**International Trade**

Since ancient times people have strived to expand their trading as far as

technology allowed.

Today, container ships laden with cars and machines and Boeing 747s shuttled with fresh fruit, fresh New Zealand lamb, and French cheeses ply the sea and air routes, carrying billions of dollars worth of goods and services. Trade in goods such as food, raw materials, and manufactured goods is known as visible exports and visible imports. Trade in services such as banking, insurance,and tourism is known as invisible exports or invisible imports. So why do people go to great lengths to trade with those in other nations?

International trade is a form of specialization. Sri Lanka specializes in tea because it has an appropriate climate and soil, and skilled growers and packers. The principle is just the same as individual specialization: Jill specializes in math teaching because she is good at math and at dealing with people, Jack specializes in dentistry because he understands the biology and is deft with his hands. Of course, it is important for both that there is demand for what they are offering.

Economic theory distinguishes between absolute advantage and comparative advantage.

Absolute advantage is the ability of a country to produce a good using fewer resources than another country.

Comparative advantage is a bit harder to understand, but more important for trade. The principle of comparative advantage is a central concept in international trade theory which holds that a country or a region should specialize in the production and export of those goods and services that it can produce relatively more efficiently than other goods and services, and import those goods and services in which it has a comparative disadvantage.

Comparative advantage is the ability of a country to produce a good at a lower opportunity cost than another country. Comparative advantage refers to the relative opportunity costs between countries of producing the same goods. World output and consumption are maximised when each country specialises in producing and trading goods for which it has a comparative advantage.

The majority of economists believe that international trade should be based on comparative advantage and free trade. Free trade is a system which allows certain countries to buy and sell goods from each other without any financial restrictions. In practice, despite the advice of economists, every nation protects its own domestic producers to some degree from foreign competition. Behind these barriers to trade are people whose jobs and income are threatened, so they clamour to the government for protectionism. Protectionism is the government’s use of embargoes, tariffs, quotas, and other restrictions to protect domestic producers from foreign competition.

Embargoes are the strongest limit on trade. An embargo is a law that bars trade with another country. For example, the United States and other nations in the world imposed an arms embargo on Iraq in response to Iraq’s invasion of Kuwait in 1990.

Tariffs are the most popular and visible measures used to discourage trade. A tariff is a tax on an import. Tariffs are also called customs duties. Historically, these provided revenue to governments when taxes were not easily collected from other sources. Modern tariffs are usually imposed for a different reason: to shut out (or add to the price of) certain imports in order to protect home producers from foreign competition. An obvious example is the protectionist policy used by European Union for many agricultural products. The current US tariff code specifies tariffs on nearly 70 percent of U.S. imports. A tariff can be based on weight, volume, or number of units.

Another way to limit foreign competition is to impose a quota. A quota is a limit on the quantity of a good that may be imported in a given time period. For example, the United States might allow 10 million tons of sugar to be imported over a one-year period. Once this quantity is reached, no more sugar can be imported for the year. Quotas can limit imports from all foreign suppliers or from specific countries. Like all barriers to trade, quotas invite other nations to retaliate with more measures to restrict trade. With tariffs, it is impossible to know the quantity that will be imported, because prices might be elastic.

With quotas, governments can set a limit to imports. Yet unlike tariffs, quotas provide no revenue for the government.