International Trade

Resource Distribution and Trade

- Each country of the world possesses different types and quantities of land, labor, and capital resources.
- By specializing in the production of certain goods and services, nations can use their resources more efficiently.
- Specialization and trade can benefit all nations.

Absolute and Comparative Advantage

- A person or nation has an **absolute advantage** when it can produce a particular good at a lower cost than another person or nation.

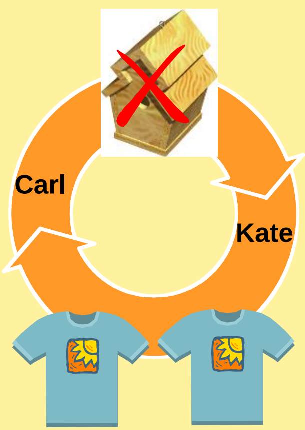
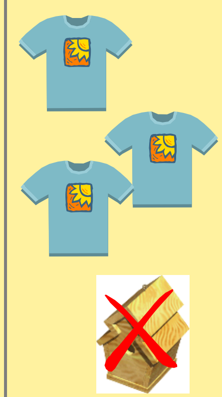
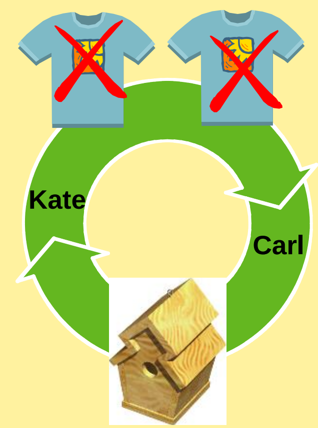
- **Comparative advantage** is the ability of one person or nation to produce a good at a ***lower opportunity cost*** than that of another person or nation.

The **law of comparative advantage** states that nations are better off when they produce goods and services for which they have a comparative advantage in supplying.

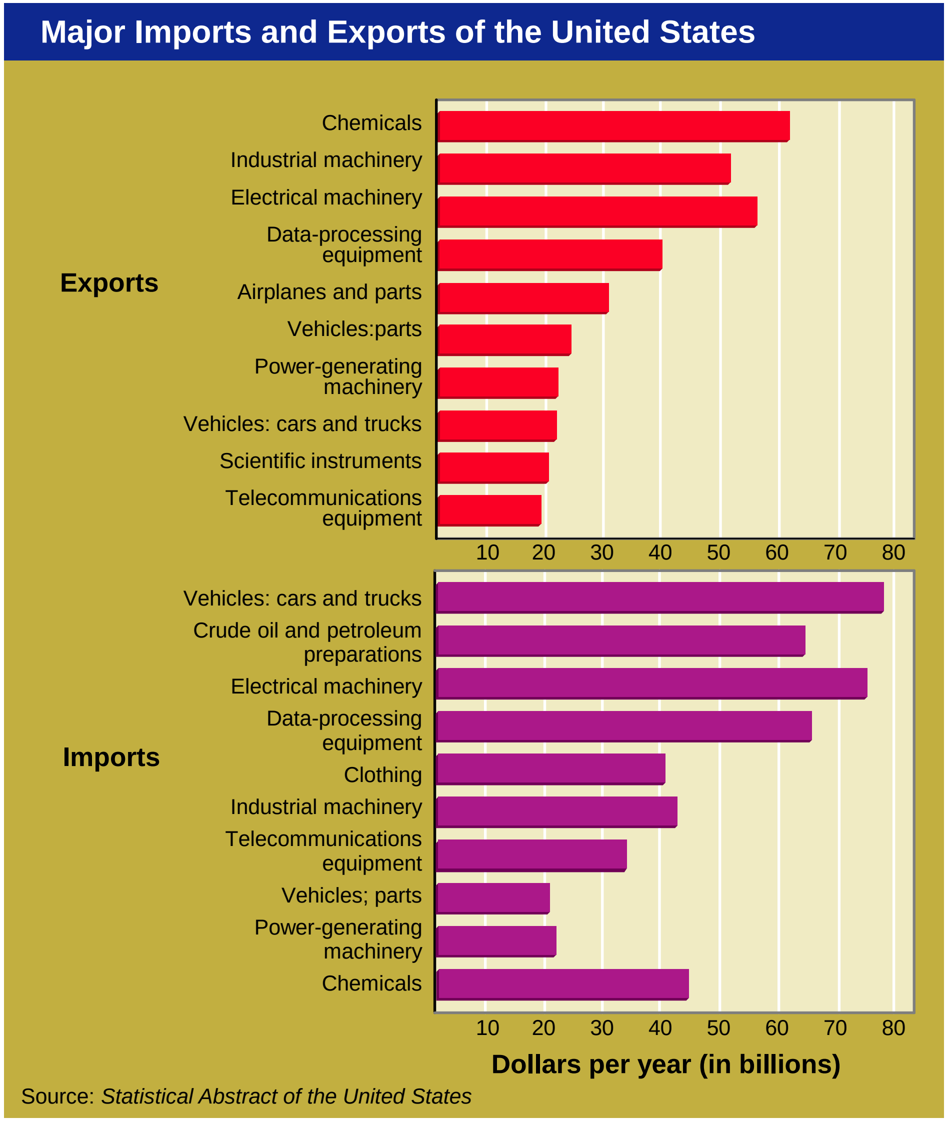
Benefits of Trade

In this example, both Kate and Carlos benefit from specialization.

Benefits from Specialization and Trade for Carl and Kate

Carl			Kate		
Specialization	**Trade**	**Net Effect**	**Specialization**	**Trade**	**Net Effect**
					
Carl specializes, switching 2 hours from T-shirt production to birdhouse production.	Carl trades 1 birdhouse for 2 T-shirts.	Net effect is same number of T-shirts and 1 more birdhouse.	Kate specializes, switching 1 half-hour from birdhouse production to T-shirt production.	Carl trades 2 T-shirts for 1 birdhouse.	Net effect is same number of birdhouses and 1 more T-shirt.

Imports and Exports of the United States



- The United States is the world's largest exporter.
- The United States is also the world's largest importer.
- The United States' main trading partners are Canada, Mexico and Japan.

Trade and Employment

As nations begin to specialize in certain goods, dramatic changes in the nation's employment patterns also occur.

Specialization and Unemployment

- Workers who lose their jobs due to specialization face three options:
  - inability to adapt and find a new job
  - **Relocation:** moving to where current skills meet current jobs
  - **Retraining**: gaining new human capital to meet the demands of specialized labor markets

What Are Trade Barriers?

A **trade barrier** is a means of preventing a foreign product or service from freely entering a nation's territory.

Import Quotas An **import quota** is a limit on the amount of a good that can be imported.	***Voluntary Export Restraints*** A **voluntary export restraint (VER)** is a self-imposed limitation on the number of products shipped to a certain country.
Tariffs A **tariff** is a tax on imported goods, such as a customs duty.	***Other Barriers to Trade*** Other barriers to trade include high government licensing fees and costly product standards.

The Effects of Trade Restrictions

Increased Prices for Foreign Goods

- Tariffs and other trade barriers increase the cost of imported products, making domestic products more competitive.
- Although manufacturers of many products may benefit from trade barriers, consumers can lose out.

Trade Wars

- When one country restricts imports, its trading partner may impose its own retaliatory restrictions.

Arguments for Protectionism

Protectionism is the use of trade barriers to protect a nation's industries from foreign competition.

Protecting Jobs

- Protectionism shelters workers in industries that would be hurt by specialization and trade.

Protecting Infant Industries

- Protectionist policies protect new industries in the early stages of development.

Safeguarding National Security

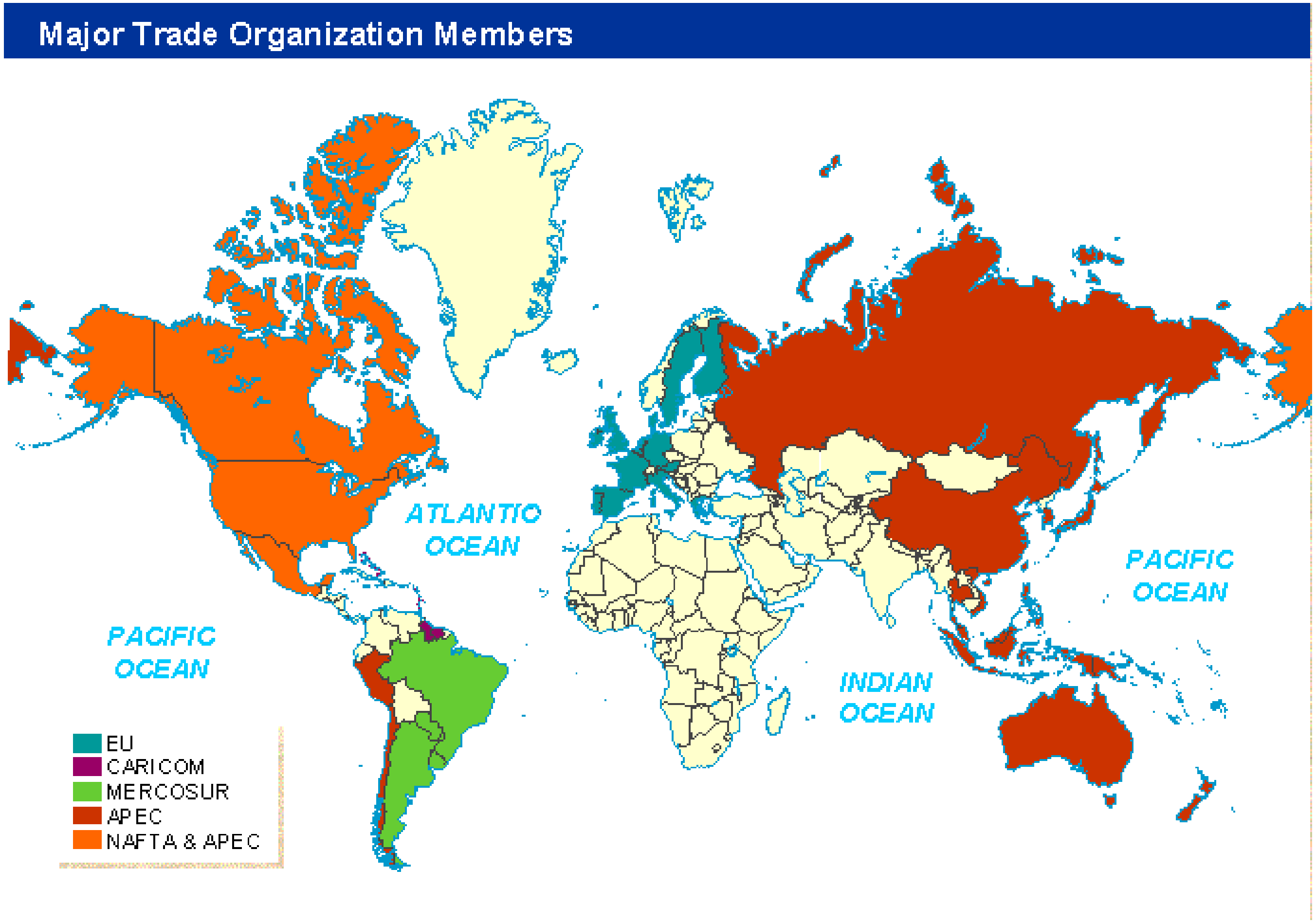
- Certain industries may require protection from foreign competition because their products are essential to the defense of the United States.

International Cooperation

- Recent trends have been toward lowering trade barriers and increasing trade through international trade agreements.
- In 1948, the General Agreement on Tariffs and Trade (GATT) was established to reduce tariffs and expand world trade.
- In 1995, the **World Trade Organization (WTO)** was founded to ensure compliance with GATT, to negotiate new trade agreements, and to resolve trade disputes.

Global Trade Agreements

Many nations have formed regional trade organizations. These trade organizations establish **free-trade zones**, or regions where a group of countries has agreed to reduce trade barriers among themselves.



Exchange Rates and International Markets

The value of a foreign nation's currency in relation to your own currency is called the exchange rate.

- An increase in the value of a currency is called **appreciation.**
- A decrease in the value of a currency is called **depreciation.**
- Multinational firms convert currencies on the foreign exchange market, a network of about 2,000 banks and other financial institutions.

Reading an Exchange Rate Table

The following table shows an example of exchange rates.

Foreign Exchange Rates

	U.S. $	Aust $	U.K. £	Canadian $	¥en	Euro	Mexican NP	Chinese renminbi
U.S. $	1	0.6489	1.599	0.6764	0.01	1.051	0.11	0.12
Australian $	1.541	1	2.465	1.042	0.01	1.62	0.17	0.19
U.K. £	0.6252	0.4057	1	0.4229	0.01	0.657	0.07	0.08
Canadian $	1.478	0.9593	2.365	1	0.01293	1.554	0.16	0.18
¥en	114.3	74.19	182.9	77.34	1	120.2	12.24	13.81
Euro	0.9516	0.6175	1.522	0.6436	0.01	1	0.1	0.11
Mexican nuevo peso	9.33	6.06	6.3	6.3	0.08	9.81	1	1.13
Chinese renminbi	8.28	5.37	13.25	5.6	0.07	8.7	9.8	1

Types of Exchange Rate Systems

Fixed Exchange-Rate Systems

- A currency system in which governments try to keep the values of their currencies constant against one another is called a **fixed exchange-rate system.**

Flexible Exchange-Rate Systems

- **Flexible exchange-rate systems** allow the exchange rate to be determined by supply and demand.

Balance of Trade

The relationship between a nation's imports and its exports is called its balance of trade.

- When a nation exports more than it imports, it has a **trade surplus**.
- When a nation imports more than it exports, it creates a **trade deficit**.

The United States Trade Deficit

The Trade Deficit

- The United States has run a trade deficit since the early 1970s.

Why the Trade Deficit?

- Imports of foreign oil as well as Americans' enjoyment of imported goods account in part for the large American trade deficit.

Reducing the Trade Deficit

- Quotas and other trade barriers can be used to raise prices of foreign-made goods and urge consumers to buy domestic goods.