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THE PRIMACY OF RENTS IN THE CHOICE OF THE MEANS OF
PROTECTION

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Abstract

We revisit the political-economy of the choice between tariffs and import quotas as means of protection, beginning from the observation that revenue provided by a tariff becomes part of overall budgetary spending and is usually insignificant for budgetary finance whereas quotas provide politically assignable rents that can be significant for private incomes. The rents underlie a presumption of political choice of quotas. Societal latitude in political discretion (or political culture) underlies whether quotas can be used as means of personal rent creation, for rent assignment for political support, or for the conduct of foreign policy. Politically valuable quota rents explain sequencing whereby quotas have been eliminated first as a means of committing future governments to proceed with liberalization agreements.

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1. Introduction

When policy makers decide on international trade policy, they also decide on how to implement policy. In addition to tariffs (specific and ad valorem), there are various administrative protectionist means (see Nganga 2014). A basic choice is between tariffs and import quotas, with the two also often combined through reduced tariffs levied on a quota-constrained quantity of imports. For simplicity, we refer to all quota-constrained imports, whether or not there is an accompanying tariff, as subject to “quotas”. Our question is why quotas have been at all used, given the apparent economic advantages of tariffs. Tariffs are easier to administer and provide budgetary revenue whereas quotas with rare exceptions do not. Tariffs are also transparent indicators of protectionist levels (ad valorem tariffs more so than specific tariffs) whereas quotas require complex transformations to establish comparable tariff equivalents (Anderson 1988, Deardorff and Stern 1997). Quotas can sustain domestic monopoly whereas tariffs sustain domestic competition by allowing imports from any source for those willing to pay the import duty, which also minimizes administrative complexity. The choice between tariffs and quotas has arisen in the course of trade liberalization, which has in general involved eliminating quotas first, directly or by initial conversion of quotas to tariffs (see Lawrence 1989 and Cramer et al 1999).

Although the economic case for tariffs is quite compelling and the GATT and subsequent WTO have favored tariffs over quotas (see for example Supachai Panitchpakdi 2005), we know that economic merit is not sufficient to ensure political choice (Hillman 1991). Quite some time ago, in Cassing and Hillman (1985), we adopted a political-economy perspective on the choice between tariffs and quotas. We asked whether we could predict which means of protection a self-interested government could be expected to choose. We based our study on the political-support hypothesis for trade policy decisions – as in Hillman (1982, 1989) and Grossman and Helpman (1994, 2002). Other than the self-interested policy objective, we remained within the bounds of the tariff-quota comparison of Bhagwati (1965, 1968). Bhagwati had assumed that import quotas were competitively auctioned and provided budgetary revenue that paralleled the budgetary revenue from non-prohibitive tariffs. “Equivalence” between tariffs and quotas was defined as the same quantity of imports, the same domestic price, and the same domestic production and consumption.¹ Bhagwati showed that there was equivalence between tariffs and import quotas when the domestic import-competing industry was competitive but not when there was domestic monopoly. In Cassing and Hillman (1985) we showed that, while in the competitive case tariffs and quotas

¹ Bhagwati (1965) also assumed that imports under a quota were competitive (the quota did not provide domestic market power). Shibata (1968) suggested alternative perspectives on “equivalence” and noted the possibility that imports might not be competitively supplied.

were politically equivalent, with domestic monopoly for which the Bhagwati tariff/quota equivalence did not hold, the tariff was the preferred instrument of protection if the objective was political support. If however, in addition to political support, governments assigned positive weight to budgetary revenue, a quota could be chosen.²

The reasoning or proof is as follows.³ As in Bhagwati (1965), we focused on the domestic market for one import-competing good. In the absence of a revenue motive, the political-support function maximized by the political decision maker is $M[P, \pi(P)]$ where P is the domestic price of the import-competing good (negatively associated with consumer utility) and $\pi(P)$ denotes industry profits (positively associated with industry political support). As in Peltzman (1976), Hillman (1982) and Grossman and Helpman (1994), there is thus a trade-off between pleasing the industry and pleasing voters at large or consumers. At any domestic price P determined by a given world price and tariff, industry profit π is greater under a tariff than a quota (because the quantity of competitive imports is less with the tariff than the quota). Consumers care only about P and not the policy means whereby P is

² The conclusions are independent of whether tariffs are ad valorem or specific. In other circumstances, whether the tariff is ad valorem or specific can matter. See for example Lockwood and Wong (2000). The conclusions also apply in principle to trade in services (see Hoekman and Primo Braga 1997 and Francois and Hoekman 2010) as well as goods.

³ We disregarded consequences of changes in an industry's price on other output prices, although we subsequently describe a case in which price changes in other markets influence policy decisions.

established. With P the same but industry profit π greater under a tariff, tariffs are politically preferred to quotas.

With government revenue R politically valuable, and equally so for tariff revenue and proceeds from competitive auction of an import quota, the government's objective function becomes $V[M [P, \pi(P), R]$. At any domestic price of import-competing output P , government revenue is greater with a quota than with a tariff (because imports are greater with the tariff). Whether the tariff or a quota is preferred therefore depends on a government's preferences regarding political support M and revenue R . A "leviathan" government seeking to maximize government revenue (see Brennan and Buchanan 1977, 1980) would choose the quota but all that is required is sufficient weight on revenue.⁴

2. Two basic propositions

We now amend the conclusions in Cassing and Hillman (1985) with two empirically substantiated propositions (Hillman 2015a):

(A1) At least in high-income economies, tariff revenue is a negligibly small part of government budgetary revenue.⁵ Governments therefore care little or not all

⁴ We did not assume uncertainty. Dasgupta and Stiglitz (1977) investigated how uncertainty affects tariff revenue and revenue from auctioning of quotas.

⁵ See <https://stats.oecd.org/Index.aspx?DataSetCode=REV> (accessed August 5, 2015).

about budgetary consequences of changes in tariff revenue. The insignificant tariff revenue is also of limited importance for achieving political-support objectives since the revenue is not directly assignable to private beneficiaries.

(A2) Governments or political decision makers, whether in high or low-income economies, can benefit politically or possibly personally from a quota through rent sharing and assignment of quota rents.⁶

(A1) and (A2) are subject to the qualification that, because of low tax-administration capacity for income and corporate taxation and value-added and sales taxes, governments in low-income countries may rely significantly on tariffs for government revenue (Baunsgaard and Keen 2005). In all countries, rent seeking can take place to influence the assignment of budgetary revenue (Park et al. 2005). Tariff revenue from imports of any particular good is however not identifiable in aggregate budgetary revenue and is not specifically appropriable whereas quota rents are identifiable and specifically assignable and can be significant additions to personal income. Tariff revenue and quota

⁶ Rent creation through a quota and rent assignment would not influence policy decisions if governments were altruistic (did not care about losing office) and so were not subject to political-support considerations when making policy decisions, or political decision makers were not inclined to direct personal self-benefit. On the self-interested model of government, see Hillman (2009, chapter 2). The view that individuals maximize utility or profit whether in the private or public sector was propagated in the second half of the 20th century by the public-choice school. The model has subsequently become orthodoxy in the “new” political economy.

rents are distinguished by being “public money” and politically assignable “private money”.⁷

(A1) and (A2) introduce the private benefits to quota holders as influences on policy decisions. Societal rules regarding who can benefit from quota rents differ (see Hillman and Swank 2000 on “political culture”). The quota-rent beneficiaries can be policy makers themselves or members of their families or associated business interests. In high-income democracies, overtly visible monetary gain from own policy decisions is generally disallowed and more usually politically created and assigned rents are exchanged for political support. The political-support function specifies the extent to which political and private benefit in a society can be advanced at the expense of the population at large. With quotas rents more politically valuable than tariff revenue, it follows immediately that quotas are politically preferred when the domestic market is competitive. We show that a sufficient but not necessary condition for quotas to be politically preferred when domestic markets are not competitive is that quota rents be assigned to the domestic producers whom the quota protects. We also propose that the political benefits from quota rents explain the GATT and WTO preference for eliminating quotas first in the course of trade liberalization.

⁷ There have been proposals that tariff revenue from particular goods be identified and used to compensate an industry for reduced protection, which would make the tariff revenue “private money”. The tariff revenue would then be converted to an industry rent (Hillman, 1988).

3. Quotas rents and political choice

3.1 Domestic competition

In the competitive case, (A1) and (A2) result in non-equivalence of a tariff and quota. Quota rents are $R_Q(P) = (P - P_W)Q$, where Q is total imports under the quota, P is the domestic price, and P_W is a given world price. Again, consumers or voters care only about the domestic price P and not about how P is sustained. Total domestic industry profits with a tariff $\pi_T(P)$ and with a quota $\pi_Q(P)$ are equal. Political support with a tariff is $M^T = M^T(\pi_T(P), P)$ and with a quota $M^Q = M^Q(\pi_Q(P), P, R_Q(P))$. With $M^T < M^Q$, a government concerned with political support will always choose a quota in preference to a tariff, or will choose private income in preference to government revenue, which contrasts with the tariff-quota instrument indifference in competitive markets in Bhagwati (1965).

3.2 The non-competitive case

Quite generally, for any non-competitive market structure, domestic producers confront residual demand after subtraction of the competitively supplied quota Q from domestic demand. In such cases, and in particular a monopolized domestic industry, at any domestic price P at which imports take place, imports are greater with a quota than a tariff and domestic producers prefer the tariff

that results in higher profits (Cassing and Hillman 1985). The quota however provides politically assignable rents. Therefore:

Proposition 1

With monopoly or more generally imperfect competition, the tariff is politically preferred if political support from domestic producers is valued more than political support from beneficiaries of quota rents; conversely, the quota is politically preferred if political support from beneficiaries of quota rents is valued more than political support of domestic producers.

The ambiguity in proposition 1 is eliminated if the import quota is assigned to domestic producers. Domestic producers then maximize profits subject to costs of domestic production and the availability of imports at the world price under the quota. The option to use imports for domestic supply cannot decrease profits. Therefore:

Proposition 2

Independently of domestic market structure, the import quota is politically preferred if domestic producers are assigned the quota.

4. Trade liberalization

The primary explanations proposed for the GATT and WTO preference for elimination of quotas and conversion to quotas to tariffs have been transparency and comparability.⁸ Proposition 2 underlies a prediction that quotas will be eliminated first as a means of committing of future governments to liberalization. Viewing for simplicity trade liberalization as a sequential decision in two periods, two governments A and B can agree on a two-period two-stage liberalization sequence.⁹

Abstracting from discounting and with symmetry between the two countries, at the same domestic price P , the political loss from elimination of tariffs for governments A and B in period 1 and 2 is

⁸ The transparency of tariffs for comparison assumes that tariff rates or tariff levels are fully reflected in the relation between domestic firms' profit-maximizing prices and the world price of competitive imports. On unutilized or redundant tariffs, see however Fishelson and Hillman (1979). A quota may also be underutilized: see Hillman et al (1980).

⁹ The governments are prevented from unilaterally assisting their export industries using export subsidies because of WTO (or past GATT) illegality but can provide benefits for each other's export industries through reciprocal "exchange of market access" (see the exposition in Hillman, Moser and Long 1995 and Hillman and Moser 1996). We refer to two countries but trade liberalization is in general subject to a most-favored-nation clause (which stipulates that "concessions" or benefits given to one trading partner through market access are to be provided to all countries). Ethier (2002) observes that most-favored nation clause preempts opportunistic behavior in the granting of market access. Quite separately, beyond "exchange of market access", incentives for trade liberalization arise through personal portfolio diversification: see Cassing (1996) and Feeney and Hillman (2004).

$$L_j^i (T_j^i) \quad i = A, B, j = 1, 2. \quad (1)$$

The political loss from elimination of quotas is

$$\mathcal{L}_j^i (Q_j^i), \quad i = A, B, j = 1, 2. \quad (2)$$

At the same domestic price P :

$$\mathcal{L}_j^i (Q_j^i) > L_j^i (T_j^i), \quad i = A, B, j = 1, 2. \quad (3)$$

Benefits through “exchange of market access” are the same in periods 1 and 2 whether it is quotas or tariffs that are eliminated:

$$B_j^i (Q_j^i) = B_j^i (T_j^i) = B_j \quad i = A, B, j = 1, 2. \quad (4)$$

The incentive for reciprocal liberalization agreement by government A and B in period 1 is that:

$$\sum_j B_j > \mathcal{L}_j^i (Q_j^i) + L_j^i (T_j^i), \quad i = A, B, j = 1, 2. \quad (5)$$

Now introduce discounting. With the benefits from liberalization independent of how liberalization takes place and with costs of liberalization greater with quotas than tariffs, it follows that:

Proposition 3

With discounting, the two governments eliminate tariffs first, so deferring the greater political cost of eliminating quotas.

Continuation of liberalization initiated by the period-1 governments is at the discretion of successor governments. Any one of the two successor governments X and Y can block the period-2 completion of liberalization.

Governments X and Y have no incentive to proceed with liberalization if

$$B_j^i(Q_j^i) = B_j^i(T_j^i) = B_j < L_j^i(T_j^i) < \mathcal{L}_j^i(Q_j^i) \quad i = X, Y, j = 1, 2. \quad (6)$$

It is also possible that:

$$L_j^i(T_j^i) < B_j < \mathcal{L}_j^i(Q_j^i) \quad i = X, Y, j = 1, 2 \quad (7)$$

If (7) describes benefits and costs of liberalization, the period-2 governments reciprocally liberalize if the quota was eliminated in period 1 but not if the tariff was eliminated.¹⁰

We conclude:

¹⁰ We do not consider the possibility of reintroducing quotas in period 2 if the quotas were eliminated in period 1. Reintroducing quotas in period 2 while retaining tariffs is subject to the political cost of denial of previously negotiated foreign market access. On the other hand, a period-2 government can have an incentive to reverse period-1 tariffication by replacing tariffs with quotas. The assumption is that quotas that have been eliminated or converted to tariffs remain so. If tariffs were eliminated in period 1, a government in period 2 can decide not to liberalize trade but to appease existing quota-rent beneficiaries or reassign the existing quota rents to other beneficiaries.

Proposition 4

The sequencing of elimination of quotas first is a commitment device for the best prospects of subsequent governments proceeding with liberalization.

International trade agreements can be means of commitment for governments to resist domestic interest groups that seek to avoid liberalization (see for example Maggi and Rodriguez 1998 and Staiger and Tabellini 1999). In proposition 4 the commitment is by one government regarding decisions of a successor government that can have different preferences regarding rent assignment.¹¹

5. Different practices

5.1 *Why have tariffs been used to protect?*

We return to protection. If quotas politically dominate tariffs, why have tariffs been used? Tariffs were historically introduced for revenue motives because of low collection costs. Quotas would have incurred administrative costs that tariffs did not require. With both means however feasible, and with tariffs providing public money and quotas creating rents that can be assigned for political advantage or self-benefit, governance and voter resistance to privilege

¹¹ Aidt and Hillman (2008) describe rents assigned by a government that are re-assignable by a successor government.

are issues. We have described consumers as caring only about the price at which they have access to a good and the political- support response of consumers as voters is independent of whether price changes take place because of changes in a tariff or quota. An extended political objective function includes consumer or voter response to whether tariff revenue is added to the budget or politically assignable quota rents are created. For the same domestic price P , we distinguish domestic price sustained by a tariff $P(T)$ and price sustained by a quota $P(Q)$, with

$$P = P(T) = P(Q).$$

The policy maker now compares

$$M^T = M^T(\pi_T(P(T)), P(T))$$

and

$$M^Q = M^Q(\pi_Q(P(Q)), P(Q), R_Q(P(Q))).$$

With consumer political support reduced by use of the quota, in neither the competitive case or when in the non-competitive case producers receive the quota rents are we assured of

$$M^T < M^Q.$$

5.2 *Different political choices*

Voter response in a democracy can therefore favor tariffs or public money rather politically assignable rents. Moreover, not all countries are democracies, or democracies to the same degree. Practices accordingly differ.

The original tariff-quota comparison assumed that import quotas are auctioned and the revenue is added to budgetary spending, yet it seems that only Australia and New Zealand have auctioned import quotas (see Takacs 1987). Both of these countries rank low on presence of political corruption and high on political accountability.¹²

In the U.S., where also there is low political corruption and high political accountability, the possibility of auctioning import quotas has existed but was not used. Import quotas have been mainly on agricultural goods.¹³ In general the quotas have been to domestic import-competing producers. “Framing” occurs through the argument that the domestic producers “know” whether additional supply from imports is required in the domestic market. It would be

¹² Auctioning of quotas also provides an indication of the extent of protection provided the quota and the amount of tariff revenue that would be provided if the quota were converted a tariff.

¹³ The list is: Sugar and products with more than 65% sugar content, tobacco, peanuts and peanut butter, specific dairy products (e.g. powdered milk, baby formula), cotton, beef, animal feed, anchovies, wire rod, ethyl alcohol, olives, mandarin oranges, tuna, and brooms. Sugar producers benefit from additional subsidies and a price support scheme. See <http://www.wsj.com/articles/the-sugar-scandal-1438212128/> (accessed August 5 2015).

politically difficult in the U.S. to assign quota rents domestically to other than domestic producers. Quotas have been assigned to foreign producers.¹⁴

The EU, for corruption indicators differ for member countries, has had import quotas on various goods including sugar, steel, wood, textiles, footwear, and potassium chloride. Quotas have been means of conducting EU foreign policy.¹⁵ Japan has also used country quota assignment for foreign policy objectives.¹⁶

In corruption-endemic countries, a wide range of means has been observed for rent creation and extraction (see for example Cassing 2000 on Indonesia and Mabuku and Kiyemi 2015 on sub-Saharan Africa). The scope of corruption includes, for example, false certification of the quantity of imports

¹⁴ Through “voluntary export quotas”, the U.S. government assigned rents to a foreign export cartel, to compensate foreign producers for prior agreed market access. See Hillman and Ursprung (1988) for a political economy perspective on voluntary export restraints. Quotas have however assigned to producer producers more widely, ostensibly as an instrument of foreign policy.

¹⁵ It was estimated in 2015 that internal EU sugar prices would fall by 2017 fall by 22-23 percent as the consequence of elimination of the EU sugar import quota. See <http://capreform.eu/eu-sugar-beet-prices-to-fall-by-22-23-when-quotas-eliminated/> (accessed 25 June 2015). There was resistance by the foreign beneficiaries of the sugar quota who declared that they were “deeply concerned with the sharp decline in the sugar prices” <http://www.kaieteurnewsonline.com/2015/04/11/sugar-producers-urge-eu-to-delay-quota-abolition/> (accessed 25 June 2015).

¹⁶ Anderson (1983) reported that the beef import quota was used to ensure imports were from the U.S., in response to observations by the U.S. government that the share of U.S. imports in total Japanese imports should be greater.

that have entered under a quota.¹⁷ It is difficult to obtain data on who actually benefits from quota rents in low-income countries. Evidence is for the most part from observations on the value of the rents created by quotas. For Indonesia, for example, we have the observation:

"Strict import quotas on Australian cattle have left the Indonesian marketplace short of beef and prices soaring at the busiest time of the year" – which we are to judge as a government policy mistake or successful rent creation."¹⁸

For China:

"The low-tariff quotas .. are allotted to state-owned and private firms in the world's top grain consumer. With Chinese grain prices the highest in the world, these import allocations have become a cash cow for well-connected companies."¹⁹

In another example, Ma (2007) has described the rents created by import quotas on wheat in Taiwan, where the import quotas have been combined with domestic flour-price ceilings. Russia uses import quotas for rent creation but

¹⁷ On the case of import quotas on rice in Nigeria, see <http://allafrica.com/stories/201501281489.html> (accessed June 22 2015).

¹⁸ <http://www.smh.com.au/national/indonesians-short-on-beef-after-import-quotas-hurt-20120810-23zp6.html> (accessed June 22 2015). On the culture of corruption in Indonesia, see Cassing (2000).

¹⁹ <http://www.cnbc.com/id/102206077> (accessed June 22 2015).

also quotas have been issues to charitable organizations in need.²⁰ Our political-support predictions are validated when observations are available. Anderson (1983) for example provided estimates of the value of rents from import quotas on beef in Japan and observed, regarding the domestic distributors who were beneficiaries of the rents, that: “This group of apparent beneficiaries from the existing policy are likely to lobby vigorously to retain that benefit” (p. 111). The government import agency in Japan assigned part of the import quota to domestic distributors at less than the world import price. Domestic producers also benefitted from a subsidy financed from part of the quota rents (ibid, p. 108). The Japanese government thereby assured that political support from domestic producers would complement political support from holders of quota rents. Ideally for the government, at the margin of political support (Hillman 1982), rents would have been assigned to equalize political benefits to domestic producers protected by quotas and domestic distributors benefitting from quota rents.²¹

²⁰ http://www.todayszaman.com/anasayfa_quotas-hinder-increased-trade-between-turkey-russia_365676.html (accessed August 14 2015).

²¹ Anderson (1983) also notes more complex general-equilibrium aspects of political influence on trade policy: domestic Japanese producers of chicken and pork had reason to oppose liberalization of beef imports, because of substitution effects of the decline in the domestic price of beef.

6. Further observations

Some further considerations merit comment before we conclude.

6.1 Corruption

We have tied quota rents to corruption. Administrative complexity affects corruption possibilities. Tariffs are paid when goods are imported. Quotas require assignment among importers and monitoring through counting of the quantities of goods that have been imported. Tariffs are subject to corruption by bribing customs' officials at border entry points. Quotas are subject to corruption by bribing government officials to provide documentation that allows or misreports imports.

6.2 Efficiency losses

Rent seeking supplements standard social or efficiency losses from protection.²² A quota adds the social loss of rent seeking through contestability of quota rents (Krueger 1974). Rent seeking can also arise for monopoly profits

²² For a review of the literature on the social cost of rent seeking, see Hillman (2013). Kahana and Klunover (2014) note the complementarity between deadweight losses and the social costs of rent seeking. On design of rent seeking to benefit the political creators of rents, see Appelbaum and Katz (1987), Gradstein and Konrad (1999), and Epstein and Nitzan (2015).

(Tullock 1967, 1989). When the social cost of rent seeking is included, we do not know beforehand whether a tariff or the quota is more socially costly.²³

6.3 Political concern for efficiency losses

Efficiency losses have also not entered into the government objective function, implying voters and interest groups do not reward efficiency. If efficiency is sought, we expect free trade, or if efficient assistance to producers is the objective, production subsidies should be observed (Mayer and Riezman, 1990; Hillman 2009, chapter 4). Our perspective on efficiency differs from Becker (1983, 1985), Wittman (1989), and others, who, in theoretical analyses, have proposed that governments will always choose efficient policies that minimize deadweight losses (there is no rent seeking in the Becker model but see Aidt 2003). The argument is that efficient policies provide more to share and everyone in society should be in favor of greater efficiency. Yet we observe inefficient policies, or inefficient policy means. Economic literacy and rational ignorance appear to matter.²⁴

²³ Monopoly rents are greater with a tariff than a quota, which also however attracts rent seeking for quota rents. Rent-seeking models (Long 2013) provide predictions about rent dissipation as the measure of social cost of rent seeking. Under various conditions, the value of a contested rent can be taken as the value of the resources used in contesting the rent (Hillman, 2009 chapter 2).

²⁴ An explanation for the use of tariffs and quotas is (see Hillman, 2009, pp. 227-78) that rents are created and assigned with the political advantage of no intermediation through the

6.4 The terms of trade

The terms of trade introduce issues that we have chosen to avoid. Tariffs and quotas affect the terms of trade through monopsony power in world markets. We have not been concerned with the “optimal tariff” nor with the role of the terms of trade in trade negotiations (Bagwell and Staiger 2002; Ethier 2004; Regan 2014). We have taken the world price of import-competing goods as given and not subject to influence through monopsony power.²⁵

6.5 Partial equilibrium

For continuity and comparability with the past studies in Bhagwati (1965) and Cassing and Hillman (1985), we have used a partial-equilibrium model. The transformation can be made to a specific-factors model. The political-support function is then specified for industry rents rather than industry profits (Hillman 1982). The conclusions about the primacy of rents in the choice between tariffs and quotas do not change.

government budget. In the case of reciprocal liberalization, the efficiency gains through exchange of market access are incidental to the political objective of benefitting exporters (Hillman and Moser 1996).

²⁵ For a comparison of tariffs and quotas when the terms of trade change, and the asymmetry, see Melvin (1986).

6.6 Where to place tariff revenue?

A logical question that arises is where to place tariff revenue. Tariff revenue in models of international trade is a general enigma. In models that present the entire economy as consisting of two traded goods, tariff revenue can be described as significant in the model. In fact, in high-income countries and more generally, non-traded goods make up the greater part of the value of national income and there are many traded goods. Our conclusions are based on the observation that the revenue for the budget that would be available from a tariff on any one traded good is negligible but quota rents can be significant when compared to private incomes. We have been not assuming that tariff revenue does not exist but that political decision makers who can choose between tariff revenue and quota rents place zero weight on tariff revenue. Zero could however be too small. We observe tariffs used in conjunction with quotas.

7. Conclusions

Some topics in the literature close too early. This has been the case with the explanation for political choice between tariffs and quotas. The mainstream non-political-economy international-trade literature based the preference for

tariffs on transparency in measurement and on desirability of tariffs because of greater market flexibility. Indeed, without comparative means of measurement, agreements to reduce protection or to engage in “exchange of concessions” could not meaningfully take place. Yet, in converting quotas to tariffs, governments also engage in the politically costly action of depriving quota holders of rents. Monopoly rents require actually producing something. Quotas rents are simply obtainable by taking advantage of a legally predetermined price differential and, other than an outright gift, are the most straightforward means of rent creation.

In an early study, we did not account for quota rents. We followed the mainstream model of the literature in assuming that quotas and tariffs yield equally politically-valued revenue for the government budget. When allowance is made for asymmetric political valuation of tariff revenue and quota rents, the presumption is in favor of political choice of quotas. Domestic institutions however underlie the extent to which policymakers can create and assign quota rents. The sequencing of ending quotas first begins trade liberalization with the more politically instrument to eliminate and is consistent with maximal commitment provided for future governments to proceed with liberalization.

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