Facultat d'Economia i Empresa

External trade (Comerç Exterior)

Code: 102324 Academic year: 2022-2023	**Grup 4** Fall term

Midterm Exam

(Duration: 90 minutes)

You can find the guidelines for the answers just below each problem. These are minimal suggestions with the key concepts to be included. Of course, this does not prevent the reply from being more elaborated.

Problem 1 (2 points)

Provide a short description of the following concepts and their domain of application in the theory of external trade:

1) Passive temporary importation under bond
2) SOIVRE
3) ITC
4) VER
5) European Economic Space

1) Passive temporary importation under bond

It is a waiver for a tariff when we are importing a good that has been produced by using a piece/input previously exported by the national firms that is importing the good. Key condition: this exported piece/input must be unique and fundamental for the production of the product to be imported.

2) SOIVRE

It is a certificate that is requested to import agricultural products (and food) in the EU. This document certifies the quality of the imported goods (for instance, no generic modified seeds etc..).

3) ITC

Index of trend (or tendency) of competitiveness. This index allows for disentangling the sources of competitiveness at country level by referring to an index of relative prices (IPR) and an index of relative exchange rate (IRX). The index is calculated as follows:

$$ITC = \frac{IPR x IRX}{100}$$

By construction, the competitiveness of the country increases (decreases) when the value of the index ITC decreases (increases).

4) VER (Voluntary export restriction)

It is a limit self-imposed by the exporter. It is a no-monetary trade barrier. The idea is to limit export of selected goods in order to enjoy more favourable conditions for selected categories of goods. Example: textile sector from South Asian countries.

5) European Economic Space (or Area).

It is an FTA between the EU and EFTA countries.

Problem 2 (5 points)

The world comprises three countries: *Alpha, Beta,* and *Gamma.*

The three countries are currently in autarky but plan to open their economies to international trade.

You are requested to advise the local government of the country *Alpha*.

2.a) Local administrators in *Alpha* require solid arguments to endorse the idea that trading would bring advantages to the country. You are requested to elaborate a document in which you present graphical arguments to show the advantages of having an open economy rather than a closed one (in the case of both export and import) in terms of the total welfare for country *Alpha*.

2.b) Given the outcome of that report, the prime minister decides to explore different alternatives and international agreements. In particular, the prime minister of *Alpha* is interested in having privileged commercial relationships with country *Beta* since it is a relevant international trading actor. She asks you to provide a clear suggestion: thinking of signing an FTA or a customs union agreement with *Beta*, she would like to know the advantages of each of the two options its potential impact of the trade relationship between *Alpha* and *Gamma*.

2.c) After analyzing your report, the prime minister thinks an FTA is a good first step. In order to conduct a pilot experiment, the prime minister charges a company exporting food and beverage with exploring the potential advantages of this agreement by performing the following test: exporting 100 kg of meat to *Beta* for a total merchandise value of 3,500€ that *Alpha* previously imported from *Gamma* for 2,500€. The prime minister also decides to elaborate a tariff scheme for importation to get at least 500€ in terms of tariff revenues from this operation. The local fiscal expert quantifies that there could be the possibility to apply a tariff of 20% of the value of the merchandise, or 100€ for a kg of imported meat, or an additional combination based on these two values. In this case, you are requested to:

(i) Elaborate at least three tariff schemes that would allow the government to get the expected amount of tariff revenues;

(ii) Evaluate whether there could really be room for country *Alpha* to export to *Beta* the imported meat from *Gamma* enjoying the FTA scheme, or whether *Beta* would prefer a direct import from *Gamma* and, if so, under which trading scheme;

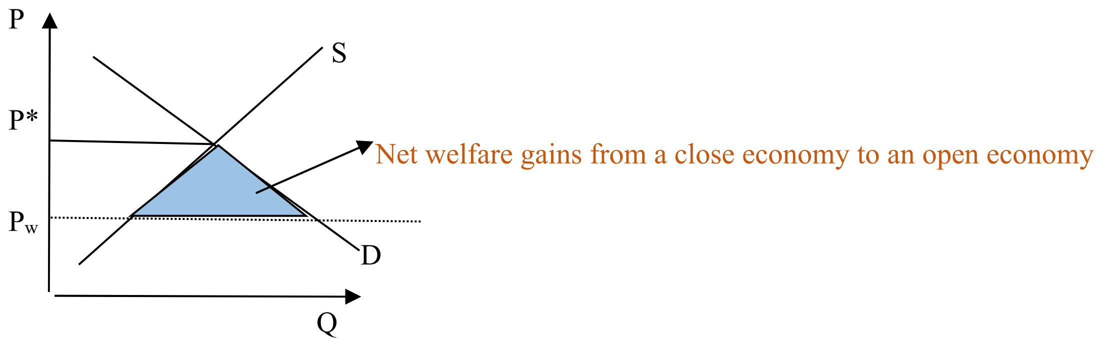
(iii) Evaluate whether your conclusion at point (ii) could be different if *Alpha* and *Beta* signed a customs union agreement.

2.d) As an additional step, the prime minister of country *Alpha* also wishes to evaluate the option to export this meat to the EU and, in particular, to Alicante (Spain).

In this case, you are requested to outline the bureaucratic duties, exporting documents to be produced, and the different places/steps to pass through to for this merchandise to be sold and commercialized in Alicante.

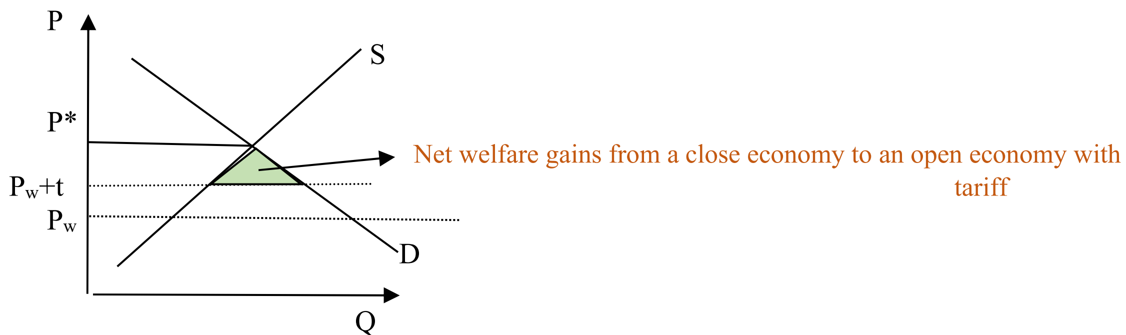
2.a) The opening to trade will allow *Alpha* for reaching a higher level of total welfare

In case of opening to trade and becoming a net importer:



In case of opening to trade and becoming a net exporter:

In the case *Alpha* opens to trade with tariffs (in the case the country will become a net importer) the total welfare of the country will still increase but the magnitude will be lower than the case of free trade



2.b)

FTA between *Alpha & Beta*: free trade policy across them and separate trade policies vs *Gamma*

Customs Union *Alpha & Beta*: free trade policy across them plus identical trade policy vs *Gamma*

FTA leaves room for a competitive behaviour between *Alpha & Beta* to get a privileged trade channel with *Gamma* by applying different trade policies to this country. Instead, being a Customs Union is more binding for all involved countries.

Consumers enjoy a reduction in prices due to the competition effect both in the case of FTA or Customs Union (it could be also the case of experiencing trade creation or trade diversion).

Producers face competition in both the cases (hence, less efficient firms will close) but in the case of FTA they can find adjustments for which imposing tariffs on import from *Gamma* they could recover part of the loss due to the closing of the plants issued by the FTA if the market conditions are favourable.

2.c) FTA between *Alpha & Beta*

Alpha

1. Import 100kg meat from *Gamma* for 2,500€. Tariff scheme: at least 500€ having an ad-valorem tariff 20% value of the merchandise or specific tariff 100€/kg
2. Export 100kg meat to *Beta* for 3,500€ (this is the price paid by *Beta*)

i) Three examples of tariff scheme to get at least 500€

a) Ad-valorem: 2,500 x 20% = 500€
b) Compound tariff with specific tariff
   100€/kg with a min 500 €: here the tariff is 100kg x 100€/kg= 10,000€
c) Compound tariff with mixed tariff
   100€/kg + Ad valorem 20% with a min 500 €: here the tariff is 10,000+500= 10,500 €

ii) In the case of FTA, the export from *Alpha* to *Beta* are already enjoying the FTA scheme because no tariff is applied. However, *Beta* can decide to import meat directly from *Gamma* to enjoy better purchasing conditions by:

a) Without imposing any tariff for import from *Gamma* and, hence, paying the merchandise 2,500€ rather than 3,500€
b) Imposing any tariff scheme on import from *Gamma* with a maximum amount of paid tariff lower that 1000€ that would imply to pay for the merchandise an amount lower than 3,500€.

iii) In the case of signing a customs union agreement, *Alpha & Beta* are forced to apply the same trade policies. Hence, the two countries agreed to apply the same tariff scheme elaborated by *Alpha*, then importing directly from *Gamma* would cost 2,500€ + 500€ (minimum tariff) = 3,000€. This option would be definitely more convenient that importing the meat from *Alpha.*

2.d) Exporting meat from *Alpha* to Alicante (Spain):

1) Official document to be used is DUA to be presented at the customs of import in Madrid; Alicante is customs of entry
2) Beyond the potential tariffs or quota that the EU can apply to the import of meat from abroad, the exporter must fulfil the quality conditions for the merchandise to be imported. In this case, it corresponds to present the SOIVRE certificate at the customs of import.
3) Before commercializing the meat in Alicante, the broker needs to complete the release of the merchandise in the customs of import (Madrid).

Problem 4 (3 points)

Consider the following data referring to import and export data of the following countries (source: World Bank):

Export (Billions LCU)	2012
South Africa	967
Vietnam	2597264
Import (Billions LCU)	**2012**
South Africa	1014
Vietnam	2483567
GDP(Billions LCU)	**2012**
South Africa	3254
Vietnam	3245419

LCU: Local currency unit

1) Compute the trade balance, the export quota, the index of competitiveness and the index of openness.
2) Discuss the previous results for each country and which one is the most competitive economy.

Answers: see document below.

PROBLEM 3

Export (Billions LCU)	**2012**
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Import (Billions LCU)	**2012**
South Africa	1014
Vietnam	2483567

GDP(Billions LCU)	**2012**
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Trade Balance (X-M)	**2012**	
South Africa	-47	Trade balance negative: the country is a net importer
Vietnam	113697	Positive balance: the country is a net exporter

Export quota (X*100/Y)	**2012**	
South Africa	29,7	The level of export from South Africa witnesses that (i) export is a relevant part of the GDP, but (ii) there is an internal market and not all GDP is devoted to export
Vietnam	80,0	Vietnam has a strong dependence on export and on international markets since exports accounts for a very relevant part of GDP making of it a very fragile economy subject to contagion effect

Export quota (X*100/X+M)	**2012**	
South Africa	48,8	These results are connected with the net result of the trade balance. The degree of the competitivenss of each country is reflected in the level of surplus
Vietnam	51,1	achieved by the trade balance. Both the countries are close to the threshold value

Index of openess (X+M)*100/Y	**2012**	
South Africa	60,9	Vietnam is definitely a small open economy and trade is definitely a key factor for its economic develpment.
Vietnam	156,6	

Overall, the statistics emphasize that both economies are active in the international market.
Vietnam is a small open economy with a very high level of export over GDP. This condition implies that this economy is quite fragile and subject to international contagion.
In terms of international competitiveness, Vietnam has an index bigger than 50%, something that is reflected in the positive trade balance.
Instead, South Africa shows a more balanced economy: exports accounts 30% of GDP (approx), the trade deficit is not so large and the index of competitiveness is close to 50%.
All in all, the two economies represent two different models of competitiveness. South Africa is a more balanced economy and less subject to international contagion effects.
Vietnam is definitely an import/export economy with a huge dependence from the fluctuations of the international markets.