2019 RIETI Workshop

RIETI

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Discussion on

"Trade agreements when profits matter"

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Key facts

- Trade policy in oligopoly gives rise to two externalities:
  - Terms-of-trade (ToT) externality
  - Profit-shifting (PS) externality
- Oligopolistic markets introduce an asymmetry between trade policies:

	Import tariff	Export subsidy
ToT	$(+)$	$(-)$
PS	$(+)$	$(+)$

Question and result

- Which of two trade policies is more self-enforcing in trade agreements?:
  - Import tariff

	Import tariff		Export subsidy
Deviation	$W_{D\tau}$	$\gtreqless$	$W_{D\sigma}$
Punishment	$W_{N\tau}$	$<$	$W_{N\sigma}$

  - Oligopoly provides a new rationale for negotiating on import tariffs (and banning export subsidies)

Country asymmetry

- How does country size matter for the choice of trade policy?:
  - This paper focuses on the number of countries
    - The greater the number of trading countries, the more self-enforcing import tariff
  - Country size may play a similar role
    - Suppose that market demand a_i is different
    - The greater the market size, the more self-enforcing import tariff?

Free entry

- What would happen if free entry (FE) is imposed?:
  - Even with FE, the two trade policies still give rise to asymmetric impacts on ToT
    - Is import tariff more self-enforcing in such a setting?
  - Recent work shows that FE can drastically change implications of trade policies and trade agreements
    - Bagwell and Staiger (2012a, JIE; 2012b, IER)
    - Ara and Ghosh (2016, EER)