

Economics of the Arms Trade

International trade theories

- Absolute advantage
- Comparative advantage: Ricardo
- Heckscher-Ohlin
 - difference in factor endowments
 - Leontief paradox
- Specific factors model: short run capital immobile across industries so earnings to capital can vary
- New trade theories –most countries that trade have similar endowments –monopolistic competition

International arms trade

- Not that important relative to total trade
- Important for foreign policy and politics
- Important for certain industries
- Secrecy and definitional difficulties make analysis difficult
- Not clear general trade theories help very much as market distorted by non economic concerns

Nature of the Arms Trade

- It is useful to categorise the commodities of the arms trade in decreasing lethality or proximity to lethality as:
 - Weapons of mass destruction (nuclear, chemical, biological weapons and long-range missiles);
 - Major 'conventional' weapons (ships, aircraft, missiles, tanks etc.);
 - small arms (guns, ammunition, grenades etc.)
 - 'dual use' equipment (electronic communications equipment, computers, transport vehicles etc.);
 - spare parts, weapon training and maintenance;
 - torture and other such security, interrogation and anti-insurrection equipment; and
 - technology, chemicals and other raw materials and components used to manufacture weapons.
- All have different levels of national and international control.

Arms trade

- SIPRI estimates major weapon systems are exports \$20bn a year in 1990 prices 200-4
- US and Russia account for half
- About 60% goes to developing countries

Some historical context

- Organised arms production on a large scale has a long history
- Government restrictions on weapons sales common
- Modern industry dates from mid 19th century
- Before WW1 thriving market was largely unregulated and global
- After WW2 shaped by Cold War and concern for comprehensive DIB

Some historical context

- Restrictions on trade and technology to non allies and potential allies -COCOM
- Later commercial interests became more important
- With decreasing demand and increasing fixed costs exports needed
- As shall becomes increasingly complex market and profitability questionable.

Global Weapons Market

- Theoretically might expect the market to be close to perfectly competitive –many buyers and sellers etc
- But it is far from it
- Few companies are private entities in reality
- National government's have direct influence on imports and exports

Demand for arms

- As we have seen:
 - World military expenditure and procurement trends in post Cold War world
 - Domestic procurement
 - Arms Exports
 - Government to government
 - Firms to government

Supply

- Sources of supply: domestic vs trade
- The world arms industry: globalisation
- Economies of scale and high mes
- Push for exports –government support
- Recognition of security issues

Price determination

- Domestic prices Government determined
- Credible threats
- International prices not necessarily market determined
- Government influence/support
 - Export credit guarantees
 - Marketing and other support

Price determination

- Often sell package of arms + services + spares etc so price obscured
- Offsets Offset arrangements similar effect
- Aid budgets
- Commissions and bribes
- Technology transfer and licensing
- Prop of UK components in exports

Effect of Quota

- Restrictions such as quotas, sanctions and export licensing and control
- Can show how creates deadweight loss in principle
- But not so simple as restricting exports may have security benefits –taking arms away from the bad guys

National returns: a good investment?

- Have seen hidden costs
- Companies vs whole economy
- Benefits licence fees etc
- Benefit provision training, spares etc
- Stagnant market?
- Changing nature of industry
- Overall estimates suggest a relatively large subsidy

Economic Effects

- Reduce costs of maintaining DIB but other costs:
- support jobs but diverts resources
- crowding out
- spin off vs spin in
- creates demand vs bottlenecks
- socio political effects
- role of MIC –vested interests

Economic Effects

- Various studies: Institutional and historical; econometric; simulation; etc
- Simple arguments of economic benefits are misleading
- hidden costs of exports
- link with aid and finance of exports
- exports can destabilise
- So: few economic problems in reducing arms exports

Conclusions

- Arms trace is complex –different markets exist eg SALW, second hand
- Linked with restructuring of the industry and procurement
- Important role of national governments
- Not transparent and potential damaging
- Not obviously profitable to economies though is to indiv companies

Conclusions

- Need concern over lack of international control
- Arms Trade treaty being supported by NGOs and governments –going beyond UN Register
- Useful to keep economics in mind given way often used justify arms exports but clearly doesn't add up
- Arms controls unlikely to have any damaging economic effects