Trade Agreements / Policies

Trade Policy

Unilateral Policies ①

Agreement

Multilateral Agreement ②

 Preferential ③

① US Trade Law
   - Antidumping
   - Safeguards (Section 201)
     (Temporary Protection)
   - Section 301
     (Unilateral Retaliation)

② Early GATT (1947)
   - Liberalizing Trade
   - Rules of Trade
   - Dispute Resolution

WTO
   - Expanded set of rules (ex: IPR’s)
   - Stronger dispute resolution mechanism
     (Ability to punish is higher, faster process)

③ WTO has the PTA waiver
DISPUTE RESOLUTION

- Complaint
- Panel Rules
- Entire GATT/WTO Apples Ruling

APPROVAL RULES

GATT
UNANIMITY TO ACCEPT

WTO
UNANIMITY TO REJECT

- Compliance OR
  Punishment
HBS
COMMERCIAL/CIVIL AIRCRAFT (100+ PASSENGERS)

IMPORTANT ISSUES

1. R&D / TECHNOLOGY / COST STRUCTURE / SALES
2. 3 COMPANIES PROFILE
3. PRODUCTION OF INPUTS / SALES LINK
4. PRICING COMPETITION
5. INDUSTRY - GOV. INTERACTION

II. LARGE R&D & DEVELOPMENT

LAUNCH INVESTMENT

DEVELOPMENT / CERTIFICATION
BEFORE PROD. BEGINS.
≈ 5 YEARS

TOTAL COST = PARTS + DIRECT EXPENSES + LAUNCH INVEST.

BREAK EVEN ≈ 400 UNITS
(10-12 YEARS AFTER LAUNCH)
Sales: Economies of scale in maintenance

Traffic growth

Demand

Big private companies

Small Government-owned airlines overseas

3 Companies

Boeing, McDonnell Douglas, Airbus

US (1916)

Military/Space programs

US (1920)

Government orders

1970

France

Germany

Spain

UK

R&D financing by Government

(70-90%) (loans)

Sales/Input production

Pricing
Pricing → Deferred Seat Plan → Trade in of competitor's aircraft → Walk in Leave → Government Intervention (Sales Assistance) → Government - Industry interaction → R&D & production subsidies → Sales assistance / outsourcing / sales / link → Disputed WTO agreements
1992: EC & US Bilateral Agreement

Objective: Regulate and limit Gov. Support

Achieved Objective

Dispute start later after EC Airbus gets 50% of market share
1992 EC/US Agreement on Trade in Large Civil Aircraft

- Until the late 70s the US enjoyed almost a de facto monopoly in the LCA sector.

- The Airbus consortium (created in 1969) started competing effectively in the 80s. At that stage the US became concerned about the European competition and the alleged subsidies paid by the European governments for the developments of the early models of the Airbus family. This became a major issue of contention.
The European side was equally concerned by subsidies accruing to US LCA manufacturers through NASA and Defense Programs.

The EU and the US started bilateral negotiations for the limitation of government subsidies to the LCA sector in the late 1980s. Negotiations were concluded in 1992 with the signature of the EC-US Agreement on Trade in LCA which focuses on the limitation of both direct and indirect government support.
Limits to Indirect Support

- The agreement establishes that indirect support (i.e. benefits provided for aeronautical applications of NASA or military programs) should be limited to a 3% of the nation's LCA industry turnover (gross revenue) and 4% of the value of the firm's annual sales.

- This discipline is primarily targeted to the support system in use in the US. In contrast to the European system of repayable royalty-based loans, since the repeal of the US rules on recoupment (reimbursement), there is no requirement for indirect support to be reimbursed.
Limits to Direct Support

- The agreement puts a ceiling on the amount of direct government support (33% of the total development costs) for new aircraft programs.

- It establishes that such support (granted in the form of repayable royalty-based loans) will be repaid at an interest rate no less than the government cost of borrowing and within no more than 17 years. Basically, this discipline applies to the form of government support in use in Europe.
• The large civil aircraft sector is generally subject to the WTO rules on subsidies, although more specific multilateral rules exist regarding forms of government support.
Laura D’Andrea Tyson

- 1992 Agreement achieved its objective: to limit profit shifting subsidies keeping some subsidies needed due to the economic characteristics of the industry
Irwin-Pavcnik: two questions

- Did the 1992 Agreement have a significant impact on pricing?
- What is the impact of the introduction of the A380 on prices and market shares of other wide body aircraft (specially the Boeing 747)?
Theory

Boeing and Airbus: multiproduct firms

- Existing models sales and prices are sensitive to introduction of new models.

- Bertrand or Cournot competition give very similar results.
Answers:

• The agreement seems to have increased Airbus and Boeing prices of both narrow and wide body aircraft by 3%. Also consistent with increases of about 5% in MC’s.

• Introduction of A380 has a significant negative effect on prices and market shares of other wide body aircraft. Effect on other Airbus wide body (A330 and A340) is even larger than that effect on Boeing 747.