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Advantages Of International Economy

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Abstract: The economic theory of international trade differs from the remainder of economic theory mainly because of the comparatively limited international mobility of the capital and labor.[5] In that respect, it would appear to differ in degree rather than in principle from the trade between remote regions in one country. Thus the methodology of international trade economics differs little from that of the remainder of economics. However, the direction of academic research on the subject has been influenced by the fact that governments have often sought to impose restrictions upon international trade, and the motive for the development of trade theory has often been a wish to determine the consequences of such restrictions. The branch of trade theory which is conventionally categorized as "classical" consists mainly of the application of deductive logic, originating with Ricardo's Theory of Comparative Advantage and developing into a range of theorems that depend for their practical value upon the realism of their postulates. "Modern" trade analysis, on the other hand, depends mainly upon empirical analysis.

Key words: Economy, analysis, application, academic.

1. INTRODUCTION

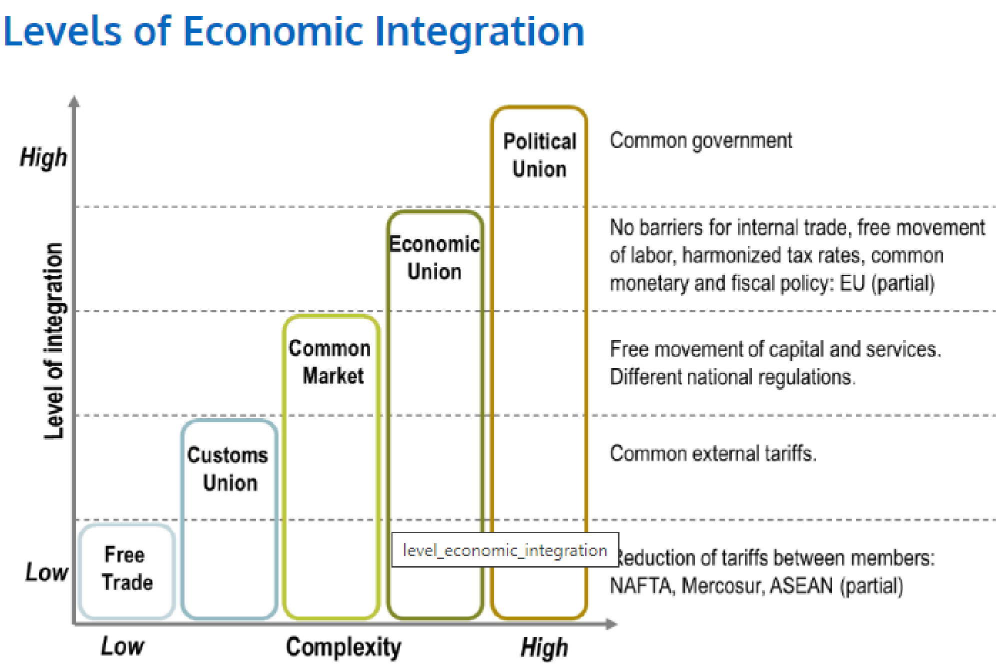
The theory of comparative advantage provides a logical explanation of international trade as the rational consequence of the comparative advantages that arise from inter-regional differences - regardless of how those differences arise. Since its exposition by David Ricardo[6] the techniques of neo-classical economics have been applied to it to model the patterns of trade that would result from various postulated sources of comparative advantage. However, extremely restrictive (and often unrealistic) assumptions have had to be adopted in order to make the problem amenable to theoretical analysis.

The best-known of the resulting models, the Heckscher-Ohlin theorem (H-O)[7] depends upon the assumptions of no international differences of technology, productivity, or consumer preferences; no obstacles to pure competition or free trade and no scale economies. On those assumptions, it derives a model of the trade patterns that would arise solely from international differences in the relative abundance of labour and capital (referred to as factor endowments). The resulting theorem states that, on those assumptions, a country with a relative abundance of capital would export capital-intensive products and import labour-intensive products. The theorem proved to be of very limited predictive value, as was demonstrated by what came to be known as the "Leontief Paradox" (the discovery that, despite its capital-rich factor endowment, America was exporting labour-intensive products and importing capital-intensive products[8]) Nevertheless, the theoretical techniques (and many of the assumptions) used in deriving the H–O model were subsequently used to derive further theorems.
The Stolper–Samuelson theorem,[9] which is often described as a corollary of the H–O theorem, was an early example. In its most general form it states that if the price of a good rises (falls) then the price of the factor used intensively in that industry will also rise (fall) while the price of the other factor will fall (rise). In the international trade context for which it was devised it means that trade lowers the real wage of the scarce factor of production, and protection from trade raises it.
Another corollary of the H–O theorem is Samuelson's factor price equalization theorem which states that as trade between countries tends to equalize their product prices, it tends also to equalize the prices paid to their factors of production.[10] Those theories have sometimes been taken to mean that trade between an industrialized country and a developing country would lower the wages of the unskilled in the industrialized country. (But, as noted below, that conclusion depends upon the unlikely assumption that productivity is the same in the two countries). Large numbers of learned papers have been produced in attempts to elaborate on the H–O and Stolper–Samuelson theorems, and while many of them are considered to provide valuable insights, they have seldom proved to be directly applicable to the task of explaining trade patterns.[11]

International financial stability

From the time of the Great Depression onwards, regulators and their economic advisors have been aware that economic and financial crises can spread rapidly from country to country, and that financial crises can have serious economic consequences. For many decades, that awareness led governments to impose strict controls over the activities and conduct of banks and other credit agencies, but in the 1980s many governments pursued a policy of deregulation in the belief that the resulting efficiency gains would outweigh any systemic risks. The extensive financial innovations that followed are described in the article on financial economics.One of their effects has been greatly to increase the international inter-connectedness of the financial markets and to create an international financial system with the characteristics known in control theory as "complex-interactive". The stability of such a system is difficult to analyses because there are many possible failure sequences. The internationally systemic crises that followed included the equity crash of October 1987,[43] the Japanese asset price collapse of the 1990s[44] the Asian financial crisis of 1997[45] the Russian government default of 1998[46](which brought down the Long-Term Capital Management hedge fund) and the 2007-8 sub-prime mortgages crisis.[47] The symptoms have generally included collapses in asset prices, increases in risk premiums, and general reductions in liquidity.
Measures designed to reduce the vulnerability of the international financial system have been put forward by several international institutions. The Bank for International Settlements made two successive recommendations (Basel I and Basel II[48]) concerning the regulation of

banks, and a coordinating group of regulating authorities, and the Financial Stability Forum, that was set up in 1999 to identify and address the weaknesses in the system, has put forward some proposals in an interim report.[49]



GLOBALIZATION

The term globalization has acquired a variety of meanings, but in economic terms it refers to the move that is taking place in the direction of complete mobility of capital and labour and their products, so that the world's economies are on the way to becoming totally integrated. The driving forces of the process are reductions in politically imposed barriers and in the costs of transport and communication (although, even if those barriers and costs were eliminated, the process would be limited by inter-country differences in social capital).

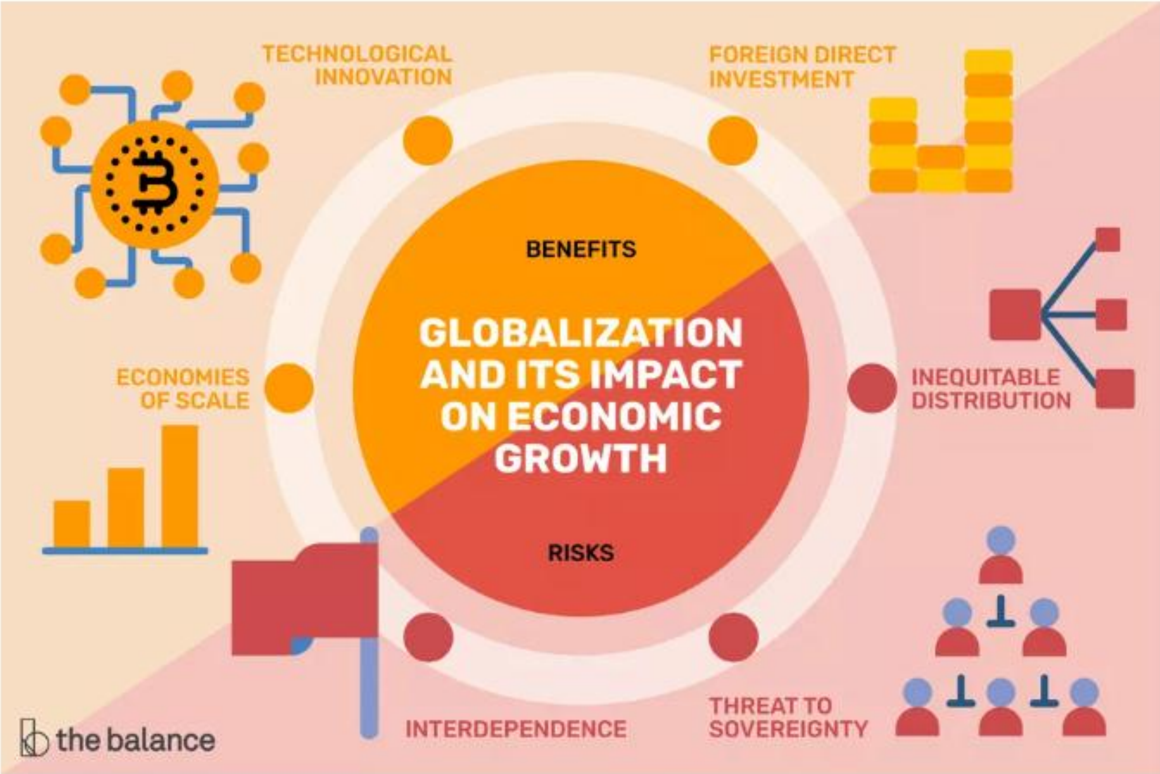
It is a process which has ancient origins, which has gathered pace in the last fifty years, but which is very far from complete. In its concluding stages, interest rates, wage rates and corporate and income tax rates would become the same everywhere, driven to equality by competition, as investors, wage earners and corporate and personal taxpayers threatened to migrate in search of better terms. In fact, there are few signs of international convergence of interest rates, wage rates or tax rates. Although the world is more integrated in some respects, it is possible to argue that on the whole it is now less integrated than it was before the first world war,[56] and that many middle-east countries are less globalized than they were 25 years ago.[57]

Of the moves toward integration that have occurred, the strongest has been in financial markets, in which globalisationis estimated to have tripled since the mid-1970s.[58] Recent research has shown that it has improved risk-sharing, but only in developed countries, and that in the developing countries it has increased macroeconomic volatility. It is estimated to have resulted in net welfare gains worldwide, but with losers as well as gainers. .[59]

Increased globalisation has also made it easier for recessions to spread from country to country. A reduction in economic activity in one country can lead to a reduction in activity in its trading partners as a result of its consequent reduction in demand for their exports, which is one of the mechanisms by which the business cycle is transmitted from country to country. Empirical research confirms that the greater the trade linkage between countries the more coordinated are their business cycles.[60]

Globalization can also have a significant influence upon the conduct of macroeconomic policy. The Mundell–Fleming model and its extensions[61] are often used to analyse the role of capital mobility (and it was also used by Paul Krugman to give a simple account of the Asian financial crisis[62]). Part of the increase in income inequality that has taken place within countries is attributable - in some cases - to globalization. A recent IMF report demonstrates that the increase in inequality in the developing countries in the period 1981 to 2004 was due entirely to technological change, with globalization making a partially offsetting negative contribution, and that in the developed countries globalization and technological change were equally responsible.[63]

The Impact of Globalization on Economic Growth.



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2. CONCLUSION

As the level of economic integration increases, so does the complexity. This involves a set of numerous regulations, enforcement, and arbitration mechanisms. The complexity comes at a cost that may undermine the competitiveness of the areas under economic integration since it allows for less flexibility for national policies. The devolution of economic integration could occur if the complexity and restrictions it creates are no longer judged to be acceptable by its members

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