



# **Free Trade, Protection and Balance of Payment**

Unit-II

# Free Trade & Protection

- Trade between the countries can either be the free trade or the protected trade.
- Free trade refers to a trade of goods and services between countries which is not impeded by government restrictions or interventions.
- Many economists have a belief that free trade leads to gains which are beyond the gains in consumption and the production.
- Protectionism refers to an economic policy which restricts trade between the economies.
- Restrictions in trade could be by way of tariffs, non – tariff barriers such as quotas, export subsidies, voluntary export restraints, technical barriers etc.



# Free Trade

- A trade policy of placing no restrictions on the movement of goods between countries is known as the policy of “Free trade”.
  - So, the trade is free from all the tariff and non-tariff barriers.
  - Free trade enables nations to focus on their core competitive advantages, thereby maximising economics output and fostering income growth for their citizens.
  - The idea that free trade is welfare enhancing is one of the most fundamental doctrines in modern economics dating back to Adam Smith (1776) and David Ricardo (1816).
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# Advantages of free trade

1. The theory of Comparative Advantage
  2. Better utilisation of factors of production
  3. Reduction in Tariff Barriers leads to creation of trade
  4. Lower prices of imported goods
  5. Increased Competition
  6. Restrict the monopoly
  7. Economic Growth
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# Disadvantages of free trade

1. Unfavorable for Underdeveloped Countries
  2. Free movement of harmful products
  3. Discourage the infant industry
  4. Environmental degradation
  5. Economic Dependency
  6. Unbalanced development
  7. Dumping
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# Protected Trade

- Protection refers to the policy of encouraging domestic industries by providing subsidies to home producers or more usually by imposing custom duties on foreign products.
- We can protect the trade with the help of tariffs and Non tariffs.
- The several instruments of non-tariffs are Import Quota, Voluntary export restraints, Technical Barriers to trade etc.



## Protectionist policies

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- Tariffs
- Import quotas
- Direct subsidies
- Technical barriers to trade
- Voluntary export restraints



# Argument in Favour of Protection

- Economic Argument
    - Infant Industry
    - Diversification of Industries
    - Increase in Employment
    - Terms of Trade
    - Balance of Payment
    - Anti-Dumping
    - Self-Sufficiency
    - Revenue
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# Argument in Favour of Protection

- Economic Argument
    - Correcting Distortions
    - Capital Accumulation
    - Basic Industry
    - Retaliation measure
    - Conservation of Resources
    - Size of Home Market
    - Equalizing Cost
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# Argument in Favour of Protection

- Non-Economic Argument
  - Defence
  - Nationalist
  - Preservation
  - To Limit the Harmful Goods



# Argument Against Protection

- Uneconomic Use of Resources
- Producers become Lethargic
- Check on Industrial Growth
- No Cure for Unemployment
- Loss to Consumer
- Unequal Distribution of Income
- Creation of Monopolies
- Encouragement to Corruption
- Loss of Revenue
- Retaliation