

Introduction to International Trade

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(A concise, organized guide for quick reference)

1. What Is International Trade?

Aspect	Definition
Scope	Exchange of goods, services, and capital across national borders.
Participants	Exporters, importers, multinational firms, governments, and consumers.
Purpose	Satisfy domestic demand, exploit comparative advantage, achieve economies of scale, and access resources not available at home.

2. Why Countries Trade

Reason	Explanation	Example
Comparative Advantage	Nations specialize in producing what they can make relatively more efficiently.	Brazil exports coffee (climate advantage).
Resource Endowment	Access to natural resources, labor, technology, or capital that are scarce domestically.	Japan imports oil, exports electronics.
Economies of Scale	Larger production volumes lower average costs, making exports competitive.	Automobile factories in Germany.
Product Variety & Consumer Preference	Wider selection of goods and services improves welfare.	U.S. consumers enjoy Japanese sushi.
Political & Strategic Goals	Strengthen alliances, secure supply chains, promote development.	EU trade agreements with neighboring countries.

3. Core Concepts & Terminology

Term	Meaning
Export	Sale of domestically produced goods/services to foreign buyers.
Import	Purchase of foreign goods/services for domestic consumption.

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Balance of Trade (BOT)	Exports – Imports of goods. Positive BOT = surplus; negative BOT = deficit.
Current Account	BOT + services, income, and unilateral transfers.
Trade Barrier	Policy that restricts trade (tariffs, quotas, subsidies, standards).
Free Trade	Minimal restrictions; goods move freely across borders.
Protectionism	Use of barriers to shield domestic industries from foreign competition.
Trade Agreement	Formal pact that sets rules for trade between parties (e.g., NAFTA, EU, CPTPP).
Most Favored Nation (MFN)	WTO principle: any advantage given to one member must be extended to all.
Rules of Origin	Criteria determining where a product is “made” for tariff purposes.

4. Theoretical Foundations

Theory	Key Idea	Policy Implication
Absolute Advantage (Adam Smith)	A country can produce a good with fewer resources than another.	Encourage specialization where absolute advantage exists.
Comparative Advantage (David Ricardo)	Even if one country is less efficient in all goods, it can still benefit by specializing in the good with the smallest relative disadvantage.	Promote free trade; remove barriers.
Heckscher-Ohlin (Factor Endowment)	Trade patterns reflect differences in factor abundance (land, labor, capital, technology).	Countries export factor-intensive goods.
New Trade Theory (Krugman)	Scale economies and network effects create intra-industry trade of similar products.	Support policies that foster innovation and market size.
Gravity Model	Bilateral trade volume $\propto$ (Economic size of both countries) / (Distance) ⁻¹ .	Infrastructure and trade facilitation matter.

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Theory

Key Idea

Policy Implication

Strategic Trade Theory

Government can improve national welfare by supporting firms in industries with increasing returns.

Targeted subsidies or export promotion.

5. Trade Policies & Instruments

Instrument	Description	Typical Use
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Tariff	Tax on imported	
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