

International Economics

Seventh Edition, Global Edition

Chapter 2

International Economics Institutions Since World War II

Learning Objectives (1 of 2)

2.1 Classify with examples the main types of international economic organizations.

2.2 Identify economic circumstances in which the IMF, the World Bank, and the WTO are active.

2.3 Compare the different levels of integration found in regional trade agreements with examples.

Learning Objectives (2 of 2)

2.4 Analyze the roles of international economic organizations.

2.5 Debate the pros and cons of international organizations.

International Institutions since World War II

- Economists define **institutions** as the rules that govern and constrain behavior.
- Institutions define what is permitted and what is prohibited.
- Institutions can be formal or informal.
 - Formal institutions are written, often embodied in laws, codes, constitutions.
 - Informal are customs or tradition such as manners and etiquette.
- Formal institutions are often embodied in an organization.

Table 2.1: Categories of International Institutions, with Examples

Type	Examples
Commodity- or industry-specific organizations: These range from trade associations, to international standards-setting bodies, to powerful cartels	<ul style="list-style-type: none"> ■ Oil Producing and Exporting Countries (OPEC) ■ International Telecommunications Union (ITU)
Commissions and agencies for managing shared resources	<ul style="list-style-type: none"> ■ International Boundary and Water Commission (IBWC) ■ Mekong River Commission
Development funds and banks	<ul style="list-style-type: none"> ■ Asian Development Bank ■ Islamic Development Bank
International trade agreements involving a few nations (regional trade alliances or trade blocs)	<ul style="list-style-type: none"> ■ North American Free Trade Agreement (NAFTA) ■ European Union
Global organizations for trade, development, and macroeconomic stability	<ul style="list-style-type: none"> ■ International Monetary Fund (IMF) ■ World Bank ■ World Trade Organization (WTO)

MCQ 2.1

- Informal institutions are
 - A) the same thing as organizations.
 - B) a written set of rules governing behavior.
 - C) associations of individuals or groups.
 - D) embodied in traditions and customs.

The IMF, the World Bank, and the WTO

- Three international organizations play major roles in international economic relations:
 - The International Monetary Fund (IMF)
 - The World Bank
 - The World Trade Organization (WTO)

The Bretton Woods Conference

- The **Bretton Woods Conference**, held in 1944 at Bretton Woods, New Hampshire, was a gathering of leaders from the Allied Powers.
 - The goal was to create a more stable and prosperous world economy.
 - They wished to avoid the problems of the 1930s by creating institutions and organizations that would define rules for trade and international payments.

The IMF (1 of 2)

- The IMF was created at Bretton Woods in 1944.
- It began operation in 1945 with 29 members; today it has 188.
- It is funded by a **quota** each member pays; the quota is proportional to the size of their economy and determines how many votes it has.
- The primary purpose of the IMF is to assist in the creation of a stable, crisis free, system of international payments between countries.
- Its main activities are to provide technical and financial assistance to countries that have debt problems or an unstable currency.

The IMF (2 of 2)

- The IMF is an international **lender of last resort**.
 - It provides loans to countries that cannot make payments on their debts and that cannot borrow elsewhere.
 - The loans are limited in size and come with a set of requirements, called **IMF conditionality**.
- The IMF monitors exchange rates and assists countries when their currencies collapse in value.
- An increasingly important role is to provide standards and technical assistance for the international reporting of economic and financial data.

The World Bank

- Also created at Bretton Woods with a membership and structure similar to the IMF.
- Countries buy shares and the number of shares determines their voting rights.
- Originally intended as a mechanism to rebuild Europe after World War II
- Its main function today is to provide capital and technical assistance for economic development.

The GATT (1 of 4)

- The **General Agreement on Tariffs and Trade (GATT)** was envisioned at Bretton Woods but did not start until 1950.
- Its main purpose is to provide a forum for discussing trade rules and a mechanism for gradually opening markets to more international trade.
- The GATT works through **trade rounds**.
 - Trade rounds are formal discussions about new rules for reducing trade barriers.

The GATT (2 of 4)

- Initially the GATT focused on proportional tariff reductions and elimination of quotas.
 - It did not promote free trade, it promoted “freer” trade.
 - Proportional tariff reductions require each country to reduce tariffs by the same percentage but tariffs remain different.
- By the 1970s, new issues arose that required discussion and negotiations:
 - Subsidies for industry that gave advantages;
 - Problems of selling goods at artificially low prices;
 - Barriers to trade in new areas, such as services

The GATT (3 of 4)

- The **Uruguay Round** was a new set of rules that began in 1995.
 - It created the **World Trade Organization** to serve as the umbrella organization for all agreements.
 - It extended trade agreements into services, agriculture, patent protections, international investment rules, and others.
- In 2001, the **Doha Round** opened discussion.
 - Its primary focus was meant to be on the issues of concern to developing countries.
 - It proposed a **Doha Development Agenda**
 - It is the first round of talks to fail; a major reason is the inability of advanced economies to lower their trade barriers in agriculture.

The GATT (4 of 4)

- The GATT remains in effect and is the primary agreement overseen by the WTO.
- The two guiding principles of the GATT are **national treatment** and **nondiscrimination**.
 - National treatment means that foreign goods must be treated the same as national goods.
 - Nondiscrimination prohibits different tariffs or rules for different countries. This is the principle of **most favored nation status**.
- All WTO members must adhere to these rules when trading with other WTO members.

Table 2.2 The GATT Rounds

Round	Year	Number of Participants
Geneva I	1947	23
Annecy	1949	13
Torquay	1951	38
Geneva II	1956	26
Dillon	1960–1961	26
Kennedy	1964–1967	62
Tokyo	1973–1979	102
Uruguay	1986–1993	105
Doha (WTO)	2001–	162

MCQ 2.2

- The international organization that serves as a forum for trade discussions and the development of trade rules is called

- A) the World Bank.
- B) the WTO.
- C) the IMF.
- D) the APEC.

MCQ。 2.3

One of the most important and most visible roles of the IMF is to

- A) hold regular negotiations over tariff reductions.
- B) intercede by invitation when countries cannot pay their international debts.
- C) investigate countries that are charged with being unfair traders.
- D) provide capital to countries that need capital to develop their economies.

MCQ。 2.4

From the late 1940s until 1995, the organization that was primarily responsible for conducting rounds of trade negotiations was the

- A) World Bank.
- B) IMF.
- C) GATT.
- D) WTO.

2.5

- Original mission of the World Bank was to
- - A) provide capital to firms around the world.
 - B provide capital to underdeveloped countries.
 - C) provide financial assistance for the reconstruction of war-damaged nations.
- D) provide a safe place for people around the world to put their money.

MCQ。 2.6

- IMF conditionality refers to the
- - A) technical assistance the IMF gives.
 - B) minimum size of a national debt problem that a country must have before the IMF gets
- involved.
- C) changes in policies a country must make in order to receive IMF financial assistance.
- D) minimum-sized loan the IMF will make.

MCQ。 2.7

- When the Germany gives most favored nation status to France, it means that
- A) France is treated better than Germany's other trading partners.
- B) France is treated worse than Germany's other trading partners.
- C) France is treated the same as Germany's other trading partners.
- D) France is better than all other nations in the WTO.

Regional Trade Agreements (1 of 5)

- **Regional trade agreements (RTA)** can be:
 - Bilateral (two members);
 - Plurilateral (several members);
 - Multilateral (open to everyone that wants to join).
- There are five levels of RTA:
 - **Partial agreement**
 - **Free trade area**
 - **Customs union**
 - **Common market**
 - **Economic union**

Regional Trade Agreements (2 of 5)

- Each level increases in complexity and includes the prior levels.
- Partial agreement: Free trade in one or a few products.
- Free trade area: Free trade in all goods and services (outputs).
- Customs union: An FTA plus a **common external tariff**.
- Common market: A customs union plus free movement of labor and capital (inputs).
- Economic union: A common market plus substantial harmonization of economic policies.

Regional Trade Agreements (3 of 5)

- Examples of prominent RTA:
 - North American Free Trade Agreement (NAFTA);
 - Common Market of the South (Mercosur);
 - ASEAN Free Trade Area (AFTA);
 - Economic Community of West African States (ECOWAS);
 - Gulf Cooperation Council (GCC);
 - The European Union (EU).

MCQ. 2.8

- European Union is an example of an RTA that is being progressed into
- A) a Free Trade Area.
- B) a customs union.
- C) an economic union.
- D) a common market.

MCQ. 2.9

- A free trade agreement plus a common set of tariffs toward non-members plus free movement of factors of production is called
- - A) a common market.
 - B) a free trade area.
- C) a customs union.
- D) an economic union.

Regional Trade Agreements (4 of 5)

- RTA have grown in number. In 2012, 338 were active, most of them created since 1990.
- Most agreements have exceptions: free trade agreements do not usually have 100% free trade.
- RTA violate the nondiscrimination rule of the GATT and WTO; countries treat member countries better than others.
 - The WTO allows this as long as **trade creation** is greater than **trade diversion**.
 - Trade creation: New trade created by the agreement;
 - Trade diversion: Trade that is diverted from a non-member to a member.

Regional Trade Agreements (5 of 5)

- Proponents of RTA claim the following:
 - They help world trade by reducing some barriers;
 - They allow countries to try new agreements that can potentially be used later in WTO negotiations;
 - They encourage WTO agreement by offering an alternative in case the WTO is stalled.
- Opponents argue:
 - They divert attention from multilateral negotiations and undermine the WTO;
 - They rarely, if ever, lead to a WTO agreement;
 - They often discriminate against poorer nations.

Why Have International Institutions?

- International institutions provide **public goods**.
 - Public goods are **nonexcludable**: Everyone benefits even if they do not pay.
 - Public goods are **nonrival (nondiminishable)**: They are not diminished by consuming them.
 - Public goods have a **free rider problem**.
- The two most important characteristics of public goods provided by international institutions are:
 - Increased international economic order;
 - Increased certainty about the behavior of other nations.

Four Public Goods Provided by International Institutions

- Open markets in recessions (GATT/WTO);
- Capital flows to less-developed countries (World Bank);
- International money for paying international debts (IMF);
- Last resort lending (IMF).

Criticisms of International Institutions

(1 of 2)

- **Sovereignty** and transparency.
 - Countries receiving assistance, particularly from the IMF, are sometimes required to give up the ability to set their own policies.
 - Decision making in the institutions is not transparent; because the U.S. and Europe have the largest voting bloc, decisions are sometimes viewed as having been directed by rich countries.

Criticisms of International Institutions

(2 of 2)

- Ideology.
 - Critics argue that the advice, technical assistance, and negotiating positions are often a reflection of the biases and ideologies of high income countries and do not adequately consider alternative policies.
- Implementation and adjustment costs.
 - There are asymmetries in the fiscal burdens associated with implementing agreements and adjusting to the changes they create; richer countries do better at this than poorer ones.