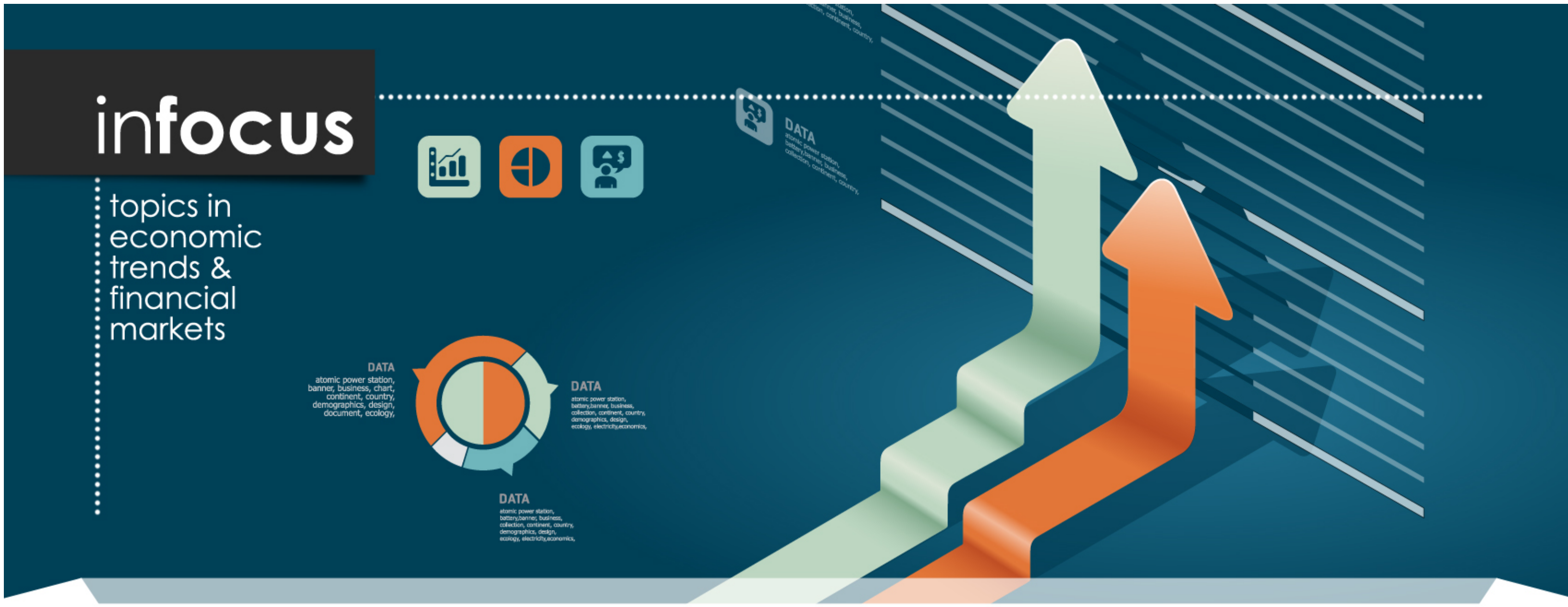

Trade Policy

International trade is a cornerstone of what we understand as modern commerce. Trade expands the free market and allows every country to profit from the goods they create and purchase the resources they need.

However, when the trade system is misused, it can cause considerable difficulties for a country's people. It is essential for governments to maintain trade policies that both improve the lives of citizens and give their countries a valuable place in the world economy.

World Trade
International trade can provide immeasurable benefits to participating countries. Trade promotes business competition, driving down prices and forcing increased product quality—both of which are good for consumers. Additionally, it also allows for specialization in certain industries, allowing companies to focus on one portion of an industry and boost production rates.

Modern trade has allowed for the rapid increase in quality of life and the accelerated development of technology. The global exchange of goods has led to the exchange of ideas and greatly increased global economic output. It has also improved international relations and discourages wars and other conflicts.

Trade Policy
Though the major benefits of trade are built on free market exchange, national governments discovered long ago that they could influence trade in order to provide optimal benefits to their economies.

A government's trade (or "commercial") policy is the rules it lays down on the importing and exporting of goods. In general, trade policy is most often used to influence prices to shrink the competitive advantage of other nations. Trade policy primarily functions through tariffs and import/export restrictions.

Tariffs – Tariffs are taxes on traded goods. By increasing tariffs on imports, a government can effectively raise the price of foreign products. Countries can also place tariffs on exports, but this is rare and usually involves a mutual export tariff agreement with another country.

Import restrictions – Governments often put quotas on foreign goods to limit their share of the market. If a country restricts or blocks all goods traded with another country, it is often referred to as a trade "embargo."

Trade policy can be an important tool in protecting domestic businesses, but unless a country decides to move away from international standards, it is difficult to see the impact of policy on investing.

Goals of Trade Policy
Governments may have several reasons to change their trade policies with the rest of the world or just a single country. However, the vast majority of trade policy is meant to protect domestic businesses.

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By raising tariffs or limiting imports, a government can limit the appeal of buying another country's goods. High tariffs, which can be a flat rate or a percentage, increase the cost of target goods, allowing domestically produced goods to automatically become cheaper by comparison. Similarly, quotas can directly limit the amount of market share a foreign product is allowed to take in a country. In either case, a government is using trade policy to protect its businesses and give them a market advantage at home.

In some cases, trade agreements are necessary to protect a country's industries from total collapse. This is particularly true when a foreign company threatens to "dump" goods on a domestic market.

In such a "dumping" case, a well-established company from one country floods a foreign economy with its goods, selling them at a discount, and possibly even a loss. Since the established company is supported by sales in other countries, it can continue to suppress prices in a target market until all its domestic producers go out of business. Once the company has a monopoly, it can raise prices above a fair value. Governments will usually make "anti-dumping" agreements with each other, banning their companies from disrupting domestic markets through abnormal business practices or pricing.

Finally, a government's trade policy could involve punitive embargos against nations that are misbehaving economically or politically. If carried out by a large enough country, a full embargo can be devastating to an underdeveloped nation.

Problems

Trade policy is hardly free of problems. It is often said that trade policy works in opposite directions for businesses and for consumers. This refers to the increase on tariffs or other strategies used to protect domestic businesses. When a country drives up the cost of imports to protect businesses, it is doing so by lowering consumer choice (at a previous price point.) Additionally, higher tariffs allow domestic businesses to needlessly raise their own prices without costing more than foreign competitors do.

If a country routinely sets high tariffs or severely restricts imports, other countries may respond by sharply taxing its goods or avoiding its market altogether. This can lead to economic isolation, which (though beneficial to young domestic businesses) can cripple a country's international manufacturing or high-tech industries that depend on foreign sales.

World Trade Organization

Officially beginning in 1995, the World Trade Organization (WTO) is an independent body that oversees the creation and implementation of trade agreements between participating countries. The organization also provides an open channel for countries to discuss or debate international commerce and actions needed to accommodate the needs of developing countries. The WTO replaced the earlier General Agreement on Tariffs and Trade (GATT) that had governed since the late 1940s.

The vast majority of nations operate within the WTO (more than 95 percent of all countries are involved with it.) Though many countries settle bilateral agreements in private, the WTO provides an important public voice for trade policy. Since the existence of GATT and the WTO, tariff rates have stayed much more consistent around the world, increasing the stability of the global market.

Trade and Investing

Trade policy can be an important tool in protecting domestic businesses, but unless a country suddenly decides to move away from international standards, it is difficult to see the impact of policies on investing. Hikes in tariffs usually lead to increased profits for businesses that only provide domestic services. However, this domestic growth is usually accompanied by a drop in international sales and exporting.

Unless purchasing shares in a company that works primarily with imports or developing countries, international trade policies are unlikely to affect investors in avoidable ways. Changes to policy may cause short-term instability, but the market adjusts and new tariffs quickly become another part of doing business. Still, investors should always investigate a company's foreign operations before purchasing shares, just to be informed. A history of stability cannot guarantee anything about future trade policy.

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