International Trade

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International trade is the exchange of capital, goods,
and services across international borders or territories because there is a need or want of goods or services.

In most countries, such trade represents a significant share of gross domestic product (GDP). While international trade has existed throughout history (for example Uttarapatha, Silk Road, Amber Road, scramble for Africa, Atlantic slave trade, salt roads), its economic, social, and political importance has been on the rise in recent centuries.

Carrying out trade at an international level is a complex process when compared to domestic trade. When trade takes place between two or more nations factors like currency, government policies, economy, judicial system, laws, and markets influence trade.

To smoothen and justify the process of trade between countries of different economic standing, some international economic organisations were formed, such as the World Trade Organization. These organisations work towards the facilitation and growth of international trade. Statistical services of intergovernmental and supranational organisations and national statistical agencies publish official statistics on international trade.

Differences Between International Trade and Domestic Trade

1. Language:

Different countries have different languages. This factor can and often does act as a barrier to trade. Traders who sell abroad may have to employ language specialists and incur additional expenses through the necessity of having special forms, labels, instructions, etc., printed.

2. Differences Regarding Mobility of Labour and Capital:

In the case of domestic trade there is a fair amount of mobility of labour and capital, but the immobility of labour and, to a smaller extent, of capital is found in the case of international trade. Labour and capital are fairly mobile within the country, but they cannot freely move between two countries.

3. **Differences in Natural and Economic Conditions**:

The natural and economic conditions are, so far as international trade is concerned, not the same in all countries. Some countries have greater natural advantages in producing jute or tea, and some in making machines or electronic goods.

It leads to the international specialisation or division of labour. International trade is based on this international specialisation. But, the natural and economic conditions do not, so far as domestic trade is concerned, very much in the different parts of a country.

4. **Differences in Banking Systems and Economic Policies**:

Monetary, banking and currency systems as also economic policies of different countries also differ. International trade is governed by these differences in domestic economic policies and regulations. But, such restrictions (except minor restrictions like entry tax, restrictive inter-state movement of essential goods such as rice or wheat, etc.) do not, as a rule, exist between the different regions of a country and so do not affect, in a large measure, domestic trade.

5. **Currency**:

Each country has a different currency, that is a different type of money which is acceptable only within its own frontier. In India, the currency is the rupee, in France the franc, while in the United States it is dollar. If an Indian importer buys goods from a French manufacturer then payment must be made in francs which have to be purchased in the foreign exchange market.

Such a procedure is both time-consuming and cost-raising than any payment made in the home country. Furthermore, foreign exchange rates often vary and an adverse movement in the conversion rate may involve a trader in a loss.

6. **Systems of Payment**:

As far as payment is concerned there may be more delay and less certain in foreign trade than in case of domestic trade. An exporter has to obtain payment from a

debtor who may live on the other side of the world and about whom very little is known.

The exporter will be reluctant to ship the goods without being reasonably certain of payment, while the importer will not wish to pay without some guarantee for receipt of the goods. In domestic trade, a manufacturer may often get cash on delivery or quick payment from a wholesaler.

7. **Distance**:

The risks involved in transporting goods increase with the distance and the frequency with which the goods are handled. Hence, there is greater chance of loss, damage or delay when sending goods to countries abroad.

8. **Customs Duties and Import Quotas**:

Certain goods may be subject to heavy duties or tariffs. This often makes it almost impossible for exports to compete in price with home products. Furthermore, exports may be limited by quotas imposed by importing countries.

Even if exporters consider they can compete (in spite of customs duties) they have to ensure that the correct duty is paid. Duties vary according to the way that goods are classified and strict penalties apply to false declarations. Hence, a correct understanding of the classifications list is absolutely essential.

Finally, exporters run the risk that duties and quotas may be changed suddenly so that their market in a particular country may be suddenly lost, either partly or fully.

9. **Competition**:

At home, a manufacturer may be protected from foreign competition by duties or quotas imposed by the government. Hence, competition may be restricted to other home manufacturers. However, in foreign markets, the manufacturer may have to face competition from producers in that market as also from other foreign exporters.

10. **Local Conditions**:

Exporters have to consider the customs and habits of the countries to which they sell goods. For example, foreigners may like their goods in different dimensions and in different kinds of packages from those found suitable in the home market. Similarly, attention has to be given to various methods of trading adopted in foreign markets.

For example, at home manufacturers may leave the provision of spare parts and after-sales service to others, but if no such facilities are available abroad importers must themselves contact other firms to get such facilities. Thus, international trade involves much greater risks and difficulties than domestic trade.

Role of International Trade in Economic Development

International Specialisation:

International trade enables a country to enjoy the advantages of international specialisation according to comparative costs. Every country specialises and exports those commodities which it can produce cheaper in exchange for what others can provide at a lower cost.

When a country specialises according to its comparative advantage, it gains an increase in real income and consequent rise in the standard of living of its people.

Therefore, international trade by enabling better and more efficient utilisation of the resources of a country increases its real national income and hence has a growth-promoting effect.

Widening of Market and Raising Productivity:

It is argued that the productivity gains arising out of extension of market is a consequence of foreign trade. Improvements in productivity result from greater division of labour, a higher degree of mechanisation and greater possibility of innovation.

Foreign trade, by widening the extent of the market and the scope of the division of labour, permits a greater use of machinery, stimulates innovations, overcomes technical indivisibilities, raises the productivity of labour, and generally enables the trading country to enjoy increasing returns and economic development.

Thus foreign trade, by extending the size of the market, exercises a dynamic influence on the economy. In turn, it helps to raise the production at higher trade. As a result, country enjoys the benefits of external and internal economies of scale.

Helpful for High Growth Potential:

Foreign trade also helps in the development of a country enabling it to exchange domestic goods saving low growth potential for foreign goods with high growth potential.

It provides an opportunity for importing capital goods and materials required for development purposes. The import of machinery, transport equipment, vehicles, power generation equipment, road building machinery, medicines, chemicals and other goods with high growth potential provides greater benefits to the developing countries.

Educative Effect of Trade:

International trade can serve as a vehicle for the dissemination of technological knowledge. A deficiency of knowledge can be a biggest handicap in the development of a country and this deficiency can be effectively removed through contact with more advanced economies i.e. by making possible through foreign trade.

The technical know-how and skills is an indispensable source of technological progress, and the importation of ideas in general is a potent stimulus to development.

Capital Formation:

Foreign trade helps to increase capital formation. The capacity to save increases as real income rises through the more efficient resource allocation associated with international trade. Foreign trade also provides stimulus for investment and thus it tends to raise the rate of capital formation.

This stimulus comes from the possibility of realising increasing returns in wider markets that foreign trade provides. Moreover, by allowing economies of large scale production, the access to foreign markets makes it profitable to adopt more advanced techniques of production.

Thus international trade, by creating conditions for increased capital formation in underdeveloped countries, can help in their economic development.

Basis of Import of Foreign Capital:

International trade also helps in promoting development by creating suitable conditions for the import of foreign capital.

The amount of capital that an underdeveloped country can obtain from foreign countries depends to a considerable extent on the volume of its trade. The larger the volume of trade of a country, the greater will be the volume of foreign capital that can be expected to become available to it.

It is an established fact that it is much easier to get foreign capital for export industries because they have a built-in solution of the transfer problem.

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The underdeveloped countries are characterized by the existence of vicious circle of poverty. It implies, low income, deficiency of demand and lack of demand accounts for low supply which in turn accounts for low income. But, international trade enables underdeveloped countries to produce more of those goods in which they enjoy greater comparative advantage.

Consequently, production, income and employment in these countries increase leading to increase in demand. This increase demand is partially met by domestic production and partially by foreign imports. In this way, exports and imports of various products help in breaking the vicious circle of poverty.

Thus, it accelerates the rate of economic development automatically in the economy.

Efficient Use of Means of Production:

International trade, it is felt, provides better ground for efficient use of various resources due to its comparative advantages. According to Prof. J.S. Mill it adds to the efficiency of production. In underdeveloped economies, agriculture is backward and subsistence farming is the rule.

With the development of trade, use of latest and improved techniques of production become possible in agriculture as well in industrial sector.

This, in turn helps to increase, the efficiency of means of production. The commercialisation of agriculture becomes possible. Similarly, many new industries come into being and some of them are meant for the production of export goods

only. Therefore, efficient use of means of production leads to all-round development of the economy.

Import of Capital Goods & Export of Primary Goods:

Another direct advantages of foreign trade for the economic development of underdeveloped countries is that these countries can industrialize themselves by importing necessary capital goods like machinery, semi-finished products and industrial raw materials from industrialized developed countries.

In return, these countries can export primary goods and mineral resources and thus solve the problem of balance of payments. In this way, import of capital goods and export of primary goods are possible under foreign trade.