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TOPIC:- ANALYSIS OF FREE TRADE POLICY

Policy of non-interference by government in foreign trade is referred to as "free trade." Free trade policy implies absence of any artificial restriction on or obstacle to the freedom of trade of a country with other nations. According to Adam Smith, the term 'free trade' is used to denote "that system of commercial policy which draws no distinction between domestic and foreign commodities and, therefore, neither imposes additional burdens on the latter, nor grants any special favour to the former." In other words, free trade implies complete freedom of international exchange. Under such a policy, there are no barriers to the movement of goods among countries and exchange can take its perfectly neutral course. Classical economists like Adam Smith, Ricardo and others pleaded for free trade for the welfare of the world.

Advantages of Free Trade:—

Following are the advantages of free trade policy :—

(1) Comparative cost advantage:—

Free trade is the natural outcome of the comparative costs advantage. It permits an allocation of resources and manpower in accordance with the principle of comparative advantage, which is just an extension of the principle of division of labour.

(II) More factor earnings:-

Under free trade, factors of production will also be able to earn more, as they will be employed for better use. Hence, wages, interest and rent will be higher under free trade than otherwise.

(III) Cheaper imports:-

Free trade produces or procures import at cheap rates. It seems to be an attractive argument in favour of trade at least from the customer's point of view. However, it ignores the question of employment and the interests of producers in importing country. Here, it has been pointed out that under free trade, when consumers gain through lower prices, producers also gain as the factors of production are directed to more gainful and specialised production which gives better earnings.

(IV) Enlarged market:-

Free trade widens the size of the market as a result of which greater specialisation and a more complex division of labour become possible. This brings about optimum production with costs reduced everywhere, benefiting the world as a whole.

(V) Competition from abroad:-

Free trade policy encourages competition from abroad which induces

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domestic producers to become more alerts and improve their efficiency.

(VI) Restricted exploitation:-

Free trade prevents growth of domestic monopolies and consumers' exploitation due to competition from abroad.

(VII) Greater welfare:-

Free trade permits large varieties of consumption goods and improves consumer's welfare.

Disadvantages of Free Trade:-

Following are the disadvantages of free trade policy:-

(I) Free trade policy runs smoothly if all the countries follow the same. If some countries do not adopt it, the system can not work gainfully.

(II) Free trade may prove advantageous to developed and technologically advanced nations but less developed countries are certainly at a disadvantage on account of unfavourable terms of trade.

(III) Competition induced under free trade is unfair and unhealthy. Backward countries cannot compete with advanced countries.

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(IV) Gains of trade are not equally distributed under free trade due to unequal state of development of different countries.

(V) A country with unfavourable balance of payments finds it difficult to overcome this situation under free trade policy.

(VI) Free trade may encourage interdependence and discourage self-sufficiency. But, in the matter of defence, each country should have self-reliance and self-sufficiency as far as possible.