[Frequently Asked Questions]

International Trade and International Inequality

Subject:	Business Economics
Course:	B. A. (Hons.), 6th Semester, Undergraduate
Paper No. & Title:	Paper – 641 Elective PaperE2 – Economic Growth and Policy
Unit No. & Title:	Unit – 4 Technological Progress
Lecture No. & Title:	Lecture – 3 International Trade and International Inequality

Frequently Asked Questions

Q1. Why is the demand for primary goods in international market price and exchange rate inelastic?

A1. Countries of the world do not depend much on other countries for their staple food requirement. And, the demand for agricultural goods is limited as these goods have limited industrial applications. Hence, when prices of these goods fall in international market, their demand expands in a lesser proportion than the fall in price.

Even when exchange rate moves in favour of countries exporting primary goods, these countries are not able to increase the export quantities and revenues much.

Q2. What is meant by demand intensity of imports?

A2. Demand intensity of imports means the severity of the need for imported goods. The need of developing countries for certain types of technologies, capital, industrial raw materials, spare parts etc. is very severe. The development process of these countries will severely slow down if they do not obtain such goods.

Q3. What is meant by factor endowments?

A3. Factor endowments mean the magnitude or amount of natural factors which a country is bestowed with.

Q4. Which are the static gains from trade?

A4. The static gains from trade are the gains in the form of, higher incomes, improved terms of trade, employment of unused or unemployed factors, rise in production, increase in foreign exchange reserves etc.

Q5. Which are the dynamic gains from trade?

A5. The dynamic gains from trade pertain to widening of markets, increase in savings and capital formation, enhancement in awareness, transmission of knowledge, education etc.

Q6. Mention one important trade benefit explained in the *staple theory of growth.*

A6. In order to undertake trade, when developing countries explore the use of their unexploited or unused resources or they use their surplus staple resources to produce exportable goods and obtain imports which they need for their development then they gain in trade by giving vent to their unused resources. This is an important benefit of trade pointed out in the ***staple theory of growth***.

Q7. Mention any three effects of trade according to the supply-motored theory of trade-induced growth.

A7. Three important effects explained in the supply-motored theory of trade-induced growth are:

- The 'capital accumulation effect' which occurs when the static gain in the form of increased real income is invested. Thus when investment is made by curtailing consumption in the current period, there is a transfer of real income from present to the future.
- There may be a relatively greater fall in prices of investment goods than in the prices of consumption goods because of two reasons. (a) When more capital is imported the supply of capital goods in the home country grows. (b) When the trade

induced increased incomes are invested in domestic economy, the supply of capital goods increases. This way when the ratio of investment to consumption rises, the rate of growth increases.

- There will be an 'income distribution effect' towards the export-oriented sector. Investments in export-oriented sector will increase and income of factors which are used intensively in the export sector will rise. When exports tend to raise the real income and growth, the society will invest more in this sector.

Q8. What is the nature of exports of developing countries?

A8. Developing countries export more primary goods, or goods produced by their traditional sector. The demand for such goods in the international market is less intense and hence the price and exchange rate elasticity of such exports is lower.

Q9. What is the nature of imports of developing countries?

A9. Developing countries import goods like capital, technology, industrial raw materials, spare parts etc. The import intensity of such goods for developing countries is higher.

Q10. Mention three reasons owing to which trade may increase inequality among countries.

A10. Three reasons owing to which trade may increase inequality among countries are:

1. The quality of factors is poor in countries with high economic and social inequalities and the effectiveness of their production efforts is also low. Trade fails to equalize remuneration of factors thus disproving the factor price equalization theory of trade.

Rather, trade aggravates the economic divide. It will award the efforts of those factors which are skilled and thwart the efforts of those which are unskilled. In other words, the sectors with fair amount of technology and skill sets will be able to export their goods and increase their incomes while the backward sectors will remain poorer.

2. Small and less developed industries of poorer countries will be competed away by foreign industries in trade. Hence, such countries may be impoverished further.

3. Countries which export only primary sector goods may face inelastic demand in the international market and if their demand for industrial imports is high, they may face a balance of payments deficit. Thus trade does not benefit the growth of these countries; rather trade results in external debt. And trade benefits countries which export technology and capital goods and shifts the terms of trade in their favour.