Trade as a Engine of Economic growth

- Trade, undoubtedly, has several benefits.
- It promotes growth and enhances economic welfare by stimulating more efficient utilisation of factor endowments of different regions and by enabling people to obtain goods from efficient sources of supply.
- Trade also makes available to people goods which cannot be produced in their country due to various reasons.
- The role of trade in enhancing consumer’s choice (even delight) is tremendous.

Benefits of trade in case of less developed countries

- 1. Trade provides material means (capital goods, machinery, and raw and semi-finished material) indispensable for economic development.
- 2. Trade is the means and vehicle for the dissemination of technological knowledge, the transmission of ideas, for the importation of know-how, skills, managerial talents and entrepreneurship.
- 3. Trade is also the vehicle for the international movement of capital, especially from the developed to the underdeveloped countries.
- 4. Free international trade is the best anti-monopoly policy and the best guarantee for the maintenance of a healthy-degree of free competition.

Gains from International Trade

The gains from international trade under two heads.

They are

(a) Static gains

(b) Dynamic gains

Static gains from Trade

- Static gains arise out of optimum utilisation of a country's factor resources. Theutilisation of resources to the optimum level contributes to increasing national outputand social welfare.Static gains comprise of the following gains:
- **(i) Specialisation and Division of Labour**
- International trade leads to specialization and geographical division of labour.Each country specializes itself in the production of that commodity for theproduction of which it enjoys a comparative cost advantage.International tradebrings about all the advantages of specialization and division of labour at theinternational level.
- **(ii) Maximisation of Production**
- As a result of specialization and division of labour each country seeks topro duce to the maximum extent possible.Thus, trade among countries leadsto the maximization of world's output.

(iii) Maximisation of Welfare

- By maximizing production,inter national trade makes available a large quantity of goods f or consumption, Thiswill have a positive impact on the economic welfare of the people world over.
- **(iv) Rise in National Income**
- International trade leads to a rise in national income because of the increasein employment and production.There will be a rise in per-capita income also.
- **(v) Use of Surplus Resources**
- International Trade provides opportunities to a country to exploit its surplusresources.This is due to the widening of the market made possible b yinternational trade

Dynamic Gains

- Dynamic Gains of international trade are those gains that contribute significantly to the promotion of economic growth of the trading countries concerned. The following are the dynamic gains of international trade:
- **(i) Widening of the Market**
- An important gain of international trade is that it enlarges the size of the market for the products of trading countries.
- This is of much importance to those countries which have surplus output to dispose off .
- Widening of the market contributes significantly to an increase in specialization encouraging innovations and inventions.
- As a result, there will be an increase in productivity and profit, contributing in the process, to an increase in economic growth.
- **(ii) Educative Benefit**
- The educative gain of international trade lies in its transfer of skills from one country to another. These skills include technical know-how, managerial skills, enterprise, ideas etc. The less developed countries will be immensely benefited as the recipients of these skills.

- **(iii) Efficient Utilization of Resources**
- International trade, based on comparative cost advantage, brings about efficient utilization of the resources of the trading countries concerned. Resources will be put to the optimum use.
- **(iv) Capital Accumulation**
- The need to buy foreign goods and thereby increase consumption and the standard of living motivates people to save more. This will Contribute to increasing capital accumulation.
- **(v) Capital Movements**
- A significant gain from international trade lies in that it leads to capital movements from one country to another .This is of much advantage to the less developed countries.
- **(vi)Advantages to Less Developed Countries**
- Trade brings enormous gains to the less developed countries. These countries can import capital, technical know-how, managerial skills etc. All this helps to accelerate the pace of economic growth of these countries. Thus, the gains from international trade are many and varied

Prebisch-Singer Thesis

- There is empirical evidence related to the fact that the terms of trade have been continuously moving against the developing countries.
- On the basis of exports statistics concerning the United Kingdom between 1870 and 1940, Raul Prebisch demonstrated that the terms of trade had secular tendency to move against the primary products and in favor of the manufactured and capital goods.
- This viewpoint has been strongly supported by H. W. Singer.
- The essence of Prebisch-Singer thesis is that the peripheral or LDC's had to export large amounts of their primary products in order to import manufactured goods from the industrially advanced countries.

- Prebisch and Singer maintain that there has been technical progress in the advanced countries, the fruit of which have not percolated to the LDC’s.
- In addition, the industrialised countries have maintained a monopoly control over the production of industrial goods.
- They could manipulate the prices of manufactured goods in their favour and against the interest of the LDC’s.
- Except the success of OPEC in raising the prices of crude oil since mid 1970’s, there has been a relative decline in the international prices of farm and plantation products, minerals and forest products.
- Consequently, the terms of trade have remained unfavourable to the developing countries.

Assumptions in the Prebisch-Singer thesis

- (i) As income rises in the advanced countries, the pattern of demand shifts from primary products to the manufactured products due to Engel’s law.
- (ii) There is slow rise in demand for products in the developed countries.
- (iii) The export market for product of LDC’s is competitive.
- (iv) The export market for products of developed countries is monopolistic.
- (v) Wages and prices are low in LDC’s.
- (vi) The appearance of substitutes for products of LDC’s reduces demand for them.
- vii) The economic growth in the LDC’s is indicated by income terms of trade.

- Singer has pointed out that the recent increase in debt problem of the LDC’s has imparted another twist to the hypothesis of secular deterioration of terms of trade for them in two ways.
- Firstly, a high proportion of proceeds from exports are not available for imports.
- Secondly, there is an increased pressure upon the LDC’s to raise exports in order to repay external debts on account of IMF-induced adjustment polices.
- These pressures make the debt- ridden LDC’s to compete with other poor countries to enlarge their export earnings.
- It results in decline in the prices of export products of these countries.

Criticisms of Prebisch-Singer Thesis

(i) Not Firm Basis for Inference:

The inference of secular deterioration of terms of trade for the LDC's rests upon the exports of primary vis-a-vis manufactured products.

(ii) Faulty Statement of Gains and Losses of Primary Exporters:

Jagdish Bhagwati has pointed out that the index of terms of trade employed in this thesis understates the gains of exporters of primary products.

(iii) Faulty Index of TOT:

This index overlooks the qualitative changes in products, appearance of new varieties of products, services like transport etc.

- **Neglect of Supply Conditions:**

In the determination of terms of trade, the Prebisch-Singer thesis considers only demand conditions.

- **Little Effect of Monopoly Power:**

One of the arguments in support of this thesis was that the higher degree of monopoly power existing in industry than in agriculture led to secular deterioration of terms of trade for the developing countries.

- **Benefits from Foreign Investment:**
- The deterioration of the terms of trade for the LDC's is sometimes linked not to non-transmission of productivity gains to them by advanced countries through lower prices of manufactured goods, yet the benefits from foreign investments have percolated to the LDC's through the product innovations, product improvement and product diversification.

Free Trade Vs Protectionism

- All economies, regardless of their size, depend to some extent onother economies and are affected by events outside their borders.
- If there were an Economist’s Creed it would surely contain the affirmations: ‘I understand the principle of comparative advantage’ and free trade’”Paul Krugman
- Trade Protection (Protectionism) - Policies that limit imports, usually with the goal of protectioning domestic producers in import-compelling industries from foreign competition

Myrdal Theses

- The Myrdal theses and free trade represent two different perspectives on the role of international trade in economic development. Let’s discuss each of them separately.
- Myrdal Theses: The Myrdal theses were proposed by Swedish economist Gunnar Myrdal in his influential book “Asian Drama: An Inquiry into the Poverty of Nations” published in 1968.
- Myrdal argued that the prevailing patterns of trade and development were inherently unequal and perpetuated underdevelopment in the Global South. He highlighted the following points

- a. Cumulative Causation: Myrdal emphasized the concept of cumulative causation, which suggests that initial economic advantages lead to further growth and development, while initial disadvantages create a vicious cycle of poverty and underdevelopment.
- According to Myrdal, the international trading system tends to reinforce existing
- inequalities between developed and developing countries.
- b. Structural Dependency: Myrdal also argued that developing countries faced structural dependency on developed nations due to their reliance on primary commodity exports. He believed that this dependence on exporting raw materials without sufficient created a vulnerable position for developing countries in the global economy.

- State/Government Intervention:
- Myrdal advocated for state intervention and planning as a means to address the structural imbalances created by international trade. He proposed policies such as import substitution industrialization (ISI), where countries develop their domestic industries to replace imported goods, and economic planning to promote equitable development.

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- imbalances created by international trade.
- He proposed policies such as import substitution industrialization (ISI), where countries develop their domestic industries to replace imported goods, and economic planning to promote equitable development.
- **Free Trade:** Free trade, on the other hand, is an economic concept that advocates for the absence of barriers or restrictions on the movement of goods and services between countries. Supporters of free trade argue that it brings several benefits
- a. Comparative Advantage: Free trade allows countries to specialize in the production of goods and services in which they have a comparative advantage. This leads to increased efficiency, productivity, and economic growth
- b. Lower Prices and Increased Variety: By eliminating trade barriers, free trade promotes competition, which drives down prices and provides consumers with a wider range of products to choose from. This enhances consumer welfare and increases living standards.

- c. Resource Allocation: Free trade enables countries to allocate their resources more efficiently by focusing on industries where they have a comparative advantage. This leads to the optimal utilization of resources and overall economic efficiency.
- d. Global Economic Integration: Free trade fosters economic integration and cooperation among nations. It encourages interdependence, promotes peace, and reduces the likelihood of conflicts by creating shared economic interests
- Myrdal theses critique the prevailing patterns of trade and development, highlighting their unequal nature and the need for state intervention to address structural imbalances.
- On the other hand, free trade advocates for the removal of trade barriers, emphasizing the benefits of specialization, competition, and resource allocation. These perspectives represent different views on the role of international trade in economic development, and the debate between them continues among economists and policymakers.

World Trade Organization

- The World Trade Organization, also known as WTO, is a Global organization that deals directly with making rules and regulations among the Nations with respect to trading.
- It was constituted on the 1st of January 1995. India also joined the WTO in 1995 and is a founding member of the World Trade Organization.
- WTO is headquartered in Geneva, Switzerland, and it consists of 164 countries, where 160 are **United Nations** countries, along with the EU, Hong Kong, Macau, and Taiwan.
- Apart from this, WTO also acts as a forum that negotiates the trading agreement and settles down trading disputes among countries by providing support and a full feeling of the needs of developing countries

Objectives of the WTO

- WTO aims to reduce barriers to trade and promote economic growth and development among its member countries. Let’s explore the major objectives of WTO below.
- To limit the trading barriers by negotiating. This results in a reduction in the prices of goods and services, which in turn results in a reduction in the cost of living.
- Stimulating **economic growth and development**, and employment opportunities
- Limit the cost of international business activities.
- To promote the concept of **good governance**.
- To reduce the trade disputes among the countries.
- Collaborating with leading financial institutions to boost economic management.

Functions of WTO

- The functions of the WTO are numerous and critical in facilitating a fair and open international trade system. The major functions of WTO include the following.
- It regulates the laws related to trade agreements.
- Organize the conferences for trade negotiations.
- Sort out and resolve the issues related to trading.
- examines trade-related policies
- Consult and cooperate with economic organizations.

Role of Trade

- Trade Development:
- The main objective behind the emergence of the WTO is to maintain the free flow of trade as much as possible without any undesirable consequences like unfair competition, hegemony in a certain variety of goods or services, biassed trade policies, etc.
- WTO helps the inclusion of developing countries in the international trading system and helps them to achieve economic growth and ensure full employment.
- It oversees the trade rules and policies governing international trade and ensures that they are transparent and easily predictable.

- Dispute settlement:
- In conducting international trade, several trade disputes also arise due to the conflicting interests of one nation and those of another nation. These disputes have been settled or negotiated by the WTO, which also involves the interpretation of WTO agreements.
- The WTO, as a neutral body, settles these disputes in accordance with the Dispute Settlement process provided in WTO agreements.

Pillar of Economic Relations

- Dispute settlement is the central pillar of the multilateral trading system, and the WTO's unique contribution to the stability of the global economy.
- The primary goal of WTO is to give an open and free trade space to international traders where they can do trading without any obstruction.
- It makes and implements the rules related to international trading.
- It creates a venue for liberalization negotiation and trade monitoring.
- It makes decisions that are more transparent and fair with all the member countries.
- It also works with other important economic Institutions and works actively for Global economic management.
- It opens the ground and provides a platform to the countries that can take advantage of WTO for the global Trading system.

Developing Country Status in WTO

- There are **no WTO definitions of "developed" and "developing" countries. Members announce for themselves** whether they are "developed" or "developing" countries.
  - However, other members can challenge the decision of a member to make use of provisions available to developing countries.
- The WTO Agreements contain special provisions which **give developing countries special rights.** These provisions are referred to as **"Special and Differential Treatment" (S&D) provisions.**

- The **special provisions** include:
  - **Longer time periods** for implementing Agreements and commitments,
  - Measures to **increase trading opportunities** for developing countries,
  - Provisions requiring all WTO members to **safeguard the trade interests** of developing countries,
  - Support to help **developing countries build the capacity** to carry out WTO work, handle disputes, and implement technical standards, and
  - Provisions related to least-developed country (LDC) Members.

Benefits to Developing Countries in the WTO:

- The Agreement Establishing the World Trade Organization (also known as **“the WTO Agreement”**) specifies that **international trade** should **benefit the economic development of developing** and least-developed countries.
- **General Agreement on Tariffs and Trade (GATT)—** gives developing countries the **right to restrict imports, if** doing so would promote the establishment or **maintenance of a particular industry,** or assist in cases of balance-of-payments difficulties.
- **Part IV of the GATT** includes provisions on the concept of **non-reciprocal preferential treatment for developing countries, i.e.** when developed countries grant trade concessions to developing countries they should not expect the developing countries to make matching offers in return.
    - However, developing countries claim that Part IV has been without practical value as it **does not contain any obligations for developed countries.**

Foreign Trade

- Foreign Trade is the exchange of goods and services between two countries in the international market.
- It helps in the availability of raw material/finished product in a country that either does not have it or has it in scarcity.
- No country is self-sufficient in terms of natural or man-made resources,, so it is prudent to approach other countries that have them in abundance.

Types of Foreign Trade

- There are three different types of foreign trade, which are as follows:
- **Import trade:** It is the purchase of goods and services by one country from another country. Here the flow of goods is from a foreign land to the home nation. Countries import goods and services when they need raw materials for producing goods or when they need a finished product for domestic consumption.
- **Export trade:** It is the selling of goods and services to another country. Here the flow of goods is from the home nation to a foreign land. Countries export goods and services to another nation when they have that particular commodity in abundance.
- **Entrepot trade:** This process is also called re-export. In this form of trade, a business purchases goods or services from one country, reprocesses those products, and then sells them to another country.

Benefits of Foreign Trade:

- Foreign Trade has many benefits for all the countries involved in it. Some of the advantages of exchanging goods in the international market are as follows:
- **Foreign Exchange:** Foreign Trade helps countries get access to foreign currency and boost up their reserves. This currency is essential when it comes to paying for imports of goods and services.
- **Consumers get more options:** People from one country enjoy superior quality goods and services from other nations. They would not have gained access to these products were it not for International trade. These products can also help them improve their standard of living in the long run.
- **Optimum use of a nation's resources:** No country can fulfil all its consumption needs independently. They have to depend on other nations for specific products. International trade allows them to procure raw materials/finished products that they don't have. It helps countries focus on producing what they are good at and help increase efficiency in the production process of those products.
- **Economic Benefits:** International trade generates employment opportunities for organisations and countries involved in the export/entrepot of goods and services. It also helps to improve the Gross Domestic Product for that country.

Foreign Investment

- Foreign Investment is the inflow of capital into a country through individuals/institutions from a different country.
- The flow of capital is from one organisation, with its headquarters in a foreign nation, into another company that belongs to the home nation.
- The investment helps companies based abroad to set up their offices or manufacturing units in another country.
- Since the foreign entity gets a stake in the domestic company in exchange for providing capital, they have to follow local government rules and regulations regarding such investments.

Types of Foreign Investment

- There are three different ways in which a company belonging to one country can invest in another country. These methods of investment are as follows:
- **Foreign Direct Investment:** This type of investment involves a foreign company infusing capital into another country's business or production units.
- **Foreign Portfolio Investment:** When an organisation based outside the country invests in the securities market of that country, it becomes a foreign portfolio investment.
- **Foreign Institutional Investment:** This is a form of investment by a foreign-based company in the passive holdings of an entity in another country.

Benefits of Foreign Investment

- The main advantages of foreign investment are as follows:
- **Economic growth:** Infusion of foreign capital helps domestic companies increase production and generate employment. It can also boost consumption in the market since the workforce in those companies will have greater purchasing power. It contributes to the overall growth of a country’s economy.
- **Resource transfer:** Foreign investment brings capital and helps the domestic workforce get access to new technologies and skills. It will help in improving their productivity while also developing the quality of goods and services produced.
- **Cost benefits:** Foreign investment can help domestic companies improve production efficiency and reduce costs via access to better technologies.

Differences between Foreign Trade and Foreign Investment

Foreign Trade	**Foreign Investment**
Meaning	
It involves the exchange of goods and services between two countries in the international market.	It involves the investment made by a foreign company into another company based in a different country.
Purpose	
The main purpose of foreign trade is as follows: •To help countries access goods and services that they need from international markets. •To sell their products in those markets and earn foreign exchange.	The primary purpose of foreign investment is as follows: •Gain access into the market of another country by providing capital and getting a stakeholding in a local company. •Use that access to conduct business and make profits.
Benefit	
Access to international markets for domestic companies.	Access to long term capital to a company via foreign investors.
Flow of resources	
Foreign trade enables both inflow and outflow of raw materials/finished products between countries.	The foreign investment enables the inflow of capital and technologies into a country from abroad.
Types	
The three types of foreign trade are as follows: •Import •Export •Entrepot	The three types of foreign investment are as follows: •Foreign Direct Investment •Foreign Portfolio Investment •Foreign Institutional Investment