International Trade

International trade is the exchange of goods and services between countries. This type of trade gives rise to a world economy.

Importance:

- Trading globally gives consumers and countries the opportunity to be exposed to goods and services not available in their own countries.
- Almost every kind of product can be found on the international market: food, clothes, spare parts, oil, jewellery, wine, stocks, currencies and water.
- Services are also traded.
- Imports and exports are accounted for in a country's current account in the balance of payments.
- Global trade allows wealthy countries to use their resources more efficiently.

The basis of international trade

The comparative cost theory developed by David Ricardo illustrated it in 1817 by using two country, two commodity model.

Country	Labour units/unit of cloth	Labour units/unit of wine	Exchange ratio between wine and cloth
England	100	120	1 wine : 1.2 cloth 120/100
Portugal	90	80	1 wine : 0.88 cloth 80/90

Portugal has an absolute superiority in production of both cloth and wine. Law of comparative advantage indicates that a country should specialise in the production of that commodity in which it is more efficient and leave the other commodity to other country. The two nations will then have more of both goods by engaging in trade.

Country Specialization

US Making computers and Brazil Growing coffee. The theory of comparative advantage states that international trade is mutually beneficial even when one of the countries can produce every commodity more cheaply than the other country.The terms

„absolute“ and comparative are key terms to understand this principle. eg: A best lawyer is best typist in the town. A secretary is less efficient than lawyer The benefit of international trade results in a more efficient employment of the productive forces of the world. (John Stuart Mill). Foreign trade expands a nation’s consumption possibilities.

Sells Buys Good Foreign trade

Sells	**Buys**	**Good**	**Foreign trade**
Japan	US	Cameras	By specializing, each nation ends up consuming more than it could produce alone.
US	Australia	Computers	
Australia	Japan	Coal	

Two issues are involved in foreign trade:

1. Trade among different nations : Problem of Protectionism : (whether foreigners are discriminated or treated equally)
2. Different nations use different currencies (or monies).

Difference between Foreign trade and domestic trade.

particular	**Domestic trade**	**Foreign trade**
Factors of production	Immobile	Mobile
Currencies	No difficulty	The possibility of variations in exchange rates between different currencies increases risk
Restrictions on trade	Relatively less	Imposed by a. Custom duties b. Fixed quotas c. . Tariff barriers d. Exchange restrictions
Ignorance	Less ignorance	Difference in culture, religion language etc.
Separate markets	India uses right hand drive cars	Ethiopia uses left hand drive cars
Transport and insurance costs	Less	Impede international trade.

Free Trade vs. Protectionism

There are opposing views. International trade has two contrasting views regarding the level of control placed on trade: free trade and protectionism. Free trade is the simpler of the two theories: a laissez-faire approach, with no restrictions on trade. The main idea is that supply and demand factors, operating on a global scale, will ensure efficient production. Therefore, nothing needs to be done to protect or promote trade and growth because market forces will do so automatically. In contrast, protectionism holds that regulation of international trade is important to ensure that markets function properly.