

International Trade & Globalisation

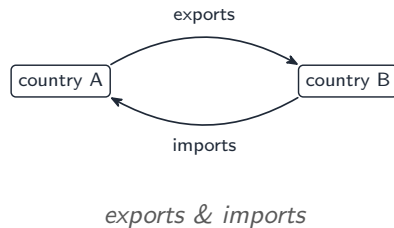
IGCSE Economics ■ Topic 6

IGCSE Economics



What we will cover

- 1 Specialisation & free trade
- 2 Globalisation & MNCs
- 3 Trade protection
- 4 Tariffs
- 5 Exchange rates
- 6 Balance of payments





Specialisation and free trade

Countries **specialise** in what they make best, sell **exports** & buy **imports** .

Free trade gives cheaper goods & more choice, but home firms may struggle to compete.



Specialisation and trade raise living standards

Specialisation and free trade – gains



more goods for everyone

Countries **trade** with each other: they sell some goods and buy others.

Just as one worker can focus on one task, a whole country can focus on making the goods it is best at.

Globalisation and MNCs

- **globalisation** – economies joined by trade, travel & the internet
- **MNCs** – bring jobs & investment, but profits may flow abroad



Trade and capital link national economies

Trade protection

Protection shields home firms:

- **tariffs** – a tax on imports
- **quotas** – a limit on imports
- **subsidies** & rules

Trade protection, in detail

Tariff

a tax on imports

Quota

a limit on import amount

Subsidy

money to home firms

Embargo

a total ban on trade

Exam: tariff = tax; quota = quantity limit; subsidy = home support; embargo = ban

The four main methods of trade protection

The arguments for protection, and the tools

Infant industry

The **infant industry** argument: protect a young industry until it is large enough to compete – and the hard part is ever removing the protection.

Dumping

Dumping : selling exports below cost to drive out **domestic** rivals. Protection here is a response, not an aggression.

Subsidy

A **subsidy** lowers a home producer's costs, so it undercuts imports without a tariff appearing anywhere.

The cost

Every tool raises prices or taxes at home, and invites retaliation – so the country becomes less **dependent** on trade, and poorer.

State who gains and who pays. Protection is always a transfer, never a free rescue.

Multinational companies

A **multinational company** (MNC) is a firm that produces in more than one country – for example, a car maker with factories in several countries.

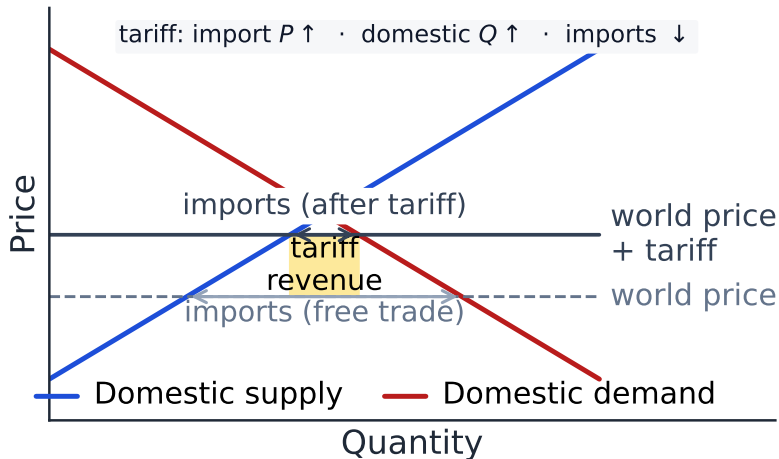
- **Benefits** to the host country: new jobs, investment, new skills and technology, and more tax.
- **Drawbacks**: profits may flow back to the MNC's home country; local firms may be pushed out; and some MNCs pay low wages or pollute (for example.

Tariffs

A **tariff** raises the import price above the world price.

This protects home producers & raises tax, but raises prices for consumers.

Tariffs, in detail



A **tariff** raises the import price above the world price.



Exchange rates

Appreciation (a stronger currency) makes exports **dearer** & imports **cheaper**.

Depreciation does the reverse.

Appreciation

(currency rises in value)

exports dearer,
imports cheaper →
exports fall, imports rise

Depreciation

(currency falls in value)

exports cheaper,
imports dearer →
exports rise, imports fall

Exam: appreciation hurts export competitiveness; depreciation can boost net exports (SPICED)

Balance of payments

The **balance of payments** records money in & out.

- exports $>$ imports – a **surplus**
- imports $>$ exports – a **deficit**

exports (money in) $>$ imports (money out)
= a surplus

imports $>$ exports = a deficit

The four parts of the current account, and free trade's cost

trade in goods

visible exports minus visible imports

trade in services

exports and imports of services – tourism, banking, shipping

primary income

wages, interest and profit **earned from abroad**

secondary income

money sent **with nothing given in return** – aid, and remittances

a surplus

the total is positive; a deficit means the country buys more from abroad than it sells

free trade's cost

new, small industries may never grow if they face strong foreign rivals from the start – the infant-industry argument

A deficit is not automatically bad. It matters how it is financed and whether the imports build future capacity – which is what an evaluation question wants.

Correcting a deficit

A country with a large deficit must borrow money or sell assets to pay for it.

- cut total demand, so people buy fewer imports.
- let the currency depreciate, to make exports cheaper and imports dearer.
- use trade protection (tariffs and quotas) to cut imports.
- use supply-side policy to improve the **competitiveness** of its firms, so exports rise.

Exam tips

- To convert currency: pounds $\rightarrow$ dollars, *multiply* by the rate; dollars $\rightarrow$ pounds, *divide* by the rate.
- When a currency **appreciates**, its exports become dearer and its imports cheaper (so exports fall, imports rise); a **depreciation** does the opposite.
- **Trade protection** (tariffs, quotas, subsidies, embargoes) can protect jobs and infant industries, but it raises prices, cuts choice, and can start a trade war.
- A **current account deficit** means more money flows out than in. It can be reduced by cutting demand, letting the currency depreciate, or improving competitiveness.



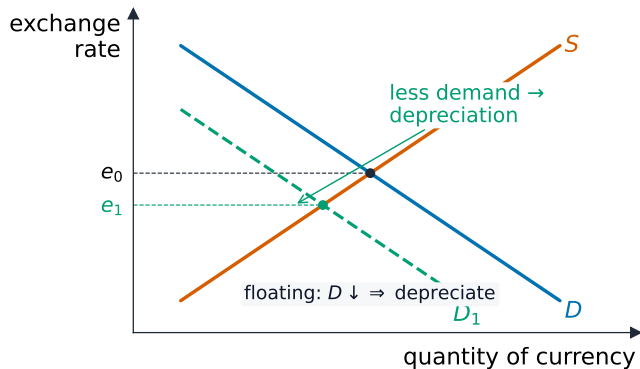
Worked example – using an exchange rate

£1 = \$1.30. (a) A UK machine costs £2,000 – price to a US buyer? (b) A US laptop costs \$650 – cost to a UK buyer?

- (a) Going from pounds to dollars: multiply.
- $2,000 \times 1.30 = \$2,600$
- (b) Going from dollars to pounds: divide.
- $650 \div 1.30 = \text{£}500$

Check the answer is sensible: £1 buys more than a dollar, so a pound price becomes a bigger dollar number. If it looks wrong, you divided instead of multiplying.

How the rate is set



The exchange rate is set where demand for the currency meets supply. If demand falls ($D \rightarrow D_1$), the rate falls – a depreciation.

Exchange rates and the current account

Floating exchange rate

A **floating exchange rate** is set by demand for and supply of the currency, and moves every day.

Fixed

A fixed rate is held by the central bank buying and selling its own currency – which needs reserves.

Depreciation

A weaker currency makes exports cheaper abroad and imports dearer at home.

Current account surplus

A **current account surplus** means the country sells more abroad than it buys; a deficit is the reverse.

A depreciation improves the current account only if demand is elastic enough on both sides – the Marshall–Lerner condition.

Topic 6 – key takeaways

1

Free trade

specialise; cheaper goods & more choice

2

Protection

tariffs, quotas & subsidies

3

Exchange rates

appreciation: dear exports, cheap imports

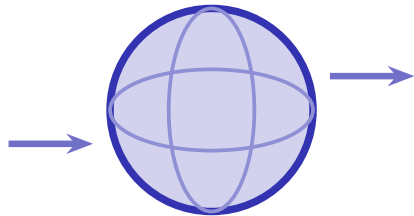
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Payments

exports vs imports: surplus or deficit

Check yourself

- 1 What is a good a country buys from abroad?
- 2 What is a tariff?
- 3 What does a stronger currency do to exports?
- 4 When is the balance of payments in surplus?



Answers 1. an import 2. a tax on imports 3. makes them dearer 4. when exports exceed imports