Imports and How They Affect the Economy

Imports are foreign goods and services bought by citizens, businesses, and the government of another country. It doesn't matter what the imports are or how they are sent. They can be shipped, sent by email, or even hand-carried in personal luggage on a plane. If they are produced in a foreign country and sold to domestic residents, they are imports.

Even tourism products and services are imports. When you travel outside the country, you are importing any souvenirs you bought on your trip.

Imports and the Trade Deficit

If a country imports more than it exports it runs a trade deficit. If it imports less than it exports, that creates a trade surplus. When a country has a trade deficit, it must borrow from other countries to pay for the extra imports. It's like a household that's just starting out. The couple must borrow to pay for a car, house, and furniture. Their income isn't enough to cover the necessary expenses that improve their standard of living.

But, like the young couple, a country should not continue to borrow to finance its trade deficit. At some point, a mature economy should become a net exporter. At that point, a trade surplus is healthier than a deficit.

Why? First, exports boost economic output, as measured by gross domestic product. They create jobs and increase wages.

Second, imports make a country dependent on other countries' political and economic power. That's especially true if it imports commodities, such as food, oil, and industrial materials. It's dangerous if it relies on a foreign power to keep its population fed and its factories humming. For example, the United States suffered a recession when OPEC embargoed its oil exports.

Third, countries with high import levels must increase their foreign currency reserves. That's how they pay for the imports. That can affect the domestic currency value, inflation, and interest rates.

Fourth, domestic companies should be able to compete with foreign companies that import similar goods and services to their businesses. Small businesses that

can't compete may fail. Small businesses added 1.8 million net new jobs in 2019. The U.S. has 30.7 million small businesses that 47.3 percent of the private workforce.

And finally, exports help domestic companies gain a competitive advantage.

Through exporting, they learn to produce a variety of globally-demanded goods and services.

Four Ways Countries Increase Exports

Countries often increase exports by increasing trade protectionism. That insulates their companies from global competition for a while. They impose tariffs (taxes) on imports, making them more expensive.

The problem with this strategy is that other countries soon retaliate. A trade war hurts global trade in the long run. In fact, this was one of the causes of the Great Depression.

As a result, governments are now more likely to provide subsidies to their industries. The subsidy lowers business costs so they can reduce prices. This strategy may lower the risk of retaliation. If other countries complain, the government can say the subsidies are temporary. For example, India claims the subsidy allows its poor to afford basics like fuel and food. Some emerging markets protect new industries. They give them a chance to catch up with technology in developed markets.

A third way countries boost exports is through trade agreements.

Once protectionism has lowered trade, countries may see the wisdom in reducing tariffs. The World Trade Organization almost succeeded in negotiating a global trade agreement. But the European Union and the United States refused to end their agricultural subsidies.

As a result, countries rely on bilateral and regional agreements.

Countries try to increase exports by lowering their currency value. That has the same effect as subsidies. It lowers the prices of goods. Central banks reduce interest rates or print more money. They also buy foreign currency to raise its value. Countries like China and Japan are better at winning these currency wars.

The United States can produce everything it needs, but emerging market countries can make many consumer items for less. The cost of living is low in China, India, and other developing countries. They can pay their workers less, creating a comparative advantage.

The United States is a free market economy that's based on capitalism. These low-cost imports cost American jobs. U.S. companies cannot both pay a living wage and compete on price.