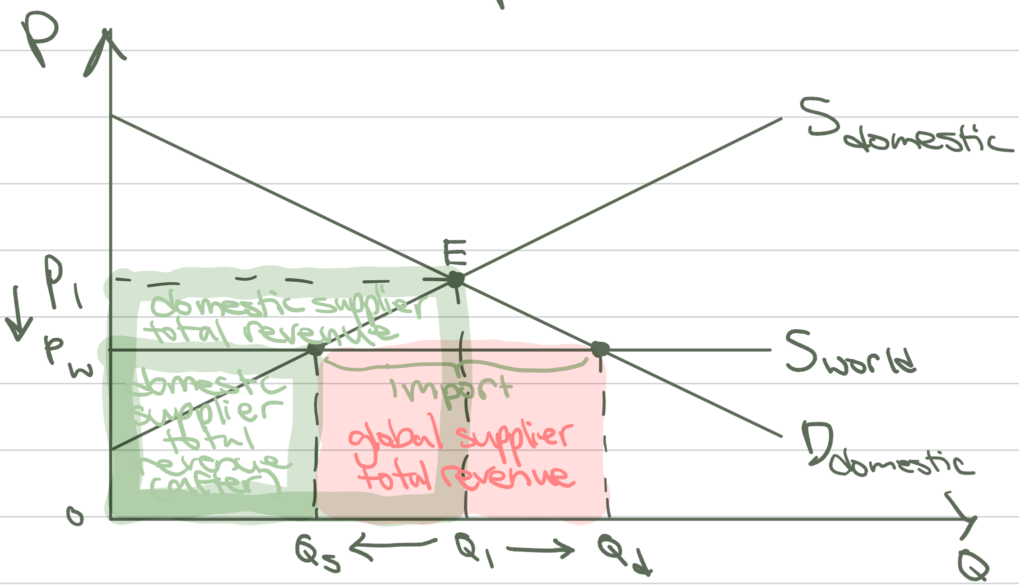
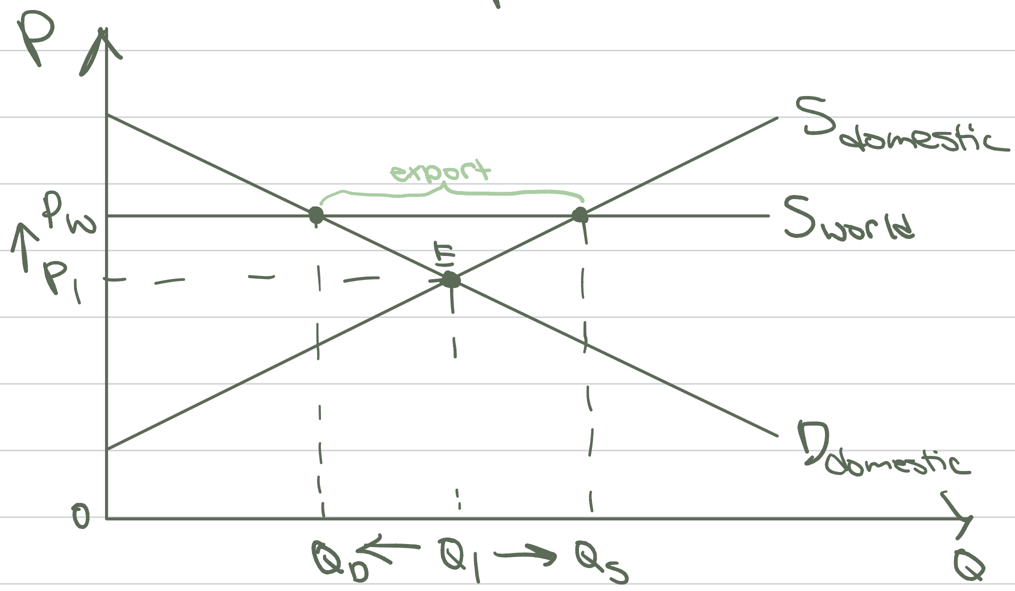
The Global Economy (Diagrams)

Free-Trade

Imports



Exports

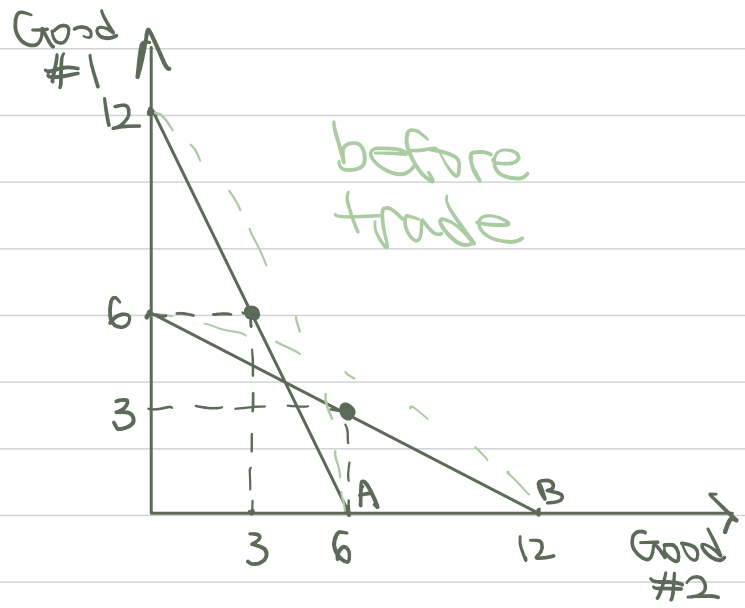


Quantity imported $= Q_d - Q_s$
Import expediture $= P_w(Q_d - Q_s)$

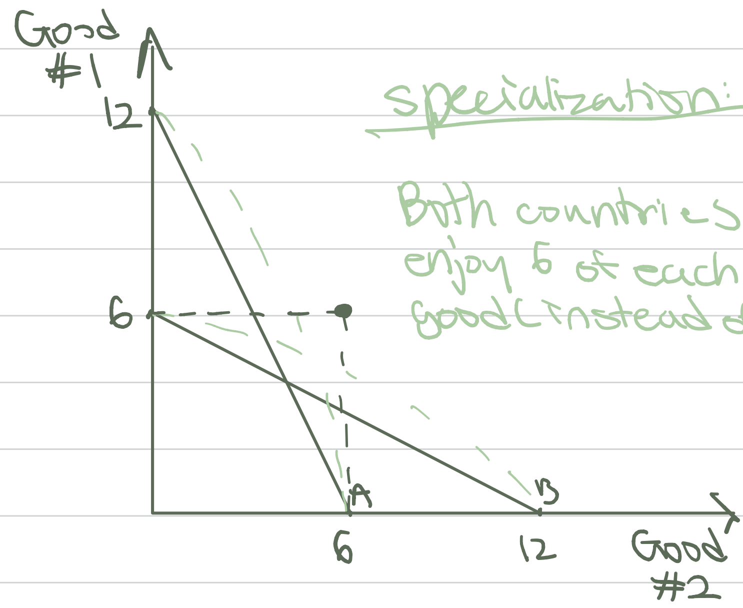
Quantity exported $= Q_s - Q_d$
Export expenditure $= P_w(Q_s - Q_d)$

Absolute advantage: country is able to produce more output than other countries using the same input of factors of production.
(both intercepts higher)

Comparative advantage: country is able to produce a good at a lower opportunity cost of resources than another country
(slope higher for y-axis good & slope lower for x-axis good)



1. Country A has a comparative advantage for Good #1
2. Country B has a comparative advantage for Good #2
3. Specialize and then trade half with other country.



specialization:
Both countries enjoy 6 of each good (instead of 3)

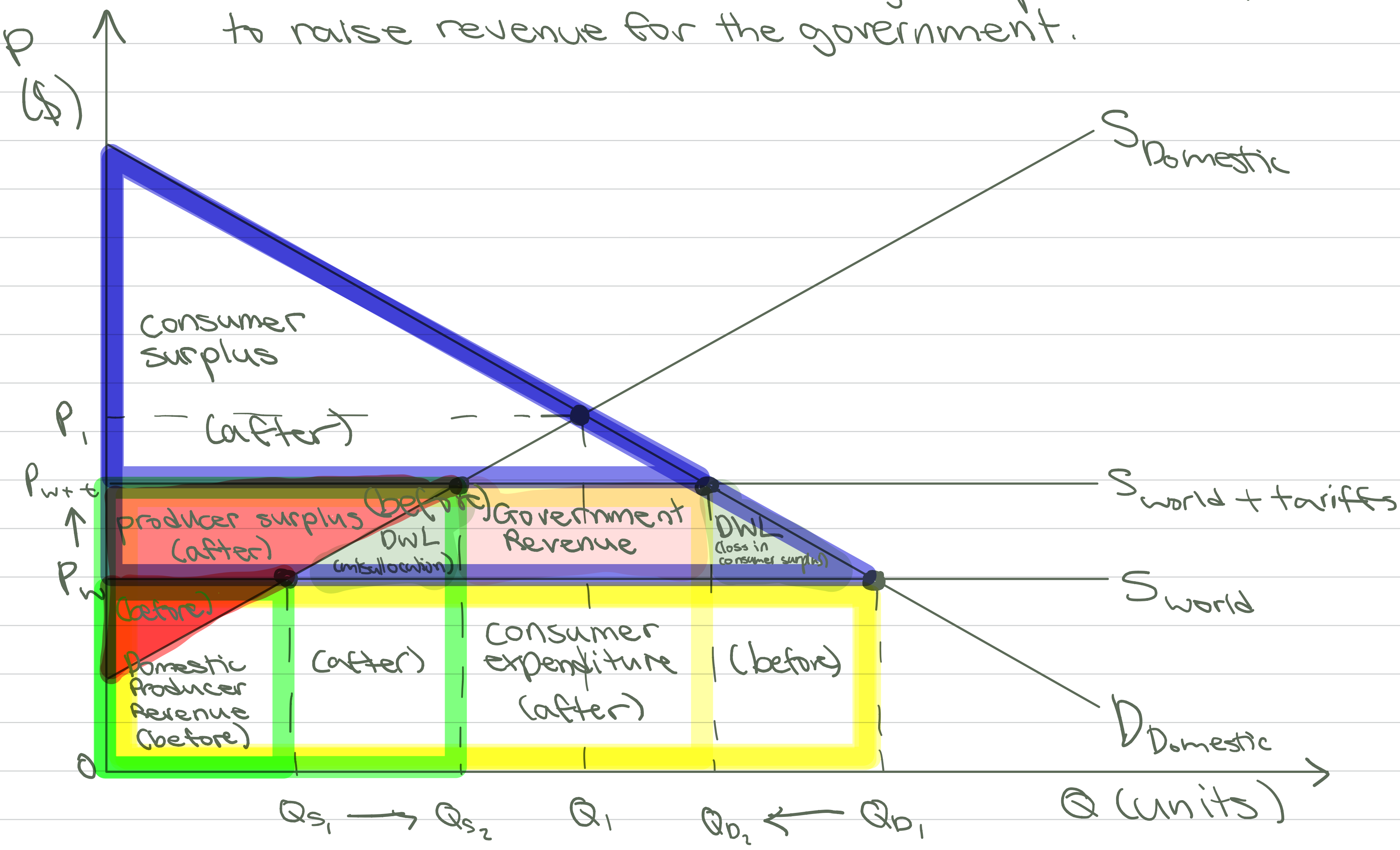
	Good #1	Good #2
Country A	12	6
Country B	6	12
Absolute Advantage	Country A	Country B

calculating opportunity cost →

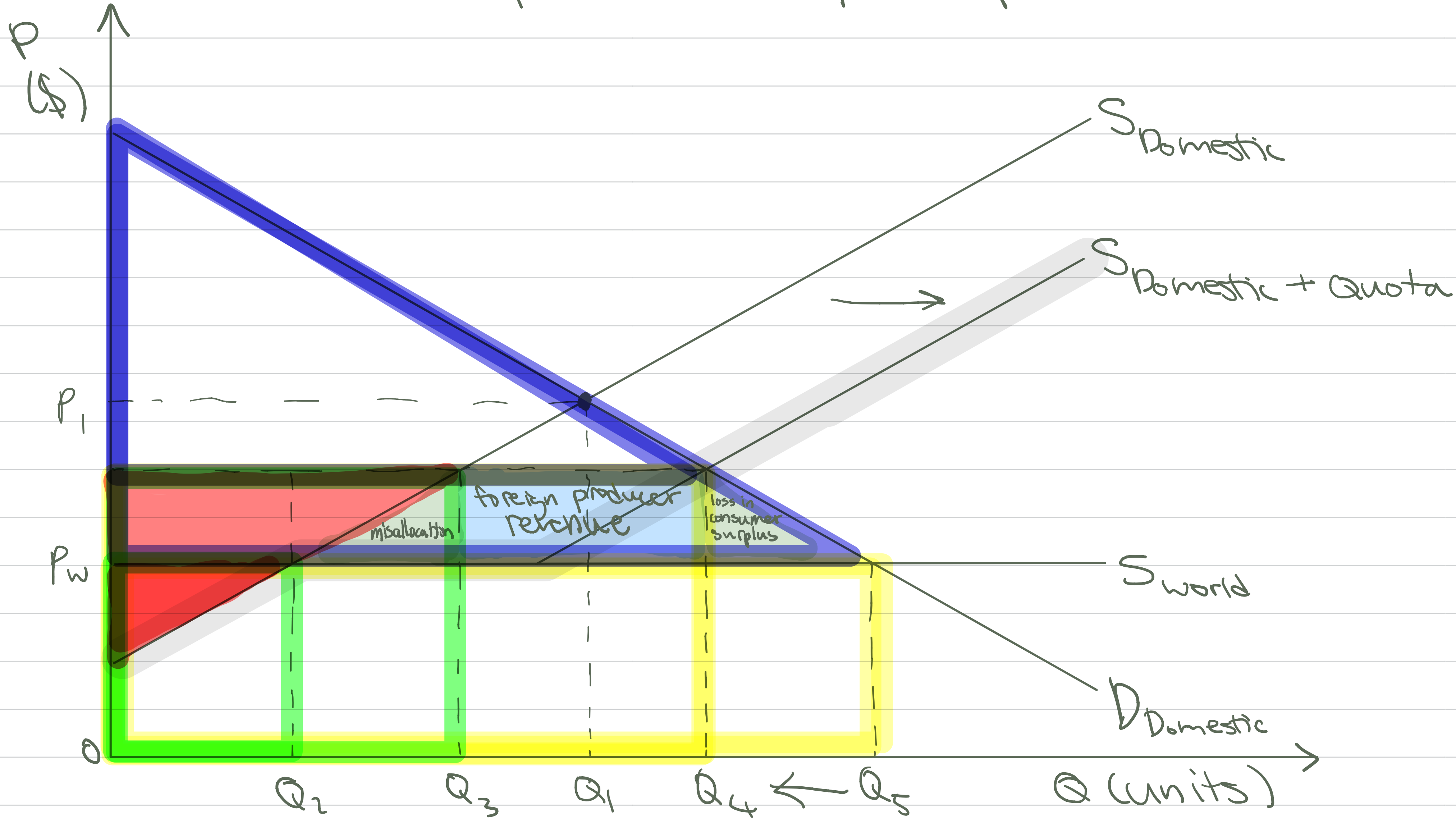
	Good #1	Good #2
Country A	$6 \div 12 = \frac{1}{2}$	$12 \div 6 = 2$
Country B	$12 \div 6 = 2$	$6 \div 12 = \frac{1}{2}$
Comparative Advantage	Country A	Country B

(types of) Trade Protection

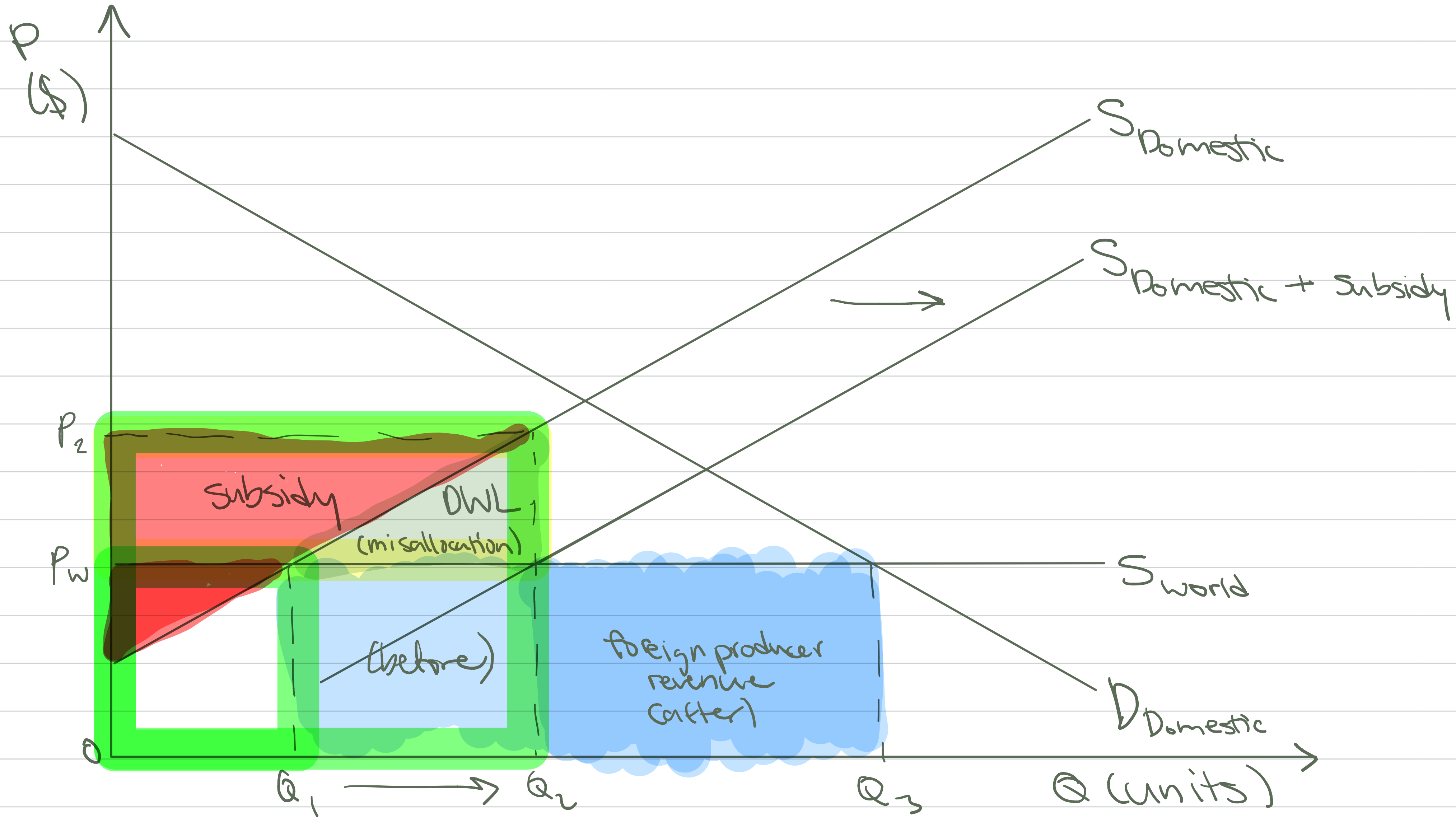
Tariffs: a duty that is placed upon imports to protect domestic industries from foreign competition and to raise revenue for the government.



Quotas: import barriers that set limits on the quantity or value of imports that may be imported into a country.



Subsidies: financial support paid by goverments to firms



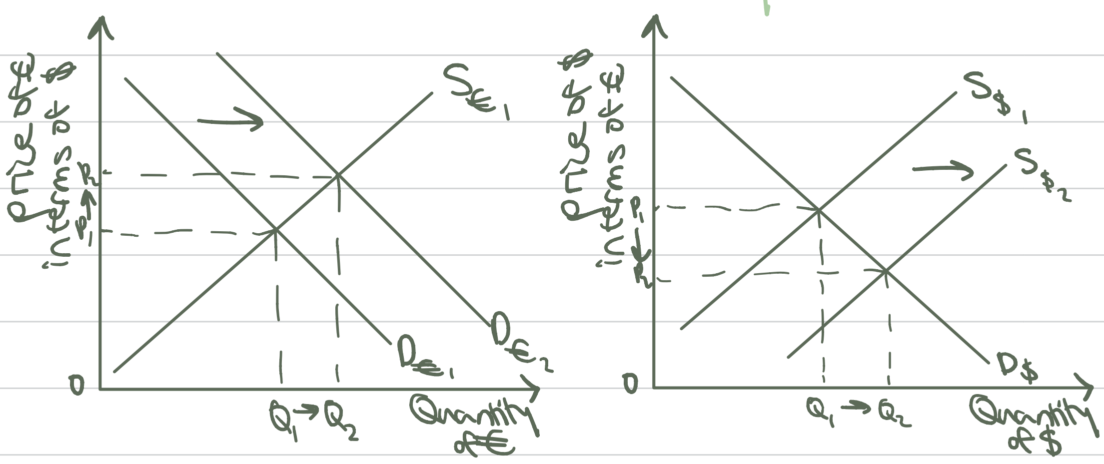
Administrative barriers:
↳ product standards
↳ voluntary export restraints
↳ 'Buy National' policies

Exchange Rates

1. Floating exchange rate
↳ an exchange rate regime where the value of a currency is allowed to be determined solely by the demand for, and supply of, the currency on the foreign exchange market.

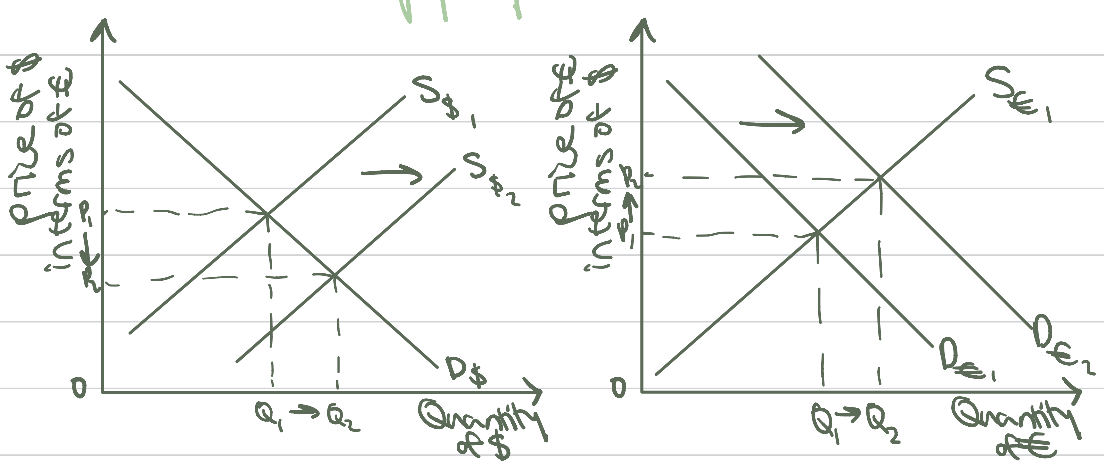
Appreciation of Value

Demand↑ (buy)



Depreciation of Value

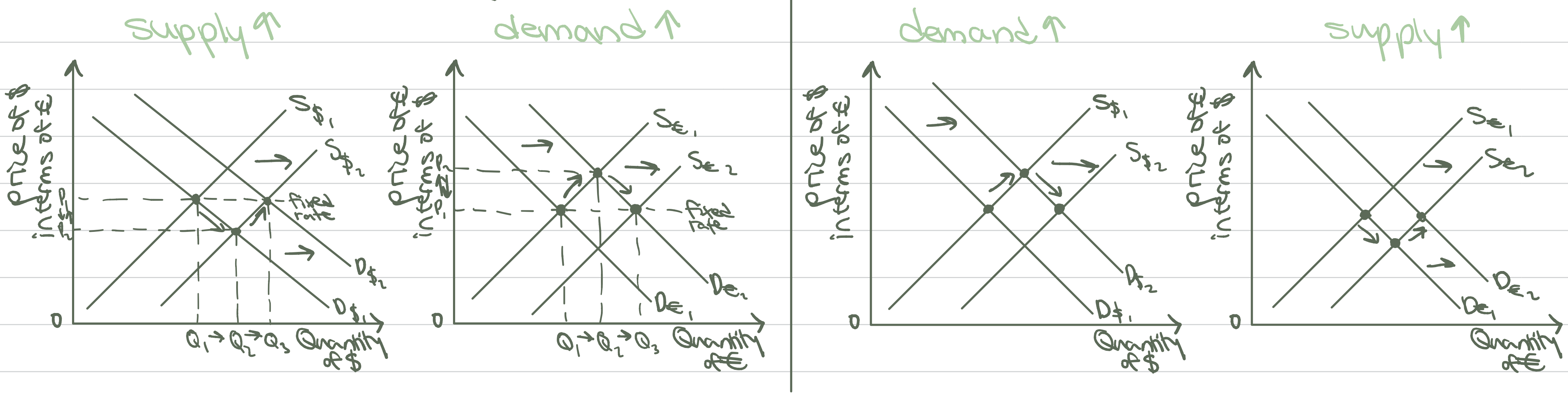
Supply↑ (sell)



2. Fixed exchange rate

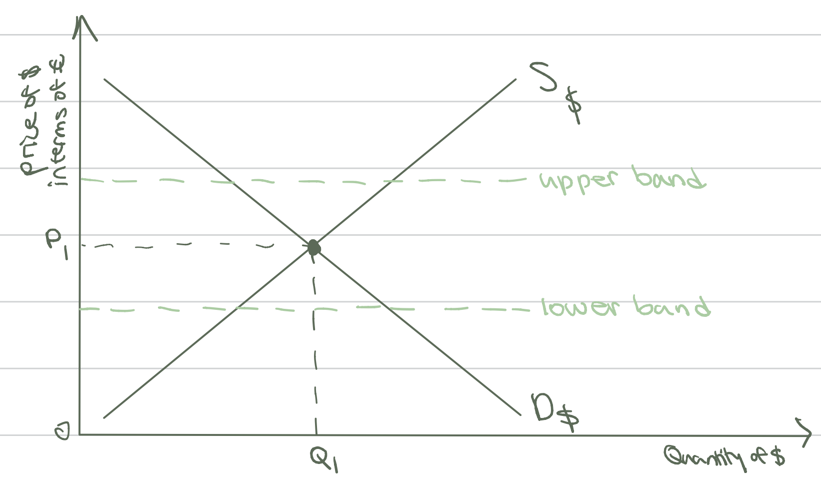
↳ an exchange rate regime where the value of a currency is fixed, or pegged, to the value of another currency, or to the average value of some other commodity, such as gold.

Revaluation | **Devaluation**



3. Managed float exchange rate

↳ an exchange rate that floats in the foreign exchange markets but is subject to intervention from time to time by domestic monetary authorities, in order to resist fluctuations that they consider to be undesirable.



The central bank will only intervene when the exchange rate falls outside of these bands.

Balance of Payments

Current account + capital account + financial account = 0

- **Current account** ↓ record of all the money coming into and going out of a country for trade in goods and services, income flows and transfers.
- **Capital account** ↓ a measure of the buying and selling of assets between country.
- **Financial account** ↓ a measure of the net change in foreign ownership of domestic financial assets.

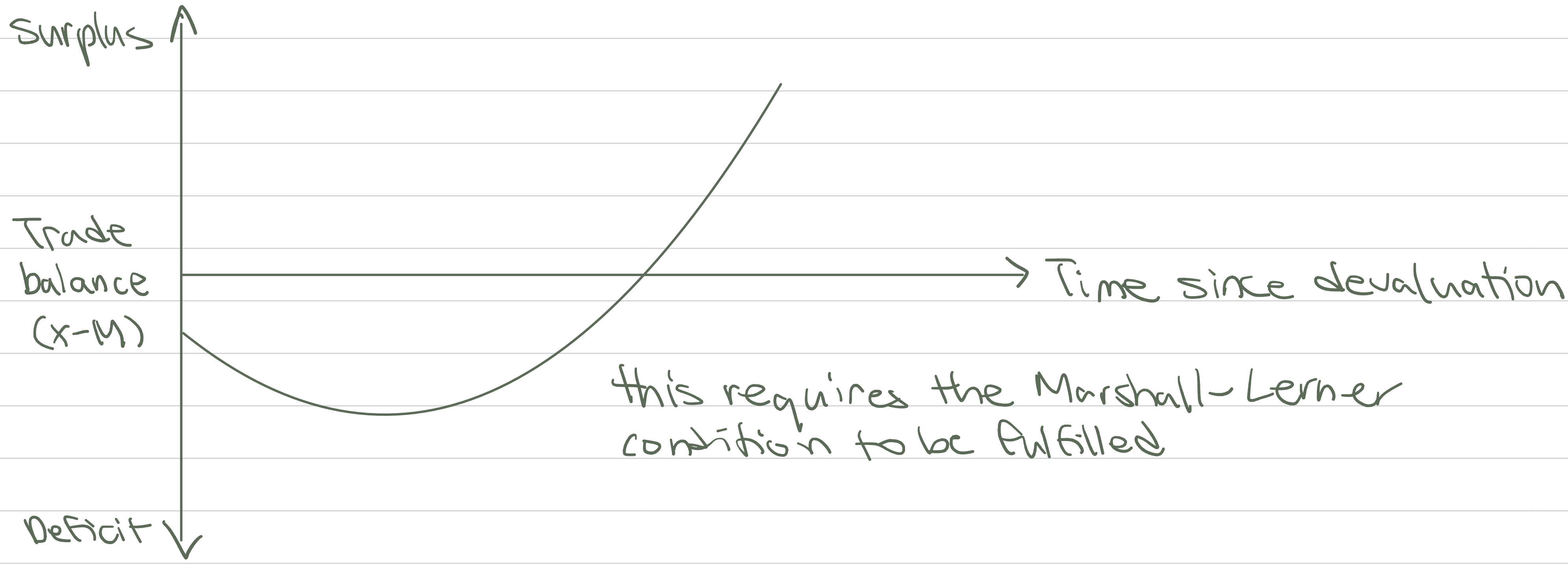
current account = exports − imports + net income + net foreign aid

capital account = capital transfers + rights

financial account = ΔFDI + ΔPortfolio Investment + ΔReserve Assets + ΔOfficial Borrowing

Marshall-Lerner: $PED_{imports} + PED_{exports} > 1$

J-curve



Poverty cycle