6. International Trade

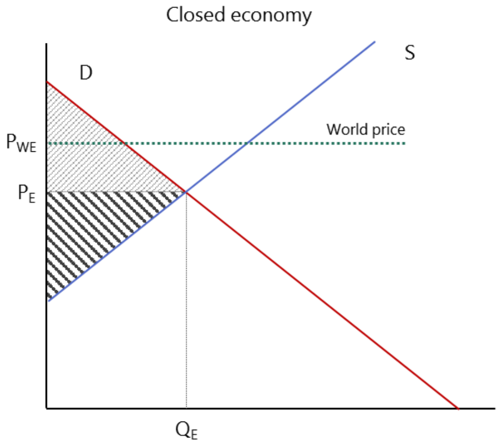
ECON1101 • KC Notes

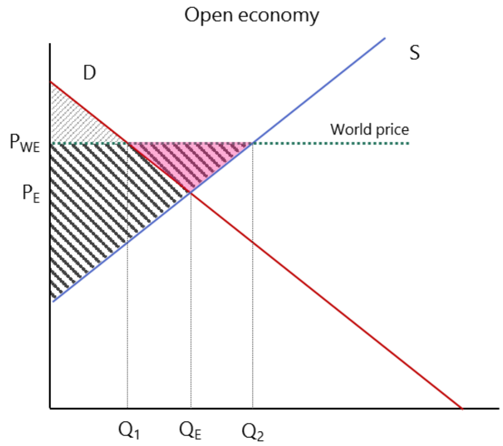
: Consumer surplus : Producer surplus : Gains in trade

- **<u>Small open economy</u>**: economy that participates in international markets but is **small enough that demand and supply do not affect the world price**
- **<u>World price</u>**: equilibrium price in the international market

6.1 Exporting Country

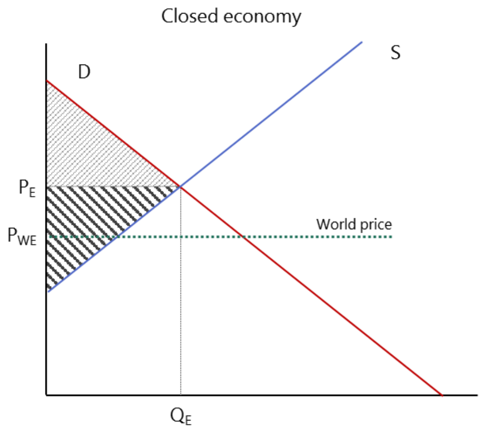
- **<u>Gains in Trade</u>**: extra total surplus in an open economy situation compared to a closed economy

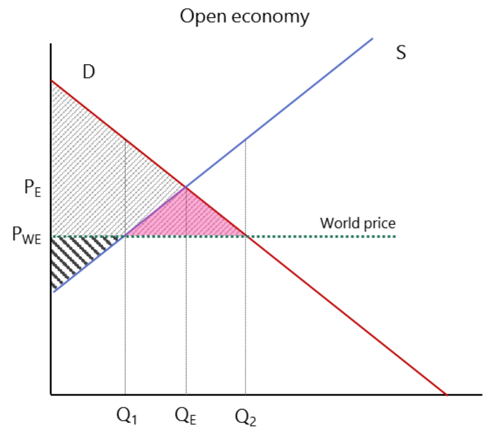




- Domestic producers are better off and **sell an extra $Q_2 - Q_1$ as exports**. They are sold to people who have a <u>relatively</u> high demand internationally; domestic consumers worse off

6.2 Importing country





- Domestic producers worse off, market imports of $Q_2 - Q_1$

6.3 Winners and Losers of International Trade

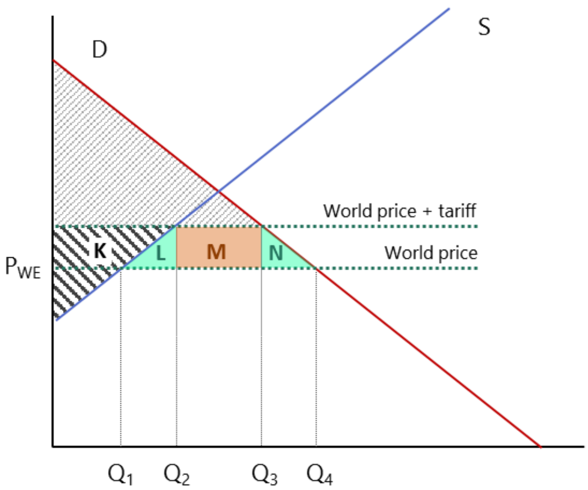
Winners	Losers
• Total surplus increases • Wider variety of goods • Economies of scale by selling to a larger market • Domestic monopolies and oligopolies face international competition and therefore their market power decreases • Better tech and ideas	• Consumers (when exporting), producers (when importing) •

6.4 Trade Restrictions

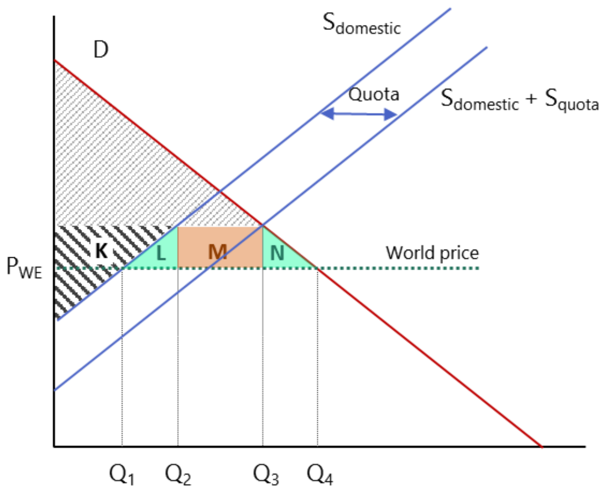
- **<u>Import Tariff</u>**: tax on imported goods and services
- Domestic consumers lose K, L, M and N
- Domestic producers gain K
- M is the tariff revenue (Quantity imported is now $Q_3 - Q_2$, from previous $Q_4 - Q_1$)
- L and N is DWL due to the tariff

- **<u>Import Quota</u>**: quantity limit on amount of goods and services imported
- Quota has the same effect on surplus as tariffs (if the same amount $Q_3 - Q_2$ is restricted)
- However, **revenue M could be for the book importers** as they can purchase books at international price and sell to consumers at world price.
    - Government can tax this revenue

Tariff



Quota



- World Trade Organisation has asked to convert trade restrictions to **tariffs** to encourage transparency and allows restrictions to be measured in percentage tariffs