

**Assignment on:** Impact of free trade on developing countries

**Course Title:** International Business

**Course Code:** BUS 305

**Submitted To:**

Nujhat Anjum Ani

Senior Lecturer

Department of Business Administration

Faculty of Business & Entrepreneurship

**Submitted By:**

Alif Al Ashad

**ID:** 181-11-5827

**Section:** A

**Submission Date:** 20/4/2020

**Impact of free trade on developing countries**

**#Introduction:** Free trade is the unrestricted importing and exporting of goods and services between countries.

Free trade is a situation in which a government does not attempt to restrict what its citizens can buy from another country or what they sell to another country.

Free trade is a largely theoretical policy under which governments impose absolutely no [tariffs, taxes, or duties](https://www.thoughtco.com/the-economic-effect-of-tariffs-1146368) on imports, or quotas on exports. In this sense, free trade is the opposite of [protectionism](https://www.thoughtco.com/protectionism-definition-and-examples-4571027), a defensive trade policy intended to eliminate the possibility of foreign competition.

**#Background:** In 1948, the United States along with more than 100 other countries agreed to the [General Agreement on Tariffs and Trade](https://www.thoughtco.com/us-government-4133021) (GATT), a pact that reduced tariffs and other barriers to trade between the signatory countries. In 1995, GATT was replaced by the [World Trade Organization](https://www.wto.org/) (WTO). Today, 164 countries, accounting for 98% of all world trade belong to the WTO.

Despite their participation in FTAs and global trade organizations like the WTO, most governments still impose some protectionist-like trade restrictions such as tariffs and subsidies to protect local employment. For example, the so-called “[Chicken Tax](https://www.thoughtco.com/chicken-tax-4159747),” a 25% tariff on certain imported cars, light trucks, and vans imposed by President [Lyndon Johnson](https://www.thoughtco.com/lyndon-johnson-36th-president-united-states-104806) in 1963 to protect U.S. automakers remains in effect today.

**#Advantages: The major 5 advantages are:**

1. **Higher Employment Rates:** As developed countries are able to move their operations into developing countries, new job opportunities open up for local workers. Manufacturing (such as automobiles), assembly (clothing) and service jobs (help desks) have all migrated to developing countries in response to the removal of trade barriers. Generally, increased levels of employment lead to a higher standard of living and more consumer purchasing. This ultimately sparks the country's economy and may help to develop locally owned business.
2. **Less Child Labor:** Child labor occurs in developing countries for many reasons but one of the main reasons is lack of technology. Children are used as a cheap substitute for manufacturing equipment. Free trade allows companies to invest in equipment that minimizes the temptation to employ child workers. International firms are also generally more able to pay the higher wages to adult workers. With higher family incomes, children are able to attend school rather than work.
3. **Access to New Markets:** Not only does free trade allow foreign-owned companies to establish themselves in developing countries, it also allows native companies to sell to foreign markets. This expands their customer base and leads to new products and services and the viability of investing in innovation. This is particularly true for small businesses in developing countries. These companies no longer have to worry about absorbing the costs of tariffs and other barriers to market entry and can sell their products freely.
4. **Higher Levels of Investment Capital:** Most free trade agreements also reduce restrictions on foreign investment. This change allows foreign firms and financiers to more easily provide funds for in-country projects. With new capital entering a developing country, it begins an upward productivity cycle that stimulates the entire economy. An inflow of foreign capital can also stimulate the banking system, leading to more investment and consumer lending.
5. **Increased Life Expectancy:** An increase in employment levels, incomes, and the general standard of living contributes to an upward cycle of improvement that helps alleviate hunger and lack of medical care in developing countries. Preventative medical care including checkups and vaccinations are available to more of the population. It also increases the number of children who are educated and attend school regularly. The ultimate result is an increase in the average life span and a reduction in infant deaths.

**Other Advantages:**

* **It stimulates economic growth:** Even when limited restrictions like tariffs are applied, all countries involved tend to realize greater economic growth. For example, the [Office of the US Trade Representative](https://ustr.gov/) estimates that being a signatory of NAFTA (the North American Free Trade Agreement) increased the United States’ economic growth by 5% annually.
* **It helps consumers:** Trade restrictions like tariffs and quotas are implemented to protect local businesses and industries. When trade restrictions are removed, consumers tend to see lower prices because more products imported from countries with lower labor costs become available at the local level.
* **It increases foreign investment:** When not faced with trade restrictions, foreign investors tend to pour money into local businesses helping them expand and compete. In addition, many developing and isolated countries benefit from an influx of money from U.S. investors.
* **It reduces government spending:** Governments often subsidize local industries, like agriculture, for their loss of income due to export quotas. Once the quotas are lifted, the government’s tax revenues can be used for other purposes.
* **It encourages technology transfer:** In addition to human expertise, domestic businesses gain access to the latest technologies developed by their multinational partners.

**#Disadvantage:** The major 5 disadvantages are:

1. **Massive Job Losses:** As trade barriers are eliminated, certain goods may be cheaper to obtain overseas than to make domestically. Because of that, job losses are likely as less competitive industries wither away. While most economists would argue that these workers can be allocated to more efficient industries in which the United States has a comparative advantage and that this benefits the country as a whole, that's not always likely or practical. Furthermore, those adjustments are easier to make in the long term than in the short term. It isn't always easy for someone who's worked in a factory all her life to start a new career as an information technology specialist, for example.
2. **Predatory Pricing:** If trade takes place with no barriers at all, even an efficient company may be burned by an overseas rival with a predatory pricing strategy. A foreign company with deep pockets, for example, might dump its products into the U.S. market to force everyone else out of the market. Once that occurs, the company will enjoy a monopoly position and be able to price accordingly. Some free trade agreements allow for retaliatory tariffs if such actions can be proved.
3. **Increased Vulnerability:** From a strategic perspective, free trade can leave a country vulnerable if it causes the demise of critical industries. If a country grows dependent on another for critical products or services, it can be subject to political pressure and denied access to the goods if the agreement is suddenly severed. Moreover, a country with a free trade agreement or a preferential trade agreement with a neighboring country may fight against an expansion of that agreement to other nations if doing so will hurt its own position. One example of this occurred when Russia threatened to break its trade agreement with Ukraine and place a tariff on Ukrainian goods when the latter sought closer ties with the European Union.
4. **Industries Can't Develop:** Developing industries often benefit from domestic strategies that influence production, such as protective tariffs or tax breaks. As these protections vanish, new industries may find it difficult to establish themselves. It would be hard for an entrepreneur with the goal of succeeding in an industry where cost is a high barrier to entry, for example, to consider launching her product in a particular country if foreign competitors already enjoy economies of scale and easy access to domestic markets.
5. **Tax Troubles:** Free trade can hinder the ability of a nation to collect taxes from domestic corporations. A country that allows free trade and the free flow of capital outside of its borders and has a high tax rate may see portable industries migrate elsewhere. While some jobs are hard to move – a farm, for example, can't easily be relocated overseas – businesses may find it easier to shift headquarters elsewhere and change accounting methods to record profits in more tax-advantageous areas.

**Other Disadvantages:**

* **It encourages theft of intellectual property:** Many foreign governments, especially those in developing countries, often fail to take intellectual property rights seriously. Without the protection of [patent laws](https://www.thoughtco.com/guide-to-patent-rights-and-ownership-1992248), companies often have their innovations and new technologies stolen, forcing them to compete with lower-priced domestically-made fake products.
* **It allows for poor working conditions:** Similarly, governments in developing countries rarely have laws to regulate and ensure safe and fair working conditions. Because free trade is partially dependent on a lack of government restrictions, women and children are often forced to work in factories doing heavy labor under slave-like working conditions.
* **It can harm the environment:** Emerging countries have few, if any environmental protection laws. Since many free trade opportunities involve the exporting of natural resources like lumber or iron ore, clear-cutting of forests and un-reclaimed strip mining often decimate local environments.
* **It reduces revenues:** Due to the high level of competition spurred by unrestricted free trade, the businesses involved ultimately suffer reduced revenues. Smaller businesses in smaller countries are the most vulnerable to this effect.

**#Opinion:** I think present free trade system is better than the previous one. In the previous system, there were many restrictions in export, import and business also. The number of exchanging goods had limitations. Permission was also a long and critical process. People cannot start a business with a country easily. Even using an app there should take owner permission. But in present system there is no business restrictions. So one country develop a business with a country easily. An entrepreneur easily can invest to foreign country and play role in national economy. There is no barrier in export and importing. App using permission is not needed.

**Ex:** Google meet. We use this app for joining our online classes. We have no ownership for this app but we use it without any permission of the app owner, because of free tread.

**#Conclusion:** Having merits and demerits free trade doing well for the world. Worldwide the business bonding has improved and the growth of economy also increasing day by day. The gathering has reduced in buying something and the process is very easy now.