Section IV

Question 28

Since the major onset of globalisation over the past 2 decades, the economies that have embraced it have experienced increased levels of trade, financial flows, accessibility to capital and labour and the use of ultra modern technology. However, there are still ongoing restraints to the theory of free trade between the global economies, and these impediments continue to hinder the economic integration of world economies.

Protection refers to any artificial barrier that restricts trade flows between economies. Protection can come in the form of tariffs: A government imposed tax on imports, Quotas: A quantative restriction on imports, Embargos: A complete ban on a product and a Subsidy: A payment made to domestic producers to ~~protect~~ help keep the price of the domestic good down.

These barriers are usually imposed on economies by groups of nations that are member to a trade agreement or trading bloc such as the European Union (EU) or North American Free Trade Agreement (NAFTA) and while the countries inside the bloc experience freer trade, the non-member countries exports are heavily taxed.

At a global level the disadvantages of protectionist policies are clear. The world price for a product under a free trade environment should be relatively low, as competition forces prices down. However when a form of protection such as a tariff is imposed on imports, the price increases, as shown in the diagram on the next page.

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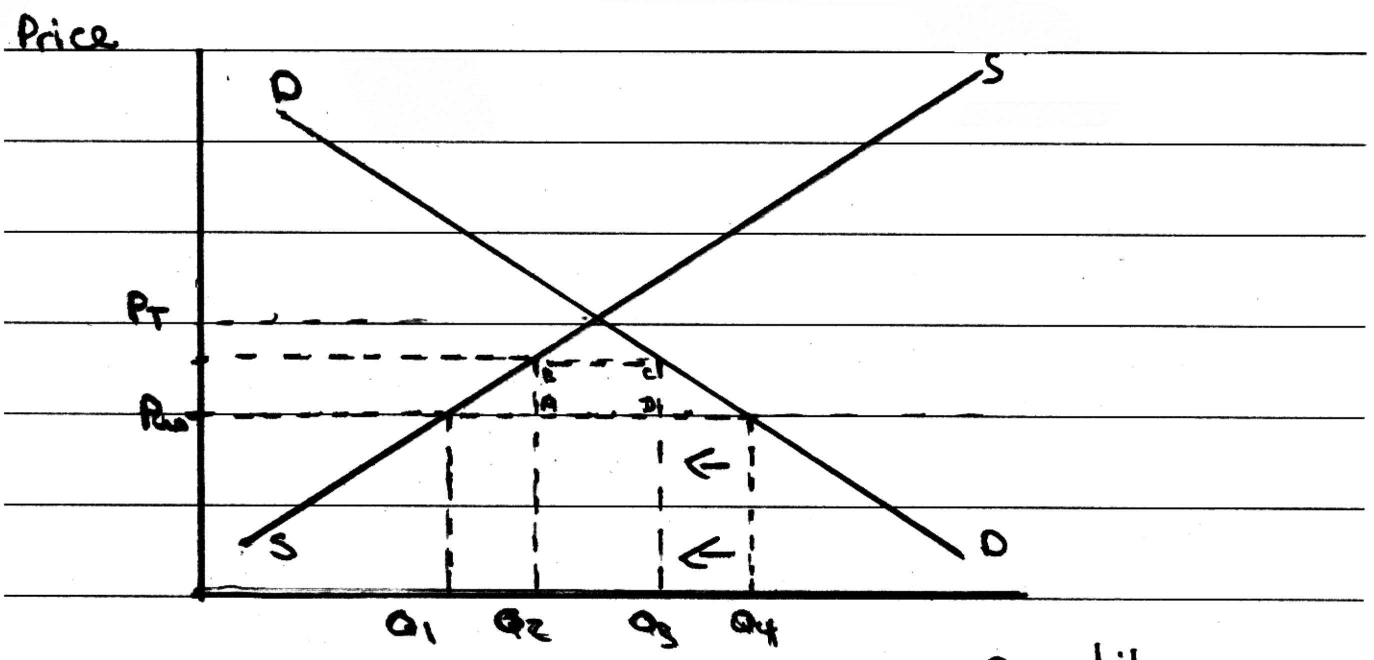


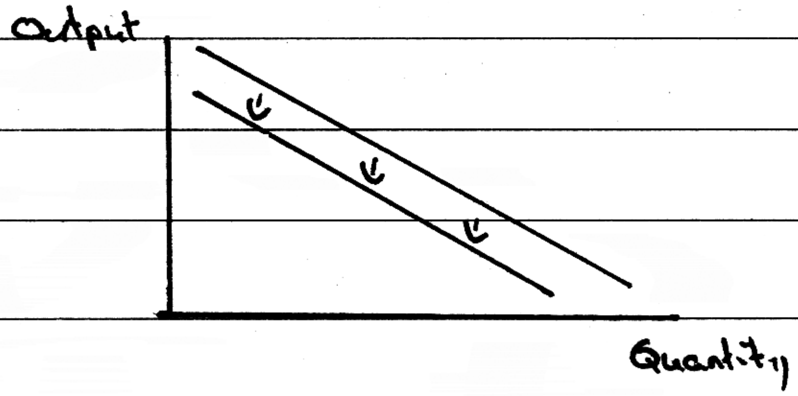
Inposition of a toriff

At price Pw (world price for the good) Q4 is the quantity demanded by consumers for the imported product. However with the inclusion of a toriff price rises ~~it~~ to PT, reducing demand to Q3. The government recieves revenue equilivant to ABCD and there are less Imports.

For a heavily commidity based exporting economy such as developing countries, protection such as US and EU subsidies to farmers (EU's Common Agricultural Policy or CAP) means that the exports are just not price competitive.

In Australia's case, protectionist policies make ~~or~~ the export industry less price competitive and the decline in exports ~~shows~~ takes its toll on the Balance of Goods and Services in the Current Account.

Protection is a major hinderence to ~~z~~ economic growth. Under the theory of comparative and absolute advantage, an increase in production will occur when specialising in a particular industry ~~are~~ takes place. However, when governments subsidise industries, they are only really promoting innefficiency and misallocating resources to those who are not efficent. This means the economy is not reaching full production potential and operating within the production possibility frontier.



Inflation can also rise due to import tariffs and various protection policies as the cost-push induced by ~~to~~ the government ultimately costs consumers more of their real-income.

Those on low incomes also suffer from protection as the real cost of a particular good or service is not what the consumers pay after protection (tariffs) and the distribution of income and wealth gap can easily be ~~[illegible]~~ accentuated by this.

Therefore, protectionist policies ~~[illegible]~~ have a huge impact on domestic and global economies.