

By Paulding County High School

# International Economics

# Standards

SSEIN<sub>1</sub> Explain why individuals, businesses, and governments trade goods and services.

a. Define and distinguish between absolute advantage and comparative advantage.

b. Explain that most trade takes place because of comparative advantage in the production of a good or service.

c. Define balance of trade, trade surplus, and trade deficit.

**Why do  
Countries,  
Businesses  
and  
Individuals  
Participate in  
International  
Trade?**



# International Economics (SSEIN)

- A good way to think of Unit 4 is “macro-macroeconomics.”
- While microeconomics covers the interaction of a single market and macroeconomics views the larger national picture, international economics views an even larger picture: how the various national economies interact to form a world economy.
- The growth of massive multinational corporations is one sign that the world’s economy is becoming more interconnected each year.

# International Economics (SSEIN)

- As national economies become more interconnected, international economic issues such as trade agreements and trade barriers become more important.
- International trade allows a country to concentrate on what it does best and trade for what it can't or doesn't produce.
- In effect, trade allows a country to specialize in certain goods, which leads to more efficient production.





# Absolute Advantage (SSEIN1a)

- When a country has an **absolute advantage** over another country, it simply means that the country can produce more of a good than another country.
- Absolute advantage refers to an individual, firm, or country using the fewest inputs to produce the same amount of output or the individual, firm, or country producing the largest number of units of output given the same productive resources.

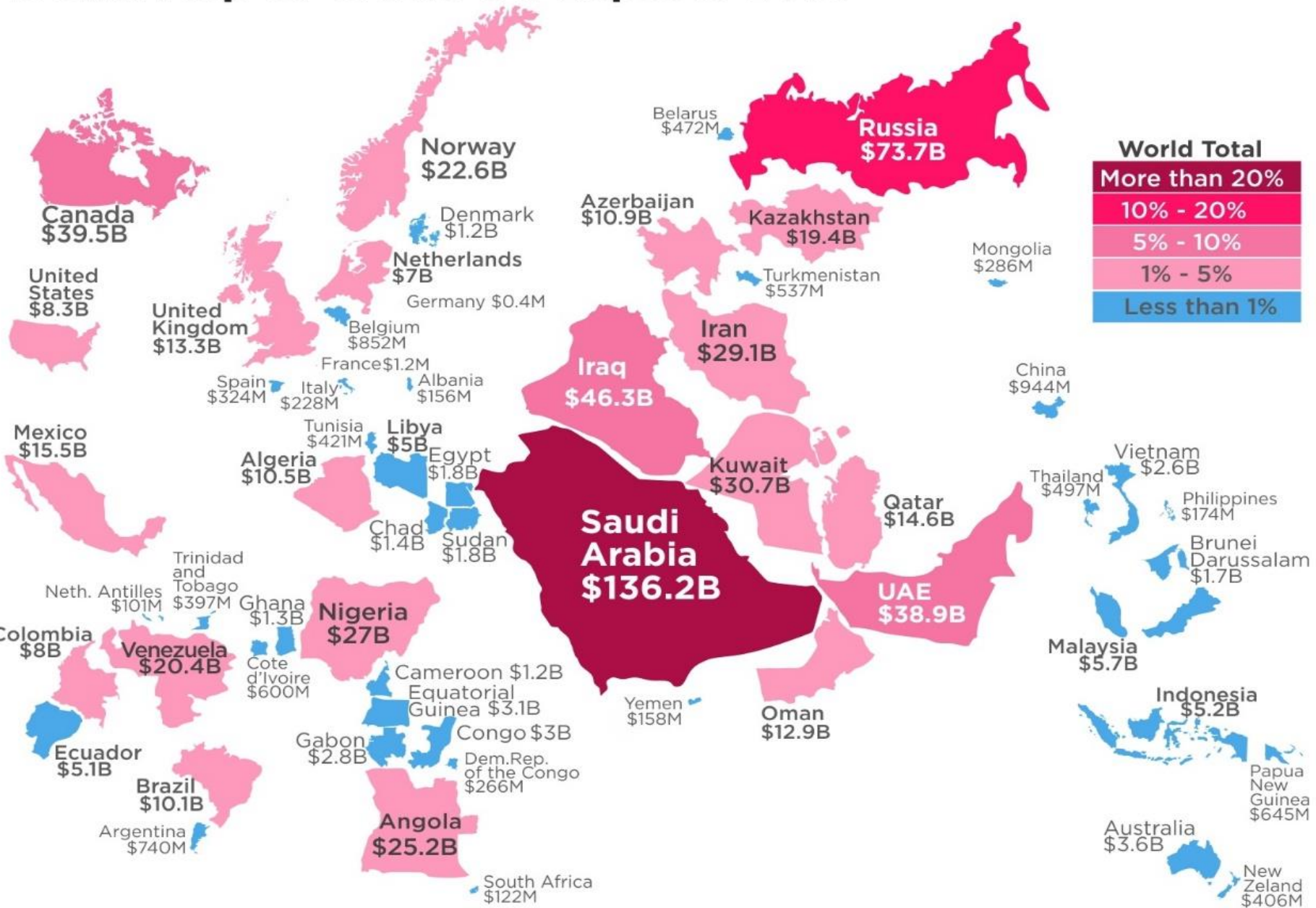
# Absolute Advantage Table

|               | Trains | Planes |
|---------------|--------|--------|
| United States | 4      | 2      |
| Canada        | 5      | 1      |

- Based the table, which country has the absolute advantage in Trains?
- Based on the table, which country has the absolute advantage in Planes?
- What should these countries trade?



# World Map of Crude Oil Exports 2016



Based on the Map, What should the United States Trade with other Saudi Arabia?

**How to read this map:** Countries appear bigger as their crude oil exports are higher. E.g. Saudi Arabia. Conversely, countries with smaller crude oil exports appear smaller. E.g. South Africa. The colour shows the percentage of total of crude oil exports.

**Source and Article:**  
<https://howmuch.net/articles/world-map-of-crude-oil-exports-2016>  
<http://www.worldstopexports.com/worlds-top-oil-exports-country/>

# Comparative Advantage (SSEIN1a)

- While large countries will probably have an absolute advantage in production over smaller countries, when any two countries are producing two goods (like cars and sugar), one country will always have a comparative advantage over the other in the production of one of the two goods.
- **Comparative advantage** in production of a good or service exists when one individual, firm, or country has the lowest opportunity cost for producing the good or service.

# Comparative Advantage (SSEIN1a)

|               | Trains | Planes |
|---------------|--------|--------|
| United States | 4      | 2      |
| Canada        | 5      | 1      |

- Based on the table, what country has the comparative advantage in Trains?
- Based on the table, what country has the comparative advantage in Planes?
- HINT: OVER GOES UNDER

# Comparative Advantage (SSEIN1a)

|               | Trains      | Planes    |
|---------------|-------------|-----------|
| United States | 4 (1T=.5 P) | 2 (1P=2T) |
| Canada        | 5 (1T=.2T)  | 1 (1P=5T) |

- What country has the lower opportunity cost of Trains? Canada
- What country has the lower opportunity cost of Plains? United States
- HINT: OVER GOES UNDER

# World Map of U.S. Trade Balance

Trade in Goods (in billions of dollars)



# What is the purpose of the following Map?

**How to read this graph:**  
Countries in red colour show where U.S. has a trade deficit.  
Countries in green colour show where U.S. has a trade surplus.  
The size of the countries represent a higher or lower trade deficit/surplus.  
e.g. U.S. has the highest trade deficit with China and the highest trade surplus with Hong Kong.

# Balance of Trade (SSEIN<sub>1c</sub>)

- A **balance of trade** records the value of all goods and services exported from a country minus the value of all goods and services imported from outside the country.
- This is often referred to as the “**trade surplus**” (if exports exceed imports) or the “**trade deficit**” (if imports exceed exports). (SSEIN<sub>1c</sub>)



# Review Questions

- Define absolute advantage (BL)
- Define comparative advantage (BL)
- What is the difference between absolute and comparative advantage (PL)
- Why does most trade take place between countries? (DL)
- Define balance of trade (BL)
- Define trade surplus (BL)
- Define trade deficit (BL)

# Standards

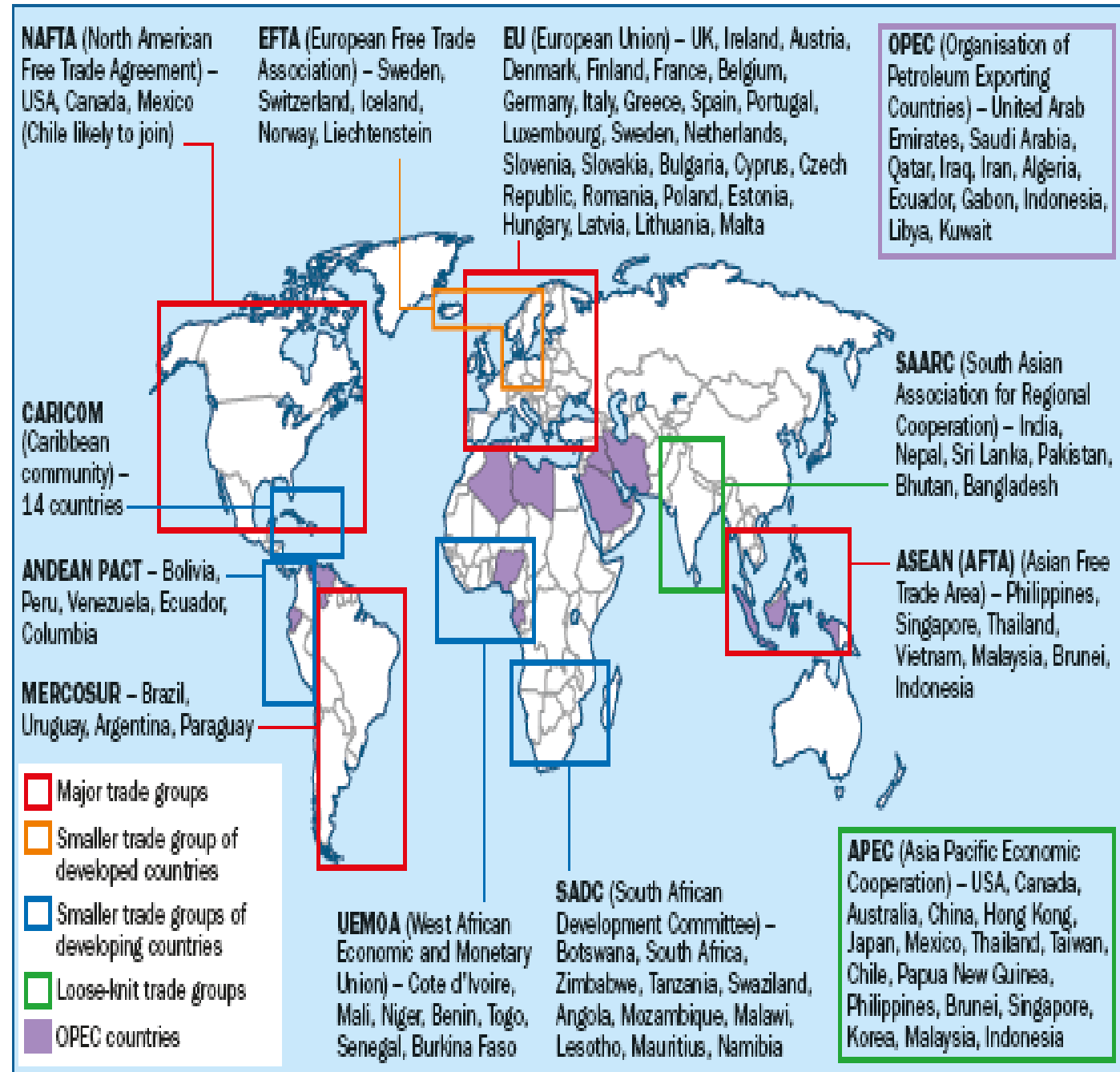
SSEIN2 Explain why countries sometimes erect trade barriers and sometimes advocate free trade.

- a. Define trade barriers such as tariffs, quotas, embargoes, standards, and subsidies.
- b. Identify costs and benefits of trade barriers to consumers and producers over time.
- c. Describe the purpose of trading blocs such as the EU, NAFTA, and ASEAN.
- d. Evaluate arguments for and against free trade.



# Trading Blocs (SSEIN2c)

- Trading blocs are formed in order to reduce barriers to trade.
- In theory, this will lead to lower prices for buyers (citizens) within the trading nations as well as for firms that are more competitive on the international market (because of increased competition).



Trade groupings

# North American Free Trade Agreement, NAFTA (SSEIN2c)

- The North American Free Trade Agreement, NAFTA, is one such trading bloc; its goal is to eliminate barriers to trade—most notably tariffs—between Canada, Mexico, and the United States.



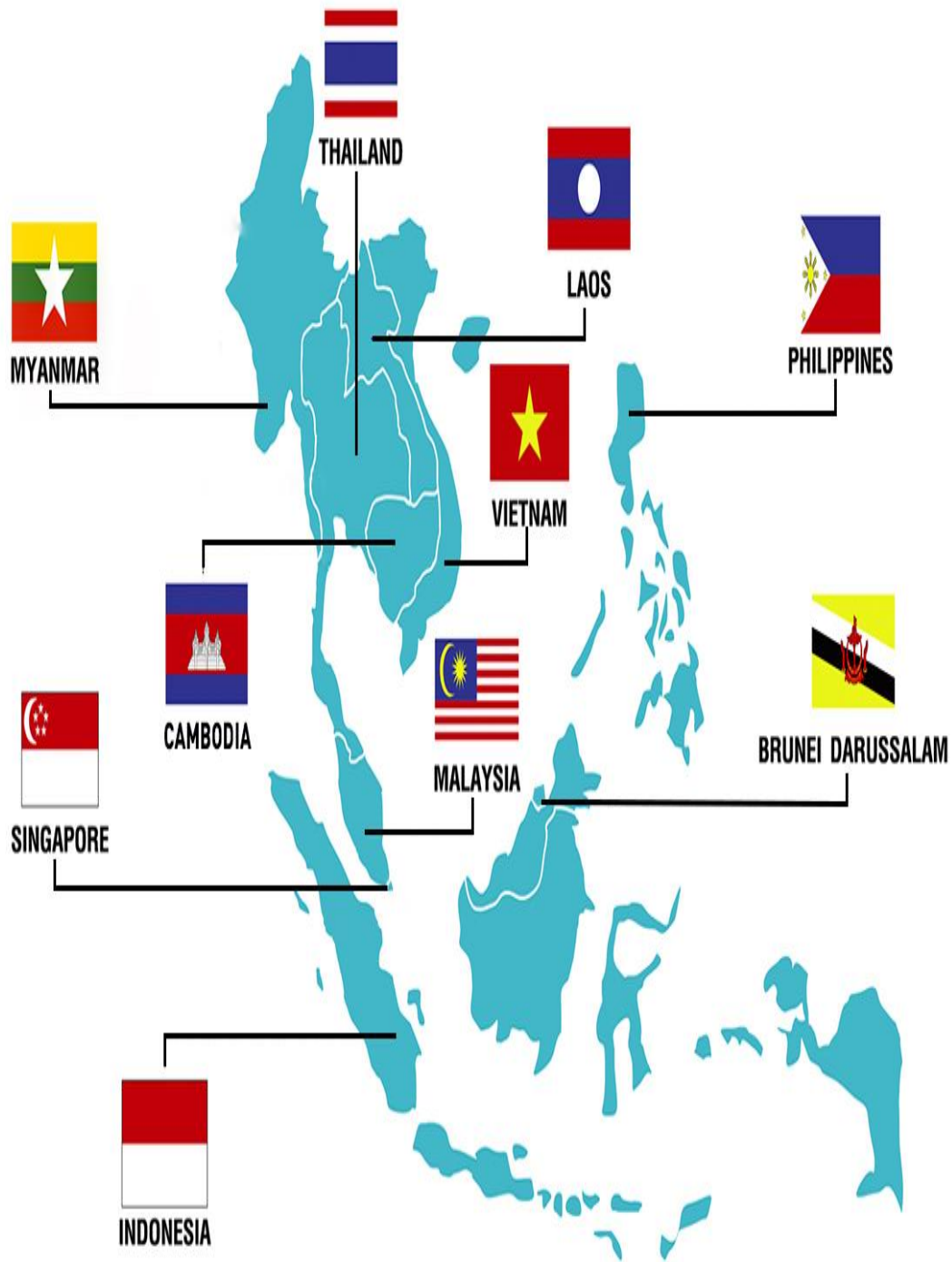
European Union countries' currency status

- Euro area
- Currency pegged to euro
- Floating currency



# European Union, EU (SSEIN1c)

- The European Union (EU) allows for free movement of goods and workers across country borders.



# Association of Southeast Asian Nations, ASEAN (SSEIN2c)

- ASEAN is the Association of Southeast Asian Nations. It was established to promote economic growth, free trade, and economic collaboration between member nations.

# NAFTA Drives U.S. Trade

**27%** | **33%**

U.S. total imports  
come from Mexico  
and Canada

U.S. total exports go  
to Mexico and  
Canada

Top 5 U.S. imports from  
Canada and Mexico

Oil & gas  
Motor vehicles  
Motor vehicle parts  
Petroleum & coal products  
Nonferrous metals

Top 5 U.S. exports to  
Canada and Mexico

Motor vehicles parts  
Petroleum & coal products  
Motor vehicles  
Computer equipment  
Basic chemicals

## What are the Benefits of Free Trade?

# Arguments in Favor of Free Trade (SSEIN2d)

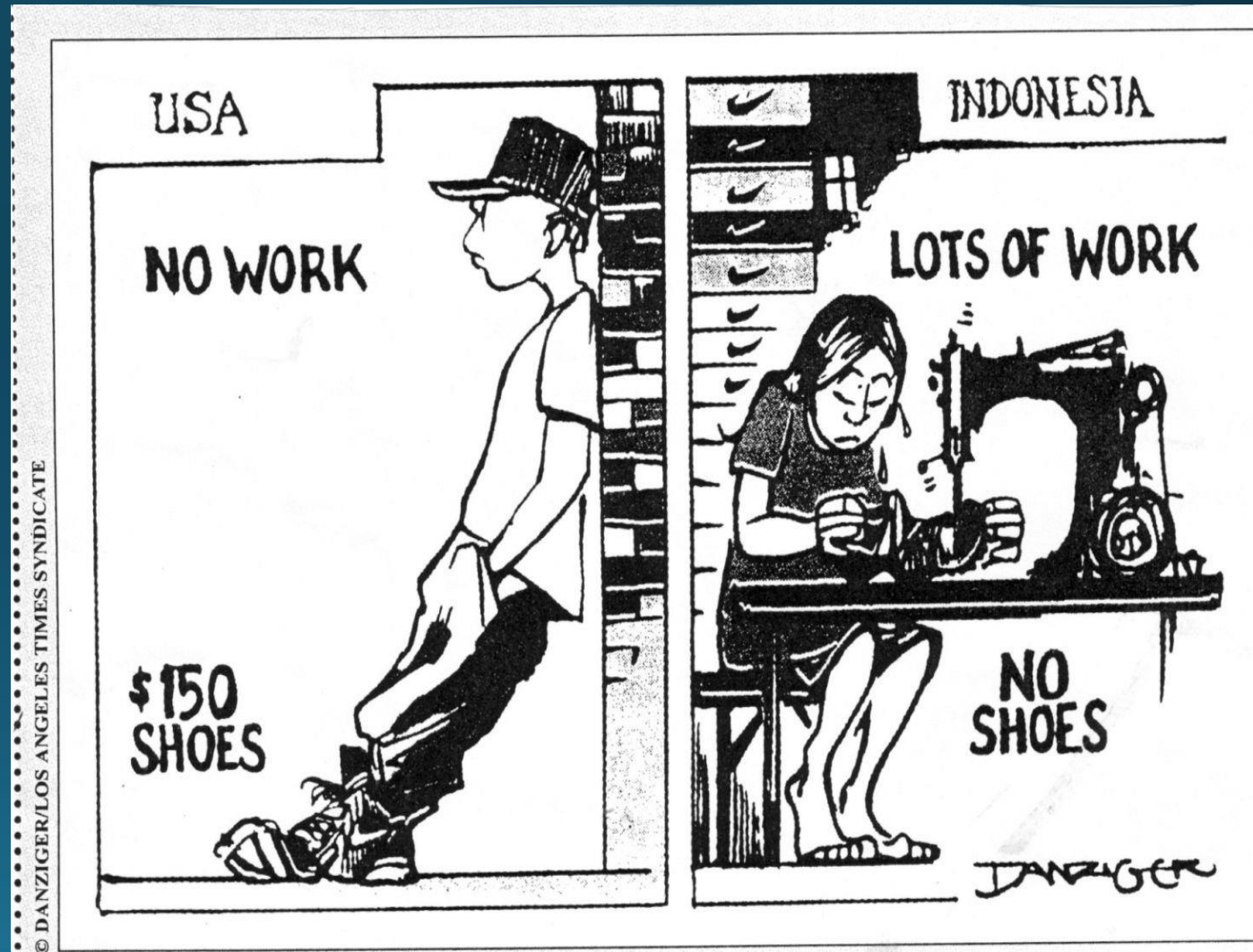
- Free trade increases competition, which reduces costs for buyers and improves quality of goods.
- Free trade allows for domestic goods to be sold all over the world and protects export industries.
- Free trade allows the country to exercise comparative advantage through specialization.

# What are the costs of Free Trade?

**Table 1. Average Hourly Apparel Worker Wages**

|                    | Hourly Wage in U.S. \$ |
|--------------------|------------------------|
| Bangladesh         | \$0.13                 |
| China              | 0.44                   |
| Costa Rica         | 2.38                   |
| Dominican Republic | 1.62                   |
| El Salvador        | 1.38                   |
| Haiti              | 0.49                   |
| Honduras           | 1.31                   |
| Indonesia          | 0.34                   |
| Nicaragua          | 0.76                   |
| Vietnam            | 0.26                   |

Source: *Globalization and the Poor*, Table 7.2, p.108.



# Arguments against Free Trade, or Promoting Restricted Trade (SSEIN2d)

- Infant industries (new industries in the early stage of development) are protected by trade barriers.
- This allows infant industries to grow.
- Free trade hurts domestic workers.
- Companies may move overseas to utilize cheaper labor and increase profits.



# Review Questions

- What are the five barriers to trade? (BL)
- Define tariff (BL)
- Define quota (BL)
- Define standards (BL)
- Define embargo (BL)
- Define subsidy (BL)

# Review Questions

- Define trading blocs (BL)
- What are three examples of trading blocs? (DL)
- What is the purpose of trading blocs? (PL)
- What countries are a part of the European Union? (DL)
- What countries are a part of NAFTA? (DL)
- What countries are a part of ASEAN? (DL)
- List two costs of free trade (DL)
- List two benefits of free trade (DL)

# Standards

SSEIN<sub>3</sub> Explain how changes in exchange rates can have an impact on the purchasing power of groups in the United States and in other countries.

- a. Define exchange rate as the price of one nation's currency in terms of another nation's currency.
- b. Interpret changes in exchange rates, in regards to appreciation and depreciation of currency.
- c. Explain why some groups benefit and others lose when exchange rates change

# Arguments against Free Trade, or Promoting Restricted Trade (SSEIN2d)

- Labor standards are not the same in all countries. Some countries may treat their workers poorly.
- Some industries are critical to the country's national security.
- These industries should be protected even if they cannot compete internationally. (SSEIN2d)

# Barriers to Trade (SSEIN2a)

- **Tariff:** A tariff is a tax on an imported good.
- **Quota:** A quota is similar to a tariff, but instead of taxing the import, a quota limits the amount of a good that is allowed into the country.
- **Embargo:** An embargo on a particular good is like a quota set at zero; a government completely prohibits the import of that item.





# Barriers to Trade (SSEIN2a)

- **Standards:** Governments employ standards to ensure the safety of imported goods and to make sure that these goods comply with local laws. For example, the use of lead in paint is prohibited in the United States.
- **Subsidy:** With a subsidy, the government makes payments to a local supplier to reduce the production costs of the supplier.

# Exchange Rates (SSEIN3a)

- Tariffs, quotas, and other trade agreements are international trade issues that entire countries must address.
- For individuals, the exchange rate is one of the most important international trade issues.
- The **exchange rate** measures the price of one nation's currency in terms of another nation's currency.



# Did the Japanese Yen Appreciate or Depreciate from Year 1 to Year 2?

**U.S. Dollar, end of Year 1**

|                      | <b>One U.S. dollar</b> | <b>in U.S. dollars</b> |
|----------------------|------------------------|------------------------|
| <b>British pound</b> | 0.49                   | 2.06                   |
| <b>Danish krone</b>  | 5.17                   | 0.19                   |
| <b>Euro</b>          | 0.69                   | 1.44                   |
| <b>Japanese yen</b>  | 114.69                 | 0.0087                 |
| <b>Mexican peso</b>  | 10.71                  | 0.093                  |
| <b>Swiss franc</b>   | 1.17                   | 0.86                   |
| <b>Thai baht</b>     | 31.7                   | 0.03                   |

**U.S. Dollar, end of Year 2**

|                      | <b>One U.S. dollar</b> | <b>in U.S. dollars</b> |
|----------------------|------------------------|------------------------|
| <b>British pound</b> | 0.52                   | 1.92                   |
| <b>Danish krone</b>  | 4.83                   | 0.21                   |
| <b>Euro</b>          | 0.67                   | 1.49                   |
| <b>Japanese yen</b>  | 121.3                  | 0.0082                 |
| <b>Mexican peso</b>  | 15.02                  | 0.067                  |
| <b>Swiss franc</b>   | 1.06                   | 0.94                   |
| <b>Thai baht</b>     | 36.8                   | 0.027                  |



# Did the Danish Krone Appreciate or Depreciate from Year 1 to Year 2?

**U.S. Dollar, end of Year 1**

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# Appreciation vs Depreciation (SSEIN<sub>3</sub>b, c)

- Exchange rates move up and down to reflect the value of one country's currency in comparison to another.
- If there is a great demand for U.S. products, people need more U.S. dollars to purchase these goods.
- This drives the demand for U.S. dollars up, causing the dollar to **appreciate**, or strengthen.
- At the same time, the peso has **depreciated**, or weakened, relative to the dollar.

# Depreciation

| Winners                                 | Losers   |
|---|--|
| Exporters                               | Consumers who buy imports                                  |
| Domestic tourist industry               | Residents who holiday abroad                               |
| Workers gaining jobs in export industry | Firms who buy imported raw material                        |
| Economic growth might increase          | Those on fixed incomes/wages who see inflation rise faster |
| Current trade deficit should improve    | Foreign exporters/tourist industry                         |

# Review Questions

- Why does currency exchange happen? (DL)
- What is the difference between appreciation and depreciation of currency? (PL)
- Why do some groups benefit or lose when currency appreciates or depreciates? (DI)