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Pearson

International Economics Analysis

Chapter 1

An Introduction to the World Economy

Learning Objectives (1 of 2)

1.1 Discuss historical measures of international with data on trade, capital flows and migration.

1.2 Compute the trade-to-GDP ratio and explain its significance.

Learning Objectives (2 of 2)

1.3 Describe three factors in the world economy today that are different from the economy at the end of the first wave of globalization.

1.4 List the three types of evidence that trade supports economic growth.

Elements of International Economic Integration (1 of 4)

- Globalization has many components, including culture, language, economics, politics and more.
- Globalization in the economic sphere is also called international economic integration.
- International economic integration has occurred rapidly since approximately 1950, but especially since the early 1970s.

Elements of International Economic Integration (2 of 4)

- The current wave of international economic integration is not the first.
- A major wave of globalization occurred between approximately 1870 and 1913.
- This earlier wave was destroyed by World War I and II and the worldwide Great Depression of the 1930s.

Elements of International Economic Integration (3 of 4)

- Economists measure international integration by looking at
  - World trade
  - International capital flows
  - International migration
  - Convergence of prices in different markets

Elements of International Economic Integration (4 of 4)

- Economists measure international integration by looking at
  - World trade
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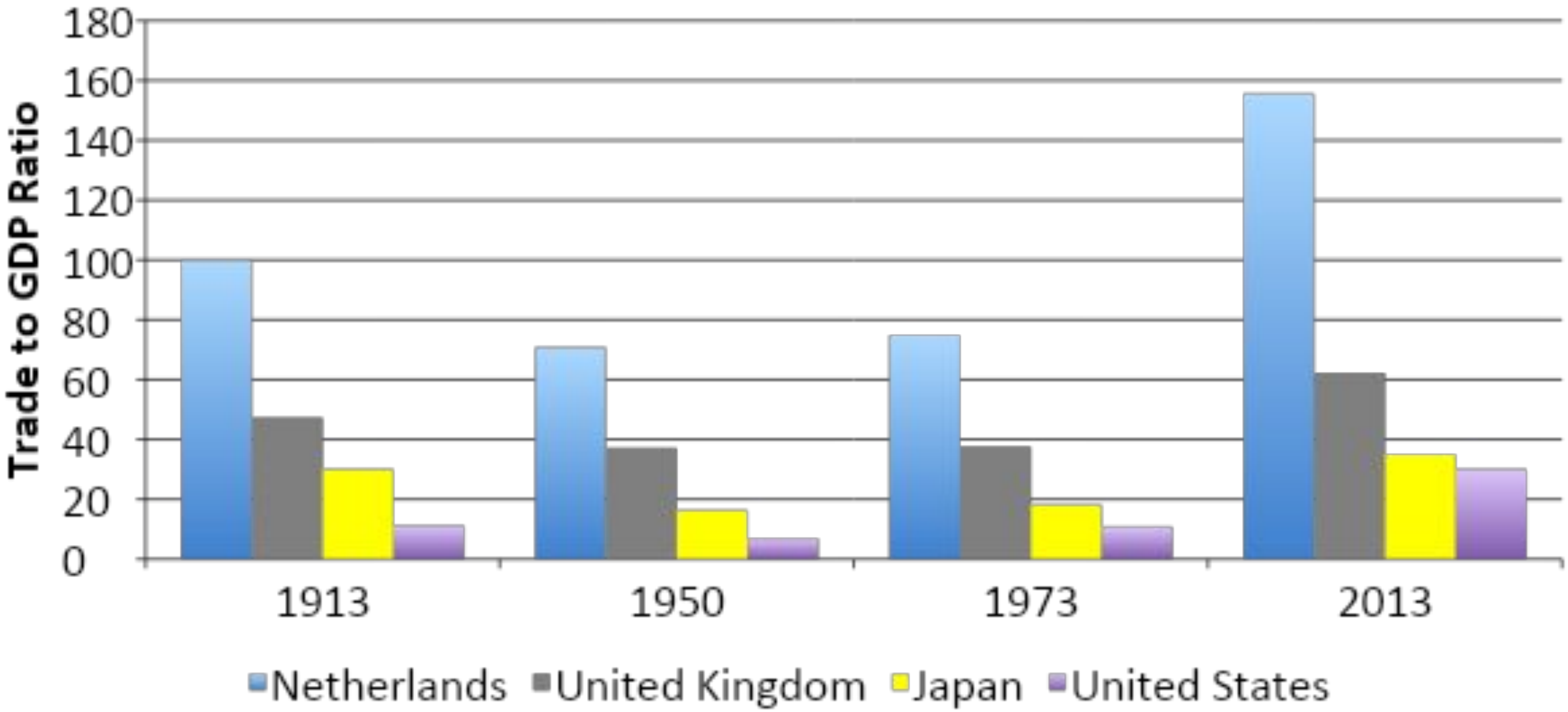
The Growth of World Trade (1 of 2)

- Since the end of World War II in 1945, world trade has grown much faster than world production.
- In 1950, world trade equaled about 5.5 percent of world **gross domestic product (GDP)**.
- In 2013, world trade was about 30 percent of world GDP.

The Growth of World Trade (2 of 2)

- Economists measure the importance of world trade with the trade-to-GDP ratio.
- Trade-to-GDP ratio is exports plus imports divided by GDP:
- **Trade-to-GDP ratio = (exports + imports) ÷ GDP**
- The ratio does not tell us much about a country’s trade policies or openness to trade.

Figure 1.1 Trade-to-GDP Ratios for Four Countries, 1913-2013



The trade-to-GDP ratio fell between 1913 and 1950, but has risen since then. Each country shows the same pattern over time.

Mcq 1.1

- The trade – to - GDP ratio is calculated by:

A. exports divided by GDP.
B. imports divided by GDP.
C. exports plus imports divided by GDP.
D. exports minus imports divided by GDP.

MCQ1.2

- Over the last fifty years, trade has grown

A) slower than GDP and slower than during the first 50 years of the twentieth century.

B) faster than GDP and faster than during the first 50 years of the twentieth century.

C) slower than GDP.

D) None of the above.

MCQ1.3

- In 2012, Frontland had $800 million in imports, GDP of $2000 million and 1000 million in exports. According to openness indicator, Frontland is

A) a wealthier nation.
B) a poorer nation.
C) a larger nation.
D) a smaller nation.

International Migration of Labor (1 of 2)

- Capital and labor movements across international boundaries are part of international economic integration.
- International migration was larger, relative to population, before World War I than it is today.
- Before World War I, most countries did not require passports and visas, and there were few border controls.

International Migration of Labor (2 of 2)

- In 1900, about 14.5 percent of the U.S. population was immigrants.
- Today, it is around 13 percent.
- Migration has increased since the 1960s, but immigrants as a percentage of the total population is less than it was in 1900.

International Capital Flows (1 of 3)

- There are many types of capital flows:
  - Financial flows representing paper assets such as stocks and bonds.
  - Capital flows that are used to purchase real assets such as real estate, or to set up businesses and factories.
  - The purchase of real assets is known as **foreign direct investment (FDI).**
- Technological improvements facilitate increased capital flows.

International Capital Flows (2 of 3)

- Capital flows today:
  - Are much larger than during the earlier wave of globalization;
  - Include many more types of financial instruments;
  - Are frequently devoted to protecting against currency fluctuations;
  - Have lower **transaction costs** than in previous eras.

International Capital Flows (3 of 3)

- Capital flows are savings of one country that are invested in another.
- High savings countries tend to have high investment, and low savings implies low investment.
  - Capital flows are not completely integrated.
  - Countries cannot completely depend on others for their investment funds.

Three Features of Contemporary International Economic Relations (1 of 6)

- More deep integration, moving beyond shallow integration.
- The presence of multilateral organizations such as the World Trade Organization (WTO)
- The growth of regional trade agreements, such as the European Union or the North American Free Trade Agreement.

Three Features of Contemporary International Economic Relations (2 of 6)

- **Shallow integration** consists of the removal of **tariffs** (taxes on imports) and **quotas** (physical limits on import quantities).
- As tariffs and quotas come down, other policies begin to limit trade.
  - Environmental policies
  - Labor policies
  - Safety standards, etc.
- **Deep integration** occurs when countries try to reform domestic policies that limit trade.
- Deep integration is much more controversial.

Three Features of Contemporary International Economic Relations (3 of 6)

- Multilateral organizations are open to all countries.
- They are new since World War II. Prominent examples include:
  - International Monetary Fund;
  - World Bank;
  - World Trade Organization.

Three Features of Contemporary International Economic Relations (4 of 6)

- Multilateral organizations reduce uncertainty in international economic relations. They
  - Mediate disputes;
  - Are forums for setting rules;
  - Propose solutions to problems;
  - Provide technical and financial assistance.
- Multilateral organizations are controversial; we look at them more closely in the next chapter.

Three Features of Contemporary International Economic Relations (5 of 6)

- **Regional trade agreements (RTAs)** are composed of countries that give special market access to each other.
- Examples include the North American Free Trade Agreement (NAFTA) and the European Union (EU), among many others.
- RTAs have dramatically grown in number since the 1980s.

Three Features of Contemporary International Economic Relations (6 of 6)

- **Regional trade agreements (RTAs)** are not new.
- RTAs are controversial among economists.
  - Some economists think they hurt world trade by focusing a country’s attention on just a few trade partners.
  - Others believe they help world trade by loosening some barriers and trying out new agreements.

Trade and Economic Growth

- Economists favor more open trade because it enables countries to grow faster and its people live better.
- Evidence comes in three forms:
  - Historical examples of countries.
  - Statistical comparisons of countries.
  - Economic models and deductive reasoning.
- As we will see, trade benefits a nation but not necessarily every individual in the nation.