



# INTERNATIONAL TRADE BARRIERS AND TRADE FACILITATION IN CENTRALASIA

**Orifjonov Bekhzodjon Odiljonovich**

*INHA University in Tashkent, School of Logistics, Junior Student (3 year)*

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## -----ABSTRACT-----

*The main idea of this paper is to provide a reader with a concrete idea about International Trade Barriers and how it influences on the trade. Why do countries need a barrier and the main types of trade barriers?*

*This study is generally a non-empirical analysis. The main sources of this study include secondary sources like textbooks, reports, relevant national and online documents and some publications.*

*In this paper, I would also like to discuss Trade facilitation in Central Asia. The existing situation with trade in Asia and the ways of improvement.*

**KEYWORDS:** *Competence, economists, specific tariffs, licenses, local, professional training.*

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## INTRODUCTION

International trade is the exchange of goods and services between countries.

Trading globally gives consumers and countries the opportunity to be exposed to goods and services not available in their own countries, or which would be more expensive domestically.

The importance of international trade was recognized early on by political economists like Adam Smith and David Ricardo.

Still, some argue that international trade actually can be bad for smaller nations, putting them at a greater disadvantage on the world stage.

International trade was key to the rise of the global economy. In the global economy, supply and demand and thus prices both impact and are impacted by global events.

Political change in Asia, for example, could result in an increase in the cost of labor. This could increase the manufacturing costs for an American sneaker company that is based in Malaysia, which would then result in an increase in the price charged for a pair of sneakers that an American consumer might purchase at their local mall.

## INTERNATIONAL TRADE BARRIER

Trade barriers are government-induced restrictions on international trade, which generally decrease overall economic efficiency. Most trade barriers work on the same principle—the imposition of some sort of cost on trade that raises the price of the traded products. If two or more nations repeatedly use trade barriers against each other, then a trade war results [1].

Economists generally agree that trade barriers are detrimental and decrease overall economic efficiency. This can be explained by the theory of comparative advantage. In theory, free trade involves the removal of all such barriers, except perhaps those considered necessary for health or national security. In practice, however, even those countries promoting free trade heavily subsidize certain industries, such as agriculture and steel.

Trade barriers are often criticized for the effect they have on the developing world. Because rich-country players set trade policies, goods, such as agricultural products that developing countries are best at producing, face high barriers. Trade barriers, such as taxes on food imports or subsidies for farmers in developed economies, lead to overproduction and dumping on world markets, thus lowering prices and hurting poor-country farmers [2]. Tariffs also tend to be anti-poor, with low rates for raw commodities and high rates for labor-intensive processed goods. The Commitment to Development Index measures the effect that rich country trade policies actually have on the



developing world. Another negative aspect of trade barriers is that it would cause a limited choice of products and, therefore, would force customers to pay higher prices and accept inferior quality.

### Why Trade Barriers Used?

Tariffs are often created to protect infant industries and developing economies, but are also used by more advanced economies with developed industries. Here are five of the top reasons tariffs are used:

#### 1) Protecting Domestic Employment

The levying of tariffs is often highly politicized. The possibility of increased competition from imported goods can threaten domestic industries. These domestic companies may fire workers or shift production abroad to cut costs, which means higher unemployment and a less happy electorate [3]. The unemployment argument often shifts to domestic industries complaining about cheap foreign labor, and how poor working conditions and lack of regulation allow foreign companies to produce goods more cheaply. In economics, however, countries will continue to produce goods until they no longer have a comparative advantage (not to be confused with an absolute advantage).

#### 2) Protecting Consumers

A government may levy a tariff on products that it feels could endanger its population. For example, South Korea may place a tariff on imported beef from the United States if it thinks that the goods could be tainted with disease.

#### 3) Infant Industries

The use of tariffs to protect infant industries can be seen by the Import Substitution Industrialization (ISI) strategy employed by many developing nations. The government of a developing economy will levy tariffs on imported goods in industries in which it wants to foster growth [4]. This increases the prices of imported goods and creates a domestic market for domestically produced goods, while protecting those industries from being forced out by more competitive pricing. It decreases unemployment and allows developing countries to shift from agricultural products to finished goods.

#### 4) National Security

Barriers are also employed by developed countries to protect certain industries that are deemed strategically important, such as those supporting national security. Defense industries are often viewed as vital to state interests, and often enjoy significant levels of protection [5]. For example, while both Western Europe and the United States are industrialized, both are very protective of defense-oriented companies.

#### 5) Retaliation

Countries may also set tariffs as a retaliation technique if they think that a trading partner has not played by the rules. For example, if France believes that the United States has allowed its wine producers to call its domestically produced sparkling wines "Champagne" (a name specific to the Champagne region of France) for too long, it may levy a tariff on imported wine from the United States [6]. If the U.S. agrees to crack down on the improper labeling, France is likely to stop its retaliation.

### Common Types of Tariffs

There are several types of tariffs and barriers that a government can employ:

- Specific tariffs
- Ad valorem tariffs
- Licenses
- Import quotas
- Voluntary export restraints
- Local content requirements

#### Specific Tariffs

A fixed fee levied on one unit of an imported good is referred to as a specific tariff. This tariff can vary according to the type of goods imported. For example, a country could levy a \$15 tariff on each pair of shoes imported, but levy a \$300 tariff on each computer imported.

#### Ad Valorem Tariffs

The phrase "ad valorem" is Latin for "according to value," and this type of tariff is levied on a good based on a percentage of that good's value. An example of an ad valorem tariff would be a 15% tariff levied by Japan on U.S. automobiles. The 15% is a price increase on the value of the automobile, so a \$10,000 vehicle now costs \$11,500 to Japanese consumers [7]. This price increase protects domestic producers from being undercut but also keeps prices artificially high for Japanese car shoppers.

## Non-Tariff Barriers to Trade

### Licenses

A license is granted to a business by the government and allows the business to import a certain type of good into the country. For example, there could be a restriction on imported cheese, and licenses would be granted to certain companies allowing them to act as importers. This creates a restriction on competition and increases prices faced by consumers.

### Import Quotas

An import quota is a restriction placed on the amount of a particular good that can be imported. This sort of barrier is often associated with the issuance of licenses. For example, a country may place a quota on the volume of imported citrus fruit that is allowed.

### Voluntary Export Restraints (VER)

This type of trade barrier is "voluntary" in that it is created by the exporting country rather than the importing one. A voluntary export restraint (VER) is usually levied at the behest of the importing country and could be accompanied by a reciprocal VER. For example, Brazil could place a VER on the exportation of sugar to Canada, based on a request by Canada. Canada could then place a VER on the exportation of coal to Brazil. This increases the price of both coal and sugar but protects the domestic industries.

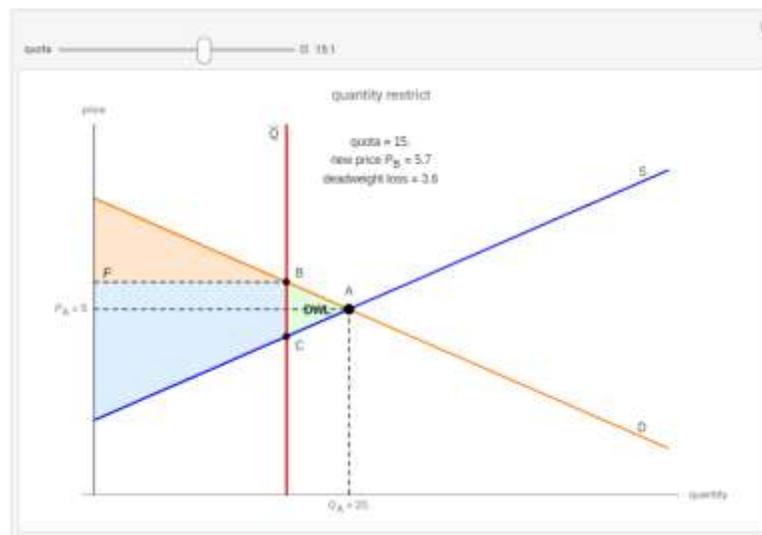
### Local Content Requirement

Instead of placing a quota on the number of goods that can be imported, the government can require that a certain percentage of a good be made domestically. The restriction can be a percentage of the good itself or a percentage of the value of the good. For example, a restriction on the import of computers might say that 25% of the pieces used to make the computer are made domestically, or can say that 15% of the value of the good must come from domestically produced components [8].

## How Do Tariffs Affect Prices?

Tariffs increase the prices of imported goods. Because of this, domestic producers are not forced to reduce their prices from increased competition, and domestic consumers are left paying higher prices as a result. Tariffs also reduce efficiencies by allowing companies that would not exist in a more competitive market to remain open.

The figure below illustrates the effects of world trade without the presence of a tariff. In the graph, DS means domestic supply and DD means domestic demand.

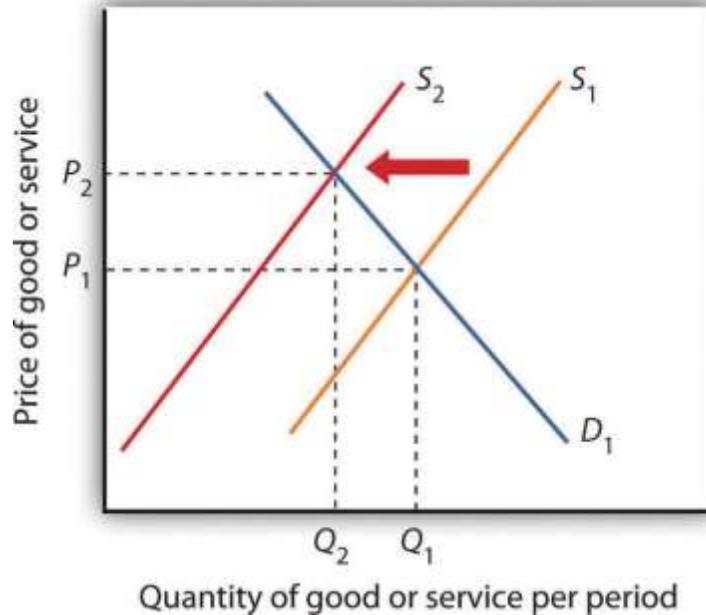


The price of goods at home is found at price  $P$ , while the world price is found at  $P^*$ . At a lower price, domestic consumers will consume  $Q_w$  worth of goods, but because the home country can only produce up to  $Q_d$ , it must import  $Q_w - Q_d$  worth of goods.

When a tariff or other price-increasing policy is put in place, the effect is to increase prices and limit the volume of imports [9]. In the figure below, price increases from the non-tariff  $P^*$  to  $P'$ . Because the price has

increased, more domestic companies are willing to produce the good, so  $Q_d$  moves right. This also shifts  $Q_w$  left.

The overall effect is a reduction in imports, increased domestic production, higher consumer prices.



Protectionist policies reduce the quantities of foreign goods and services supplied to the country that imposes the restriction. As a result, such policies shift the supply curve to the left for the good or service whose imports are restricted. In the case shown, the supply curve shifts to  $S_2$ , the equilibrium price rises to  $P_2$ , and the equilibrium quantity falls to  $Q_2$ .

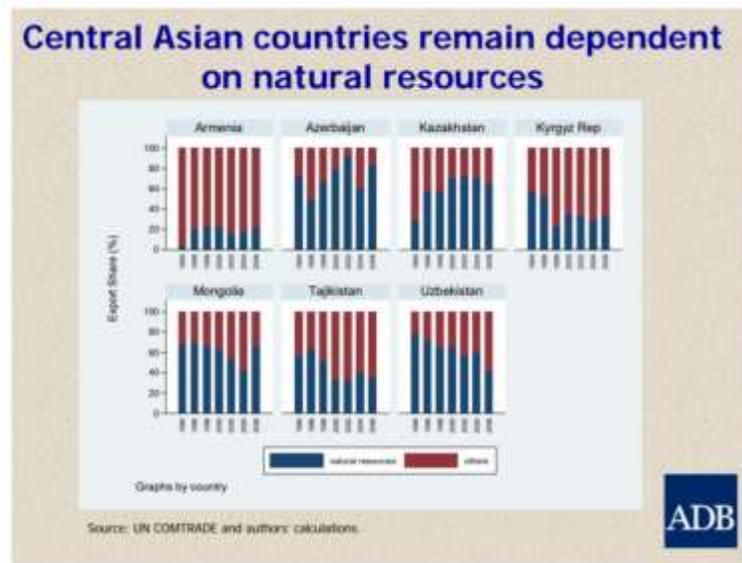
A quantity restriction is a form of government intervention in a market that limits the production and sale of goods to some fixed amount. When you introduce the quantity restriction, this model will show the amount of and the new market price. Consumer and producer surplus respond accordingly, and deadweight loss increases.

### What is the Trade facilitation?

WTO defines trade facilitation as: “the simplification and harmonization of international trade procedures, including the activities, practices, and formalities involved in collecting, presenting, communicating, and processing data and other information required for the movement of goods in international trade”. In general, trade facilitation refers to the ease of moving goods across borders [10].

Information below was taken from the ADB source

\*Since independence, the Central Asian economies have faced the challenge of how to generate sustained economic growth through a process of structural transformation and reduced reliance on natural resources. As shown in Figure 1, exports of natural resources constitute the bulk of total trade in the case of some of the Central



Asian countries [11]. As much as three-fourths of Azerbaijan's exports and two-thirds of Kazakhstan's are accounted for by natural resources. The process of structural transformation involves a change in what a country produces and a shift away from low-productivity, low-wage activities to high-productivity and high-wage activities. A very clear example of structural transformation is found in Asian economies such as the PRC, Vietnam, Malaysia, or the NIEs. The output and employment structures are changing very fast in the direction of high value-added sectors.

While the resource-rich Central Asian countries will continue to rely on natural resources as the driver of economic growth, this has long term implications. First, is the well known problem of the so-called Dutch disease. This refers to the negative effect that natural resources tend to have on a country's growth prospects. Resource exports cause the country's currency to appreciate making manufacturing activities uncompetitive [12]. These, however, might have had the potential to induce structural change. Second, reliance on natural resources exposes the country to the vagaries of international markets. Third, abundance in natural resources poses the problem of resource management and rent seeking.

Fourth, resource-rich countries make for "bad neighbors" because of limited spillovers to surrounding countries. This is important from the perspective of promoting greater regional integration among the Central Asian countries. Notwithstanding the standard arguments about trade creation and trade distortion, enhancing intra-regional trade may offer better potential for export upgrading than extra-regional trade. Increasing trade within the same geographical region can be more conducive to diversification, structural change and industrial upgrading than trade with countries outside the region. It is not only the relative pace of trade expansion but also the composition of intra-regional exports that makes regional integration a promising strategy for accelerating economic development. Recent literature (e.g., Hausmann et. al, 2007) has shown that the composition of exports impacts long-term growth. In other words, countries with a more sophisticated export basket tend to grow faster. Such a strategy relying on regional integration will require regional production networks, a spatially coordinated expansion of regional infrastructure, and better trade facilitation to encourage greater and timely flows of goods across borders.

**Table 1: Intra-regional trade in Central Asia vis-à-vis other regions**

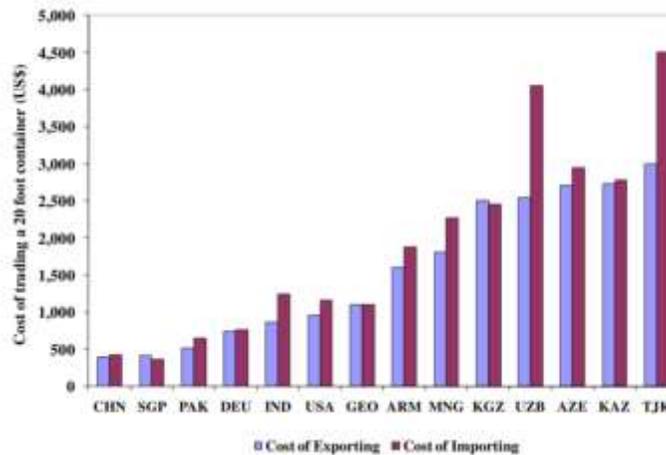
	% of total trade which is intra-regional	% of trade in manufacturing goods which is intra-regional
Central Asia	4.8	1.6
ASEAN	27.4	25.3
SAARC	5.3	4.1
EU-27	63.7	68.3
Latin America	19.4	14.7

Source: BACI, authors' calculations

Table 1 examines the extent of regional integration, as measured by intra-regional trade, among the Central Asian countries. Intra-regional trade in Central Asia is lower than within other regional arrangements such as the EU or ASEAN. Intra-regional trade in manufacturing products accounted for only 1.6% of the total trade of Central Asian countries in 2005, as opposed to 68% and 25% in case of the EU and ASEAN, respectively

The Central Asian countries, however, perform poorly when it comes to artificial nontariff barriers. These barriers take the form of inefficient customs administration and other border agencies, long-delays at the ports, transit fees, unofficial payments, poor physical infrastructure, and absence of a competent logistics sector. Artificial non-tariff barriers, such as those listed above, pose significant obstacles to trade. For example, using the World Bank's Doing Business Survey (World Bank, 2007b), the cost of exporting (importing) a 20-foot container from/to is among the highest for the Central Asian countries.

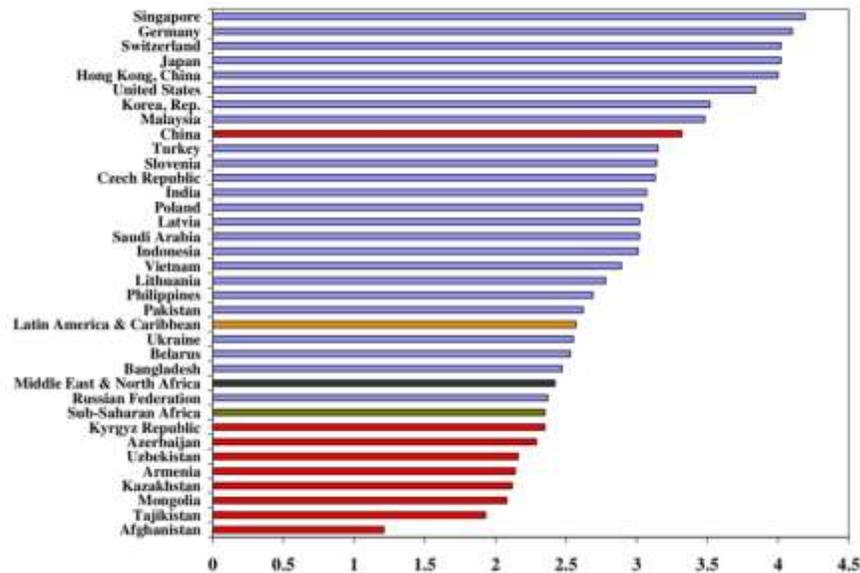
Figure 3: Cost of trading a 20-foot container



Source: World Bank (2007b).

Figure 4 provides a comparison of trade facilitation (measured by the LPI) in the Central Asian countries with other countries. Not only are the Central Asian countries ranked the lowest in terms of the overall index but are also at the bottom of the list when we compare different components of LPI. Clearly, there is scope for improving trade facilitation in the region.

Figure 4: Overall Logistics Performance Index (LPI), a measure of trade facilitation (TF) in Central Asian countries vis-à-vis other countries



Source: World Bank (2007a)

## CONCLUSION

To conclude we can say that non-tariff barriers play an important role in the revenue generation of the country. Most of the countries use tariff and Non-tariff barriers to protect their local industries and also to generate revenue. The most common type of Non-tariff trade barrier is protectionist barrier. Governments use this option to protect their local industries from the foreign competition.

Tariff has been used by countries to generate revenue but sometimes it can also be used for political gain. Some countries can use these tariffs to unfairly restrict the imports from certain countries for personal reasons. Thus World Trade Organization played an important role in persuading the member nations to reduce the tariffs.

Improvements in trade facilitation can lead to significant gains in trade in Central Asia. Infrastructure improvements lead to biggest gains in trade. Central Asian countries are landlocked and developing regional infrastructure will provide transport corridors for trade within the region and outside the region. Some measures such as improvements in customs administration and efficiency are relatively easier and cheaper to implement.

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