**International Economics**

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**Module No. # 01**

**Lecture No. # 25**

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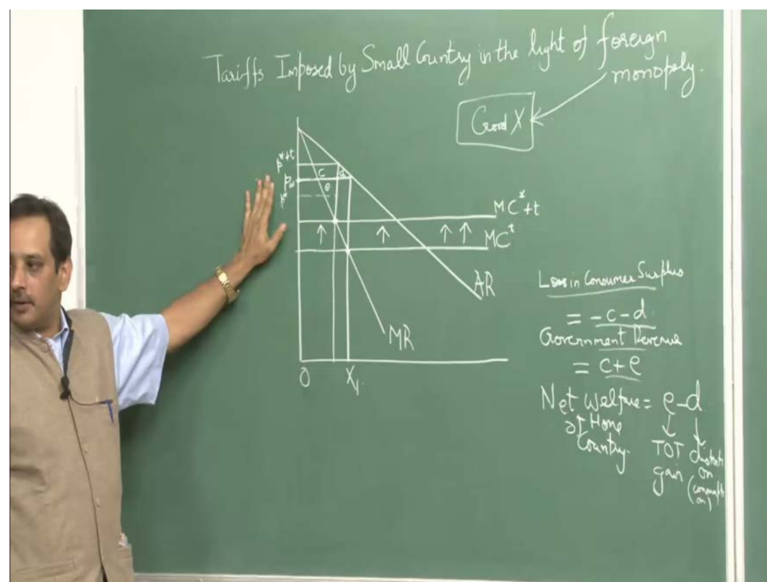


Good afternoon. Today we are back in discussing the impact of tariffs which are imposed by a country in the light of foreign monopoly. So, there is only one producer who is providing this product in this home country. There are no alternative goods there are no goods which are available domestically. It is only this foreign producer whose providing this product in this home markets. This is different from the cases that we have been discussing.

We have been discussing the case where, home country producers are perfect competitive firms. We have been discussing the case where, the home producer is has a home monopoly. This is the third case where this particular good is been provided by the foreign monopolists. So, there is no home producer of this good. It is only one producer who is a foreigner and he is the one who is providing this good.

So, then the demand curve that he faces is downward sloping and this is the marginal revenue curve; he has the fixed marginal cost curve. So, the price that will prevail in free trade is will be P W. Reason that, this is the marginal cost marginal cost cuts M R here. So, the prices prevail prices that prevail before tariffs are imposed is P W. So, this is the good x 1 is the good which is provided by the foreign monopolists. So, whatever is exported by these foreign monopolists become the imports for the home country.

Now, this country imposes tariffs. So, home country imposes tariffs when there is only one producer of that particular good who is a foreigner. It looks little odd that you impose a tariff when there is no domestic production of the same good. But, think allowed you can think of a case where say for example, you imposed tariffs on the good which is coming from abroad. So, there is no domestic production of that good. So, you do not have those intentions to promote domestic industry and deter competition and things like that.

You just want to impose tariffs you do not want to the foreign good to come in. So, for various reasons or maybe you want revenue or maybe if you are technically sound, then you think of saying that if tariffs are imposed, the terms of trade will improve. For various reasons you impose tariffs. You know what happens if the tariffs are imposed. The domestic price of that good goes up.

How would foreigners see it? The foreigners would see as leftward shift or an upward shift of their marginal cost curve why? Because, remember when we were discussing tariffs which were imposed by small or large country the export supply curve shifted to the left. The supply curve shifts to the left because if I am providing good to you impose tariffs. I would take it as a tax on me.

So, supply is a function of price of other goods technology taxes. So, those other factors are shift factors. So, the supply curve as the taxes go up that the supply curve shifts to the left. So, he has this marginal cost curve which shifts upwards because the taxes or the custom duties are imposed. So, then the new marginal cost curve cuts the M R here. So, the new prices are P star plus t, but, the domestic price do not rise by the amount of the tariffs. Because as in the earlier case, if you imposed tariffs and I want to supply goods to you and I find that my exports are coming down, I will reduce my prices just to enter your market because you are the one who is imposing tariffs.

So, I have to do something about my product I will reduce my prices. So, the increase in domestic prices is not equal to the amount of tariffs. So, then if that is so, the loss in consumer surplus is this minus c minus d because the prices earlier were P W now its P stars plus t. Government revenues c plus e. So, the net welfare is e minus d. So, as in the case of the case when the home country was large and it imposed tariffs, you got net welfare to be equal to e minus b plus d.

Here, it is e minus d only e minus d only; where e is the terms of trade gain d is the distortion the consumption distortion. So, for small tariffs you can have a positive impact on the welfare. So, the net impact the net welfare is when the tariffs are imposed by a country in the light of foreign monopolies ambiguous because this is the terms of trade gain, this is the distortion. You can have this to be positive or negative depending on what is the distortion, what is the term of trade gain.

Please recall this is different from the case when we were discussing dumping. Do you recall dumping? Dumping is a phenomenon when the foreign monopolist is again a foreign monopolist, but, he then sells the he sells the good in the foreign market at a price which is lower than the local price or at a price which is lower than the average cost. Do you recall? And still he makes profits because where he acts as a price discriminator, the same good is been provided in two different markets at different prices because the markets are segmented.

So, when Chinese find that Indian markets are elastic they will sell it at a lower price and they will sell the same product in their market in their own markets at a higher price. That is different from this there also it was a foreign monopolist, but, he was providing his products in two different markets.

Sir but, the world prices and the prices at which Chinese are supplying the good (( )) those are different means that would be different because it if they are imposing tariffs. So, the Chinese producer will reduce its prices. So, this (( )) moved it other means in distortion (( )).

Ah no, I into fully understanding the, is it in this context or is it in context of dumping? It is in this context.

(( ))

Chinese producer reducing its prices than that would be lower than the (( ))

Chinese if the Chinese producer reducing in the prices when he faces tariffs, it is starting of below the world prices because the small country cannot affect (( )).

Yeah

(( )).

Yeah

World price.

Yeah should does not affect. Do this activities effect the prices of the net welfare (( ))? This is the global net welfare.

No, this is the net welfare of this home country and because the foreigner sells at a price which is lower than P W, the prices of exports go down or the price of imports goes down. So, the home country terms of trade improves right now. Why is he selling at lower price because he impose the home country has imposed tariffs. Did I answer your question I am I am not sure whether I fully understood.

One of that means, one is the whole world demands from a r.

Well remember this, he is the only one who is providing this good in this market; see one only. So, this is the average revenue curve. So, you can say it world demand because it is in the home country that he faces a demand curve like this.

(( )), but, we can say that it intersection point is P world prices it means that we are taking world deposits. No, but, see he is the foreign monopolist who is in this home country say good x is not been produced. This is been provided by the foreign monopolist. So, what will be the demand curve that he will face in this country?

In this country, it will be a downward sloping demand curve because only by reducing prices he can increase the demand for that. So given this, you have a scenario which is similar to the case when the tariffs were imposed by the large country. When tariffs were imposed by the large country the terms of trade worked out to be e minus b plus d.

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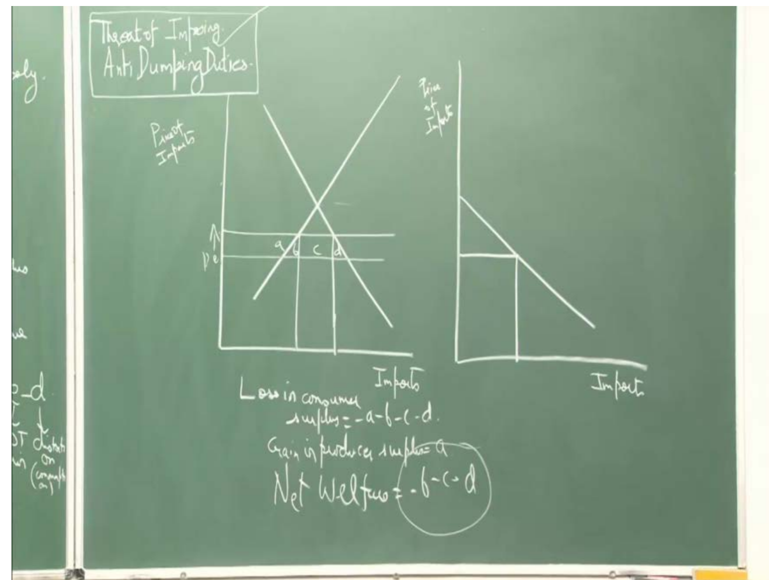


Now, let us go to

(No audio 12:13 to 12:51).

(( )) sir axis in the restoration world would (( )) P W or P star will it be P star in this. Now, in the rest of the world one would not know that it is P star because see this is a case where this person reduces the price in this market.

(( ))

For the domestic market because there is no one who is providing this product. What happens internationally one does not know because in this when you bring in imperfections. How are prices determined internationally one is not interested at all may be it is demand and supply, may be because of their imperfections. So, one does not know this is the price that he will charge in this market. So, that is.

(( )) first place P W plus t will be the proper maximizing price.

That's what.

Even though (( )).

Yeah, see the reason that this happens that you reduce the price you have to go back to the fact. Remember when you he gets a price; he gets a price bereft of tariffs. Tariff

revenue goes to the government. He gets a price which is not inclusive of tariffs. That is how you would understand and then another way of saying the same thing is that when he sees that the other country home country imposes tariffs.

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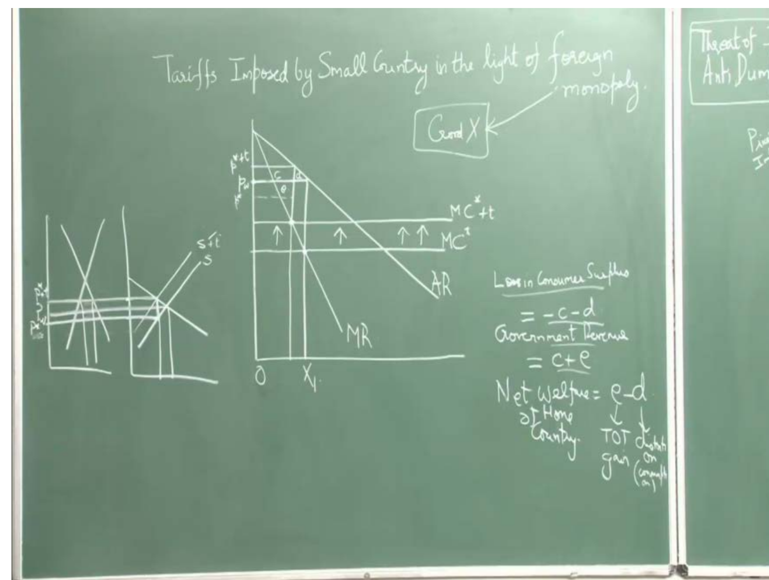


He has to reduce the price of that. Recall that diagram that I made for the large country. So, this is for the large country, this is the price; the free trade price. What happens if this large country imposes the tariffs? What happens is this supply curve shifts to the left? This is the price rise, but, the foreigners what foreigners get is this; P star. Why P star because this tariff revenue this P star plus t that tariff revenue this accrues to the government.

So, the foreigners do not get this price. Foreigners get a price bereft of tariffs they get this price or in other words when I say that a home country imposes tariffs the only way to enter the market, when they see that their exports are going down the only way to enter the market is by reducing the prices.

So, that is the price that they will they will charge. This is P star. Now, point is if we further analyse this, there is an interesting case that P star goes down to this level such that P star plus t; P star plus t is less than P W. There can be a case where, the price of the imported good declines to that level or the terms of trade improved to that level that the domestic price which needs to increase beyond P W is below P W. That is the case of the Metzlers paradox.

So, you had imposed tariffs in the hope that the price of imported goods will go up, but, the terms of trade improved to that extend that it depressed the price of the imported good. So, it goes down. So, then the whole idea of imposing tariffs gets lost because of these things.

So, I am not going into all this, but, if the question is about this P star why do you reduce P star? There are answers two answers which are basically the same that look at this is the domestic price, but, foreigners do not get this price because it is the home country which has imposed tariffs. The domestic price in the home country has gone up. Foreigners get a price which is bereft of tariffs. The only thing that they see is that when tariffs are imposed they will not be able to enter the market because the price of that good domestically has gone up.

So, their exports go down. When their exports go down, it is like saying that to enter the market they have to reduce the prices. So, this is the price that they would charge. See I am coming back to the original supply curve. I am not here. Original supply curve means that this is the price that you get without tariffs this is s star plus t. Now, we have another interesting case it is not even imposing anti dumping duties, it is the threat of imposing anti dumping duties.

(No audio 18:47 to 19:42)

Then you have a case when there is a threat of imposing antidumping duties. So, Chinese wish to enter our markets, but, they realise that the Indian government can impose anti dumping duties. And remember how anti dumping duties are calculated. It is based on the difference between the local prices, the local price in Beijing minus the export price, the price that they will charge in India

So, if I am the producer I am the Chinese producer and you are the Indian government and I know that you would impose anti dumping duties. What action would I follow or what action should I do such that these anti dumping duties go down. Do you understand my question? I am the Chinese producer. I know that there is a probably there is a case that you would impose antidumping duties and I know anti dumping duties are calculated on the basis of the difference between local price and the export price. What would I do if I know that your government will impose duties on me?

Reduce export price to local price. Are you are you sure.

(( )).

If you reduce the local price and or yeah of course, you can reduce the local price and given that you do not want to do anything in your own market. Given that I have to add this rider that given that you do not have to do anything about your local price. What could you do to reduce those duties increase the at the export price. So, this is a threat not that the Indian government has imposed the duties, the threat in itself will force me to increase the export prices. So, if this was the export price, it will go up. It will go up because I would increase the exports price in the threat in the face of the threat of India imposing antidumping duties on you.

So, then it is more pernicious than imposing tariffs because here, the loss in consumer surplus is minus a minus b minus c minus d. The gain in producer surplus is a. There is no revenue that you would get because the government have-not imposed anti dumping duties. There is only a threat that Indians will not allow the Chinese products to come in because it may impose anti dumping duties.

So, then as a producer I will increase the export price because I do not want to pay these much duties to reduce the antidumping duties, I would increase my export price. So, then the net welfare is minus b minus c minus d it is greater than when you impose tariffs. When you impose tariffs remember the welfare worked out to be minus b minus d here just the threat of it forces the foreign producers to increase their export prices.

As a result, the net welfare of this country comes down to minus b minus c minus d and remember under the W.T.O rules, there is nothing which says that the anti dumping which says that dumping cannot be done. There is nothing in the W.T.O which says that dumping has to be stopped. Only what corrective action should be taken W.T.O talks about it and what are the corrective actions anti dumping duties.

So, if you analyse the duty structure, every country has over and above the basic rate and anti dumping rate, over and above this countervailing duties to take care of the export subsidies and over and above that safeguards. So, you have a basic structure then anti dumping duties then c v d s countervailing duties and then safeguards. What President Bush did in 2001 was imposing safeguards, which is also called the escape clause

because it did not want the cheap steel to come in. So, it imposes tariffs on those steel coming in from the European nations and from some developing countries.

(( )).

Yeah see they say they understands dumping in a manner where, dumping they interpreted as foreign monopolist discriminating between markets.

(( )).

Yeah it is a case of price discrimination. So, economic argument cannot lead you to make a provision regarding that you need to reduce the dumping.

(( )) example if they do not have any floss against dumping, but, we can take measures against them, but, when we take measures against dumping we have a law similar like that. Absolutely, but, if there was floss and they restricted dumping then we wouldn't have any.

Absolutely, so, that can be one of the arguments that is one of the floss in the w t o system that it is quite about it is quite about the dumping, but, it says something about what needs to be done. Remember the US also imports something like a super 301 clause on countries which did not confirm to the good trade practices. At least that has been replaced by these by certain provisions which talk of doing something about the anti dumping duties all right. So, this is.

Sir

Yeah. What is the relationship between anti dumping duties and they are directly related or inversely related more is the difference. More is the difference; higher are the duties because local price and you have the export price. So, lower the export price, given the local price, larger will be the amount of the dumping duties you would have.

It is like Chinese products coming into India; the lower it is; the local price remaining the same, the higher will be the amount of duties. So, if I am the producer what will I do if I know that there is a threat? So, then I would try to increase the prices and it will be supported by the local producers. Do you know why would it be supported by the local producers?

(( )).

Because the prices are rising and they want the price to rise so that they can get a higher price for that import competing good. So, then interestingly what happens is that every country when it faces this when it faces this dumping, there are these producers which lobby with the government that you should do something about it. And they gain whether they impose tariffs or whether they whether the government does not impose tariffs. The producers gain because they see a rise in the export prices right. So, this is what goes on when you see the products been dumped. And dumped may be a misnomer it is not a correct thing because it is it is a case of price discrimination.

I will end up here. There are other things also in this chapter on tariffs and quotas imposed under imperfect competition, but, I am sure if you read through, you will be able to understand those things. So, when we meet on Monday then we discuss the r t s and specially the concept of trade creation and trade diversion.