Globalisation, trade and international finance

Edexcel IAL Economics WEC14 sections 4.3.1-4.3.3 full package

Topic 7 at a glance

> Countries specialise, trade, protect, and settle up in currencies.

- WEC14 spec sections 4.3.1 to 4.3.3.
- **Tariff** model: $Qd = 140 - 2P$, $Qs = 20 + 4P$.

What drove globalisation

> Freer trade, more blocs, political change, cheap transport, bigger TNCs.

- Trade, TNCs and **migration** all grew.
- Costs: displaced workers, **transfer pricing**.

FDI cuts both ways

Benefits	Costs
investment and jobs	crowding out
technology	profit repatriation
tax revenue	influence over policy

Worked: comparative advantage

1. **Cost of 1 cloth** A gives up 2 wheat; B gives up 1
2. **Specialise** A in wheat, B in cloth
3. **Trade at 1.5** A pays 1.5, not 2; B gets 1.5, not 1

Decision

Both gain: **comparative advantage** is the lowest **opportunity cost**.

Worked: the terms of trade

1. **Formula** export prices ÷ import prices × 100
2. **Tanzania (SAM)** 128.9 ÷ 117.1 × 100
3. **Result** 110.1

Decision

Terms of trade 110.1: a 10.1% improvement.

Four stages of a trading bloc

Stage	Adds
free-trade area	no internal barriers
customs union	a common external **tariff**
common market	free movement of labour and capital
monetary union	a shared currency

Trade creation or diversion?

Trade creation

cheap partner goods

replace dear domestic

welfare gain

Trade diversion

dear partner goods

replace cheap world goods

welfare loss

A tariff, drawn

A **tariff** of 4: imports 48 to 24, revenue 96, **deadweight loss** 48.

- Consumers lose 448.
- Producers gain 304.

Why and how countries protect

Motives	**Types**
infant industries	tariffs
jobs, national security	quotas
against **dumping**	non-tariff barriers
deficit, revenue	subsidies to producers

Three exchange-rate systems

System	Rate set by	A fall is
fixed	the state, pegged	**devaluation**
managed	market, within a band	depends
floating	the market	**depreciation**

The J-curve, drawn

> After a **depreciation**, the trade balance worsens first, then may improve.

- Marshall-Lerner: $|\text{PED X}| + |\text{PED M}| > 1$.
- Dearer imported inputs add inflation.

International competitiveness

Influences

productivity, skills

exchange rate, wage costs

infrastructure

Ways to raise it

education and training

investment incentives

deregulation

Data response: Egypt's float

1. **Before** $1 \div 30.9 \approx$ US\$0.0324
2. **After** $1 \div 49.5 \approx$ US\$0.0202
3. **Change** $(0.0202 - 0.0324) \div 0.0324 \approx -38\%$

Decision

The pound's value fell about 38%.

Data response: will the current account improve?

Likely to improve	May not
cheaper tourism	wheat, fuel inelastic
remittances via banks	canal fees in dollars
fewer luxury imports	inflation erodes the gain

Check yourself

Question	**Answer**
A: 1 cloth = 2 wheat; B: 1 = 1?	A wheat, B cloth
Export 128.9, import 117.1?	terms of trade 110.1
Tariff 4 at world price 12?	imports 24, revenue 96
30.9 to 49.5 per dollar?	pound falls about 38%
Worse first, then better?	the **J-curve**