

15%

Maximum

Tariff

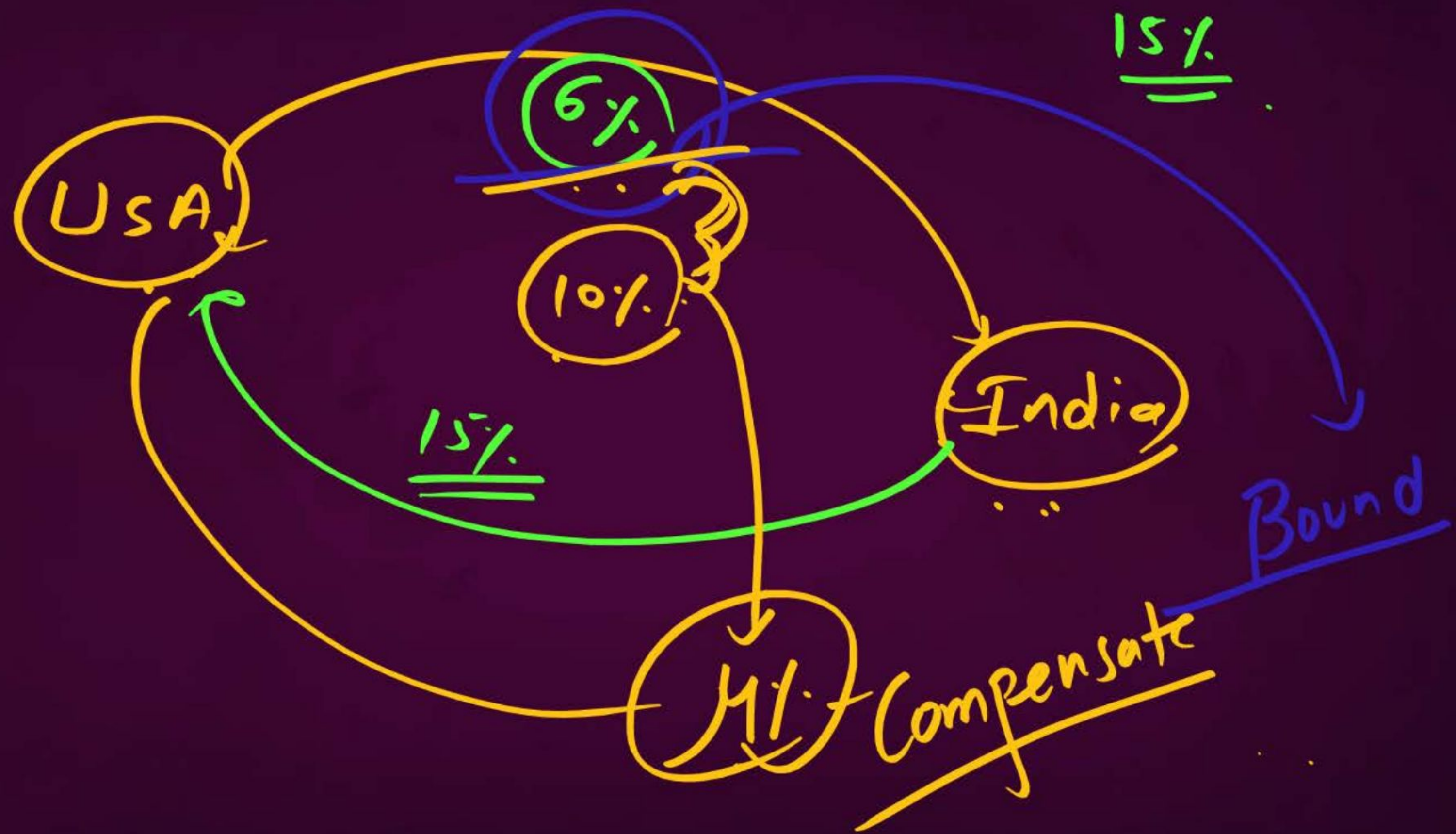
164 members

Most Favoured Nation

MFN

(9) **Preferential Tariff**- Countries promise to give another country's products **lower tariffs than their MFN rate.** These agreements are **reciprocal,**

15%


USA
6%
10%
15%
India
15%
Bound
M%
Compensate

(10) **Bound Tariff-** A WTO member **binds itself with legal commitment not to raise tariff rate above a certain level** (maximum level of import duty). A member is always **free to impose a tariff that is lower** than bound level. Once bound, a tariff rate becomes permanent and a member can only **increase** its level **after negotiating with its trading partners and compensating them for possible losses** of trade.

MFN → 15%

Preferential → 10% → Reciprocal

Bound → One way → 6%

Applied Tariff

(11) Applied Tariffs- Duty that is actually charged on imports. Applied tariff should not be higher than the bound level.

Mobile → Tariff

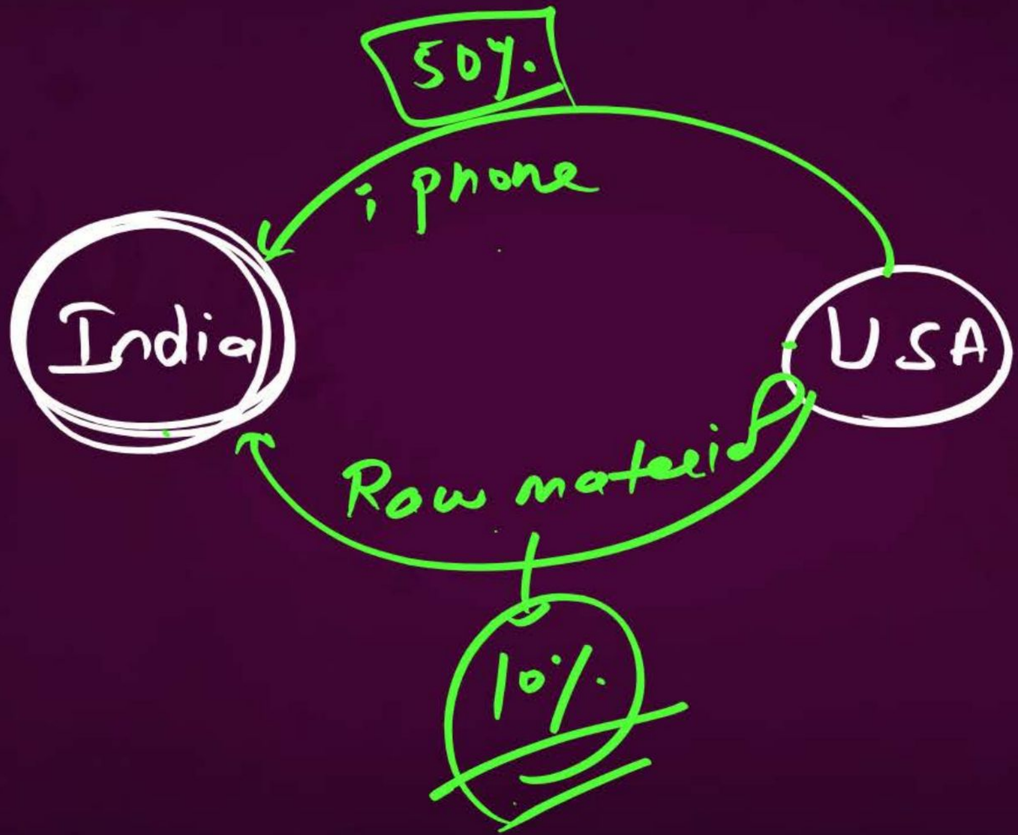
Charger → Tariff

Technical Tariff

Main Product → 10%

Raw Material → 2%

Escalated

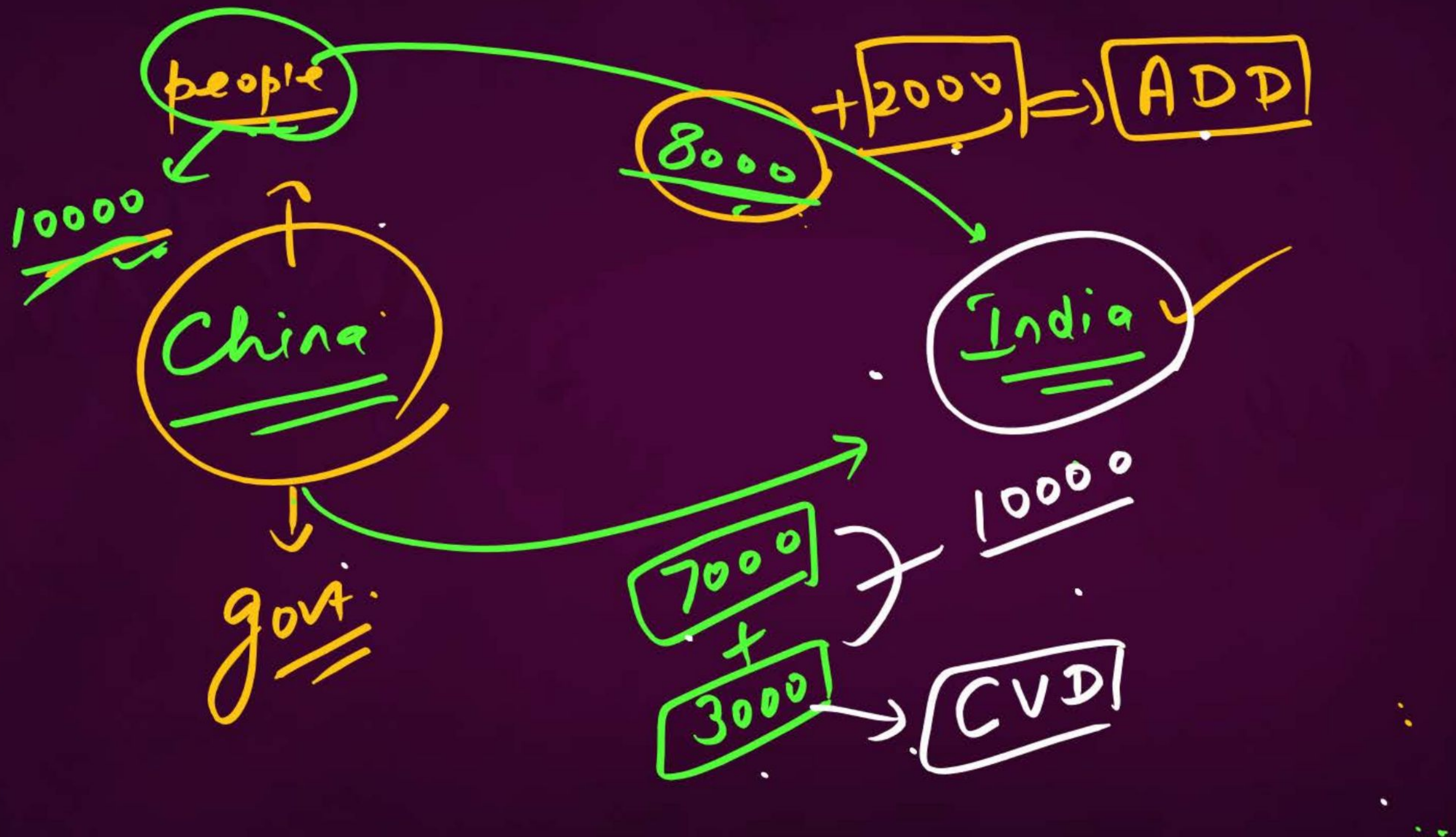

50%
iphone
India
USA
Raw material
10%

(12) **Escalated Tariff-** Tariff **rates on imports of manufactured goods** are higher than tariff **rates on intermediate inputs like raw materials.** For example, a 5% tariff on raw material of cycle and 10% tariff on American cycle. This type of tariff is **discriminatory** as it **protects manufacturing industries in importing countries** and **adversely affects industries of exporting countries.**

(13) Prohibitive tariff - It is set so high that no imports can be done.

Ban

(14) Import subsidies- It is simply a **payment per unit or as percent of value for importation of a good** (i.e., a negative import tariff)


people
10000
China
govt.
8000
+ 2000
ADD
India
10000
7000
+
3000
CVD

(15) Tariffs as Response to Trade Distortions- **Countries affected by 'unfair' foreign-trade practices, respond** quickly by measures in the form of **tariff responses to offset the distortion.** (it is also known as "trigger-price" mechanisms)

(16) **Anti-dumping duty(ADD)** - It is a **protectionist tariff** that a domestic govt. imposes on **imports** that it believes are **priced below fair market value.**

(17) **Countervailing duties-** It is charged in an importing country to **offset/remove advantage that exporters get from subsidies** (from their govt.).

Topic: Regional Trade Agreements (RTAS)

RTAs are defined as **groupings of countries** (not necessarily belonging to the same geographical region), which are formed with the **objective of reducing barriers to trade** between member countries.

RTA

Topic: Type of RTAs

Types of RTA

- Unilateral Trade Agreements
- Bilateral Agreement
- Regional Preferential Trade Agreements
- Trading Bloc
- Customs Union
- Common Markets
- Economic and Monetary Union

Topic: Type of RTAs

(1) **Unilateral trade agreements-** under which an **importing country offers incentives** to **encourage the exporting country** to **improve the exporting country's economy.**

Topic: Type of RTAs

(2) **Bilateral Agreements-** are agreements which set rules of trade **between two countries,** two blocs or a bloc and a country. These may be **limited to certain goods and services** or certain types of market entry barriers.

Bilatral

Topic: Type of RTAs

(3) **Regional Preferential Trade Agreements-** among a group of countries **reduce trade barriers on a reciprocal and preferential basis** for **only the members** of the group.

Topic: Type of RTAs

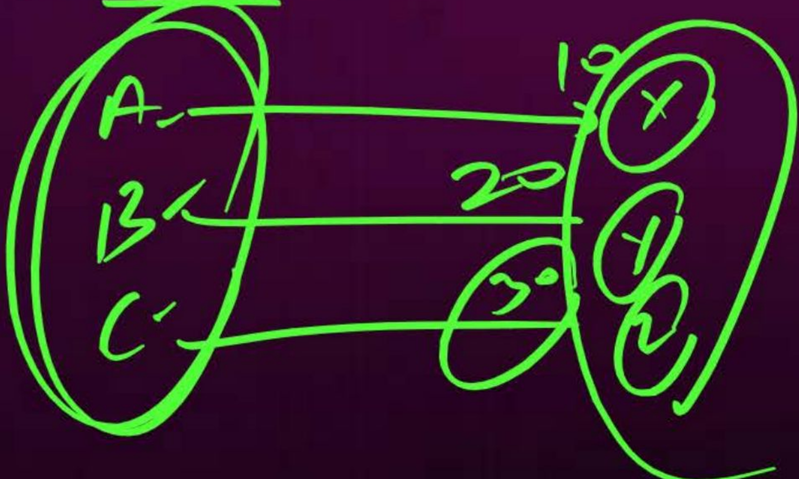
(4) **Trading Bloc**: has a **group of countries** that have a **free trade agreement** between themselves and may **apply a common external tariff to other countries.**

Example: Arab League (AL), European Free Trade Association (EFTA)

Topic: Type of RTAs

(5) **Free-trade area** is a **group of countries** that **eliminate all tariff and quota barriers** on trade with the objective of increasing exchange of goods with each other. Members **retain independence in determining their tariffs with non-members.**

Example: NAFTA



Topic: Type of RTAs

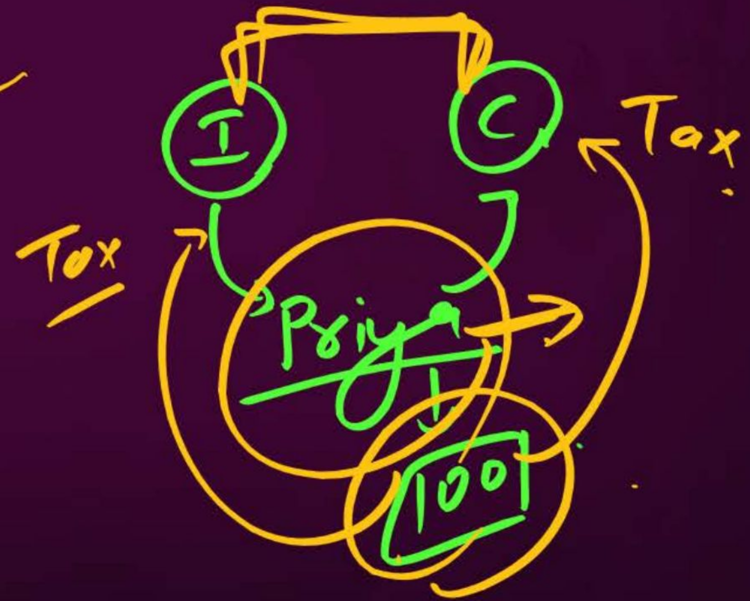
(6) **Customs union-** is group of countries that eliminate all tariffs on trade among themselves but **maintain a common external tariff on trade with countries outside the union** (thus, technically violating MFN).

Eg- European Union etc.

Trading Bloc = custom union

Custom Union

UK



Topic: Type of RTAs

(7) **Common Market-** It deepens a customs union by providing for the **free flow of output and of factors of production** (labour, capital and other productive resources) by reducing or **eliminating internal tariffs** on goods and by **creating a common set of external tariffs.** There are also **common barriers against non-members** (e.g., EU, ASEAN)

Topic: Type of RTAs

(8) **Economic and Monetary Union** - Here members share a common currency. Adoption of **common currency** also makes it necessary to have a strong convergence in macroeconomic policies. For eg, European Union countries adopt a single currency.

GATT → 1948

GATT → Goods

Goods
+
Service
+
IPR ⇒ WTO

1995

Topic: Structure of the WTO

1st Level (Top-Level)	Ministerial Conference	➢ It **takes decisions on all matters** under any of the multilateral trade agreements. ➢ It meets at least once every two years.
2nd Level	General Council	➢ It **meets several times a year** at the Geneva headquarters. ➢ It also meets as the **Trade Policy Review Body** and the **Dispute Settlement Body**.
3rd Level	Goods Council, Services Council and Intellectual Property (TRIPS) Council	➢ These councils **report to the General Council** & are **responsible for overseeing the implementation of the WTO agreements** in their respective areas of specialization.

Components of foreign capital flows

- Foreign aid or assistance
- Borrowings
- Deposits from non-resident Indians (NRT)
- Other investment

Topic: Meaning of FDI

FDI

$\boxed{10\%}$ > Equity

Subsidiary

Associate

FPI

Equity < 10%

Speculation

FDI may be categorized as

1. Horizontal Agreements
2. Vertical Agreements
3. Conglomerate Agreements
4. Two-way direct foreign investments

Car

Tyre

Car

Chole

Topic: Modes of Foreign Direct Investment (FDI)

Foreign direct investments can be made in a variety of ways, such as

(i) **Opening of a subsidiary** or **associate company** in a **foreign country.**

(ii) **Equity injection** into an overseas company,

(iii) **Acquiring a controlling interest in an existing foreign company. Mergers** and **acquisitions** (M&A)

(iv) **Joint venture** with a foreign company.

(v) **Green field investment** (establishment of a new overseas affiliate for freshly starting production by a parent company).

Topic: Modes of Foreign Direct Investment (FDI)

(vi) Brownfield investments (a form of FDI which makes use of the existing infrastructure by merging, acquiring or leasing, instead of developing a completely new one.

For e.g. in India 100% FDI under automatic route is allowed in Brownfield Airport projects.


Exam Paper
Thank
YOU