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"COMMENT" On

Richard G. Harris
"Market Access in International Trade: A Theoretical Appraisal"

by

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I would like to say first that I found Harris's paper very stimulating. The issue of market access has received practically no attention in the literature on international trade, and it is very useful to have him interpret it from a theoretical perspective. He has broken the topic down in a way that helps a great deal in thinking about it. The distinction that he makes in the three parts of the paper may, I believe, be appropriately characterized as concerning informal barriers to imports that arise from three sources: first from behavior of demanders, second from behavior of governments, and third from behavior of competing suppliers.

In the first category of barriers on the demand side he considers the possibility that demanders might show a preference for domestically produced goods. That such a preference would limit "market access" is clear. He devotes most of his remarks on this topic to trying to explain why such a preference might arise.

In the second category of barriers on the part of governments, he considers, not the formal trade barriers such as tariffs and quotas (or even VERs) that we usually discuss, but rather the phenomenon of so-called contingent protection. The reason that this is an informal barrier limiting market access is not that acts of contingent protection are themselves informal, for they are not, but rather the fact that a system of contingent protection creates an atmosphere of uncertainty about whether market access, once gained, will be preserved.

Finally, in the third category of barriers on the part of competing producers, Harris considers barriers to entry that participants in an imperfectly competitive market may be able to erect that, when the excluded potential entrants are foreign, constitute a barrier to market access.

My first question in commenting on this paper is to ask if Harris's categorization is complete. That is, are there significant ways that market access might be impeded that would not fall into one of these three categories? Try as I might, I have not been able to think of any such ways, as perhaps my own interpretation of the categorization in terms of demanders, suppliers, and government may make less surprising. Who else, after all, is there? I should say that within each category it would not surprise me to find other particular mechanisms than the ones he considers whereby barriers to market access might arise. But by and large my own conclusion is that Harris has done a fine job, hitting the major general modes that should concern us in a discussion of market access.

That being the case, the rest of my remarks will focus on just two issues that should be regarded as extensions of Harris's paper. The first is to ask whether demanders' preference for domestic goods, which is essentially the first of his three barriers to market access, really constitutes a valid grounds for policy intervention. The second is to ask whether this same three-fold classification can illuminate a discussion of another issue: that of market access in the context of international direct investment.

The Preference for Domestic Goods

Harris gives theoretical motivation to his discussion of barriers on the demand side by explaining and applying Akerlof's "social custom" model. He uses this to explain why demanders in a country may persist in a seemingly irrational preference for domestically produced goods over foreign goods that are objectively identical. His discussion of this model in connection with trade focuses primarily on the interesting dynamics that may cause such a preference to disappear, and this is of obvious importance in the context of trade policy.

I would like to devote a few of my remarks however to the much simpler question of whether such a preference, however it originates, should be properly considered grounds for trade policy action.

Suppose, much more simply than in the social custom model discussed by Harris, that consumers have a preference for domestically produced goods. It is clear that this preference, in comparison to a situation without it, will cause the country to trade less and, again in comparison to the situation without the preference, will improve its terms of trade exactly as if it had imposed a tariff. Does this make the importing country better off and the exporting country worse off? So long as the importing answer is unambiguous so long as the importing country is indeed large enough to influence the terms of trade by its behavior, the foreign country must lose unambiguously.

Is this grounds for a policy response? Not necessarily. Since the effects are so similar, the case for a policy response here can surely be no better than the case for a policy response to an effort to impose an "optimal tariff." And there the response makes sense only if the threat of the response may reasonably be expected to prevent the action in the first place. In the case of a preference for a domestic good, unless that preference is the result of a deliberate policy of, say, advertising that buyers should "buy domestic," it is quite likely that the preference would not be amenable to a policy change anyway. For without a government action to have caused it, the preference is not itself a deliberate action taken in cognizance of expected reactions. It is only a state of mind and is likely to be independent of foreign policies taken in response to it. If a protectionist response does not succeed in undoing the preference, it is only making matters worse.

This distinction between an autonomous preference for domestic goods and one that is somehow policy induced is also important, I believe, at another more philosophical level. My own view is that there is nothing wrong with a preference for domestic goods, even though such a preference does indeed restrict market access and thus trade, and even though it can be argued to be harmful to a country's trading partners, so long as that preference arises "naturally" and not as the result of a deliberate government policy.

To put it another way, suppose that there are domestic and imported goods that are in every way objectively identical except that it is somehow known where each of the goods was produced, and suppose that domestic demanders (consumers or producers, either one) have nonetheless a preference for the domestic goods. Presumably this means that buying the domestic good makes them "feel better" (or that buying the foreign good makes them "feel worse"). Such preferences I believe to be as legitimate as any others, and should not be taken as proper grounds for a policy response by other countries. One might argue that the country itself could be better off if it were not, in this way, so irrational, and perhaps an educational campaign should be undertaken to rid the public of the misperception, but that is a domestic issue. Given the preference itself, then, the economics of trade and its effects are just the same as if the preference did not exist, and I cannot see that the case for a foreign tariff is improved by it.

Direct Investment

I consider now whether Harris's framework may be helpful in understanding barriers to international direct investment as well as barriers to trade. Let me say first, though, that I am not convinced that barriers to direct investment should necessarily be viewed as undesirable, in the same manner as barriers to trade. To me, international factor movements impinge on national sovereignty in a way that trade does not. Perhaps foreign factors should be "invited in" and not presumed to be welcome guests.

On the demand side, it is clear that a subsidiary of a foreign corporation can be viewed just as skeptically, when it tries to sell its products, as can a foreign exporter, and thus that a preference for domestic goods may interfere with the success of a direct investment. However, one advantage of direct investment is precisely that it allows the foreign producer to take on certain characteristics of a domestic producer and thus to avoid such adverse preferences. In that sense, if one accepts such preferences as being legitimate, as I do, then one may object to foreign direct investment itself as being a means of misleading people about their true preferences—a kind of false advertising, if you will.

Next consider market access for investment as it may be impeded by government intervention. Here again it seems that investment serves precisely the purpose of getting behind a wall even of contingent protection, and thus provides greater security of market access. In some countries this appearance of security is misleading, however, since by locating within a country the foreign firm exposes itself to the even more serious possibility of expropriation. In some countries I would think the possibility that a firm might be nationalized or expropriated would be a prohibitive barrier to market access for direct investment.

Finally, consider barriers on the side of the competing producers. Presumably, whatever competing sellers can do to exclude a seller of exports they can also do to exclude sales by a foreign-owned domestic producer. However, an additional possibility also exists, involving the many other economic transactions that a foreign firm must enter into within the country if it engages in production there. For example, competing firms may put pressure on domestic labor not to work for the foreign firm, or not to work on the same terms as they do for the domestic producers. Or they may use their connections with local banks to make it difficult for the foreign firm to obtain local financing. Indeed, for every transaction that a local producer must undertake, there is the potential for domestic producers to interfere in some way with the conduct of that transaction and thus make successful operation more difficult. Thus I would think that the scope for this kind of inference would be much greater for direct investment than for trade.

These considerations lead me, as a last point, to observe that the three-fold classification that I have been pursuing here is not sufficient for the area of direct investment. Instead, there is a fourth category that should be considered. Since a producer must necessarily make a number of purchases in domestic markets, market access can be impeded also by preferential behavior on the part of domestic sellers—not competing ones such as Harris considers in his discussion of barriers to entry—but sellers of all of the many inputs, including labor, that a producing firm would have to buy, or prefer to buy, on the local market. As just one example, if labor is reluctant to work for a foreign firm, then direct investment will be seriously impeded. Again, however, I would not be inclined to view such a preference as grounds for policy action, but would rather insist that we respect that preference as legitimate, even though we may not approve of it.