International Trade and Globalisation

Fifth Edition

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Dedication

For my beautiful grand-daughters Seren and Abi Smith, and Zara Juliette Sabiri, and my delightful grand-son Adam Smith Sabiri.

Also, for their extended family in places all around this little globe of just 8000 miles of rock.

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Preface and acknowledgements

The first edition of this book was entitled '*Understanding International Trade*'. In order to reflect current debate, and in order to cater for the demands of re-structured examination syllabuses, the idea of the 'global' was incorporated into the title of the second edition: '*International Trade and Globalisation*' and further consideration was given to the role of globalisation in modern economic activity.

The basic structure of the book has proved tremendously popular with teachers and students, and so in subsequent editions this has been largely unchanged, apart from essential updating, while additional sections and chapters have been added to take account of new developments, and to put further stress on the phenomenon of globalisation. With respect to trade, if not with respect to power politics and militarism, this phenomenon now appears to be rather less synonymous with 'Americanisation', and must now take account of the remarkable developments taking place elsewhere, in countries like China and India. While the world moves on rapidly, it also moves in great circles. Often we fail to learn from history. For example, when planning the Fourth Edition, it was intended to remove the section in Chapter 11 referring to the economic collapse of the so-called 'Tiger' economies in 1997. However, the Credit Crunch of 2008 and the ensuing recession, according to some politicians and economists came from nowhere, was unprecedented, and totally unexpected. It affected large economies like the USA, medium sized economies like the UK, small countries like Iceland, and even shook the 'Celtic Tiger' of Ireland to its very foundations. So it was decided that this section still had some relevance after all, as a reminder that history has not ended, and one of the worst things we can do is make grand announcements, for example that we have abolished 'boom and bust', when in fact we have not remembered essential lessons from the past. For these reasons this section survives intact into the Fifth Edition.

A brief stroll round the average supermarket is enough to convince even the most casual observer that society is becoming more and more internationalised. Products that just ten or fifteen years ago were unheard of in this country are now commonplace. Items that once were expensive luxuries are now regarded as basic necessities. My mother, who came to Britain from Spain in 1947, remembered a time when olive oil was available over here only from the chemist's shop, for medicinal purposes. Once, after a visit to Spain in the 1970s, my wife and I tried to find some squid in our town's provisions market: the fishmonger looked at us as if we were Martians and pointed to a bucket containing this item which, he reckoned, was only in demand by local sea anglers who used it as bait.

There must be thousands of examples of how the rare, the exotic and the 'foreign' have become routine, familiar and domesticated. Even the seasons appear to have been eliminated, with transport and delivery systems enabling perishables to become available all the year round.

Every November the world's largest container ships edge into Felixstowe harbour, full of goods from China, ready to flood the UK Christmas market. We have been told that our future lies in services: but look at the goods on sale in the High Street or out-of-town retail sheds: clothes, electrical items, gadgets and gizmos. This stuff comes in containers from all over the world. It appears that our appetite for such goods is insatiable, and yet we are deliberately giving up our ability to manufacture them. What is going on?

In the current age of 'austerity', politicians have started to talk about 're-balancing' the economy, away from borrowing, consumption, importing and financial services, and towards saving, investment, exporting and manufacturing. However, there is little everyday evidence of this political wish-listing being translated into practical policy. In the 1970s Prime Minister Edward Heath went to the country and put the question to the electorate, "Who rules: the government or the unions?" At that time the electorate gave no clear answer, and it was left to Heath's successor, Margaret Thatcher, to tame the power of what she saw as her over-mighty subjects, the union barons. Today, politicians are grappling at a global level with rivals to their power and ability to govern. They have to cope with the influence of an amorphous, globalised and opaque grouping known as 'the markets'. And the question now is, "Who rules: democratic governments or unaccountable bankers and credit rating agencies?"

Meanwhile, the word ′globalisation′ has come to be repeated like a mantra, and we are told by people who rarely attempt to explain its meaning (probably because they do not understand it themselves) that we must accept its implications without question. The time is ripe for a re-evaluation of this concept, and this book attempts to argue that far from being a basic fact of life, or an iron law of nature, globalisation is a contestable concept, whose time has come to be contested.

The very nature of our chosen subject, economics, is both international and global, and yet many textbooks discuss international trade and globalisation as afterthoughts, and some even ignore these issue areas altogether.

Quite rightly, international trade is a core topic area in 'A' Level Economics. It is an essential part of the International Baccalaureate programme, and also figures largely in Business Studies syllabuses and in higher education Economics, Business degree programmes and MBAs. Recent and forthcoming syllabus developments confirm this central position. This booklet aims to assist teachers and lecturers to reinforce the teaching and learning of this topic area by covering the main issues in a way which is up-to-date and relevant. It is hoped that it will help the reader to improve understanding of the main complexities, make linkages between international trade, globalisation and other parts of the framework of economics, approach core examination topics with confidence, and follow current debate with a critical awareness.

Although the main purpose of this book is to examine international trade and globalisation from the UK perspective, a wholly anglo-centric point of view would be totally inconsistent with the ′internationalism′ which modern economists must imbibe and adopt as second nature. Some of the chapters therefore attempt to inject a little empathy for wider perspectives.

Economics is at once exasperating and fascinating due to its constant change and evolution. For this book, my main sources of recent statistics for the international trading position of the UK have been the printed publications of the Office of National Statistics. In the UK the ′open government′ website is becoming increasingly useful as a source of up-to-date information. Eurostat is the main source of EU statistics. The World Bank's World Development Report and the United Nations Development Programme's Human Development Report (both annual publications) are also essential sources for students and teachers. Websites such as nationmaster.com have become invaluable for international comparisons. Every effort has been made to acknowledge sources, but if any have been overlooked or wrongly attributed this will be rectified at the earliest opportunity.

What makes the teaching of economics so frustrating for some, and such a challenge for others, is that educationists in this field have to be always learning, thinking, and modifying their ideas, and I have derived great benefit from debates and discussions with colleagues and friends at home and abroad which have helped select themes for this book. I particularly wish to thank Gareth Rees, United World College of the Atlantic, and Peter Nicols, University of New South Wales, for previous collaborations which have helped to inform and underpin important parts of my current work. I have learned a lot about relationships between the global and local from Professor Sean Loughlin of Cardiff University and Dr. Jörg Mathias of the University of Aston, and their expert influence has helped greatly in my own struggle to understand some important processes and paradigms.

An advantage of the ′booklet′ format in which this work appears is that it is possible to up-date regularly, keeping the format and structure as constant as possible for the benefit of long-term users, but revising sections of the content in line with contemporary facts and issues. This is especially desirable in the field of international trade and globalisation where traditional, heavy textbooks are habitually out-dated before their ink is even dry. For the benefit of future editions the author would be very pleased to receive constructive criticism and suggestions from users, whether they be teachers, lecturers, examiners or students on any items of controversy, not least some of the predictions contained in the final chapter. Having mentioned revised editions I wish to thank Nigel Tree and his team at Anforme for their continued commitment to this publication. Special thanks are due to Peter Maunder, recently retired from the University of Loughborough, for his perceptive editing.

None of the above mentioned persons or institutions should be associated with any errors or omissions. These are all my own responsibility.

C.E.S.

Chapter 1

What is international trade?

UK plc

Globalisation is closely associated with what is known as 'free trade'. It is often said that the UK is a 'trading nation'. It is regarded as a fact of life that **open** economies (those which trade freely with the outside world) are more successful than **closed** economies (those which protect themselves against international competition). Politicians have been heard to say that countries must 'export or die'. All the world's major economies belong to an organisation called the 'World Trade Organisation', which exists in order to foster international trade. What is **international trade** and why is it important?

International trade involves the **exchange** of goods and services between one country and another. Sometimes there is a direct exchange of goods for goods, a system known as **barter**, but in modern economies the 'exchange' usually takes place indirectly, with items being sold for a money payment and the money then being exchanged for items which are bought. Where countries have different currencies, it is therefore important for these currencies themselves to be tradable (or 'convertible'), and to have a price against other currencies. This 'price' is known as an **exchange rate**, and has an important influence on international trade.

Although we talk of 'international' trade, it is important to realise that trade does not really take place between 'nations' as such. It actually takes place between **economic agents** or decision makers within nations, such as individuals, families, or businesses. Some items (certain pieces of defence equipment, for example) might be traded between governments acting as economic agents; and the government might take a high profile in encouraging and regulating trade; but on the whole most international trade takes place not between governments but private-sector decision makers who just happen to be located within different nations. So, for example, when a British family decides to buy a Japanese car, or insures the car with a French insurance company, or takes the car on a holiday in Spain, these decisions result in international trade. We might not tend to think of a foreign holiday as resulting in international trade, but what happens when a British family goes to Spain is that they purchase travel and hotel services from Spanish companies. In effect, a tourism service has been exported from Spain and imported to the UK.

Where trade is in a physical item (such as raw materials or manufactured products) it is classed as **visible** trade; where there is trade in services (such as banking, tourism and insurance) we refer to **invisible** trade.

Table 1.1: Contribution to UK GDP of industrial sectors (2008)

Agriculture	1%
Manufacturing	23%
Services	76%

Source: ONS

The UK used to be famous for its visible exports, particularly its manufactured products. The UK was the first country to go through an industrial revolution, and in the nineteenth century became known as the 'workshop of the world'. Today, the relative size of the UK's manufacturing export sector has declined.

After the Second World War the UK experienced economic growth and a general rise in living standards which were both more rapid than anything experienced by previous generations. At the same time, however, there was a **relative** decline in economic performance when compared with other western countries, and some countries around the Pacific rim also.

In 1850 the British economy was the largest in the world, measured by GDP, and Britain produced 41% of the world's manufactured exports. By the year 2000 this had fallen to 5%. However, manufacturers

continue to make a sizeable contribution to an economy that is heavily involved in international trade, providing 60% of the UK's exports. But the economic influence of the manufacturing sector is slowly dwindling. Just after World War II, for example, manufacturing accounted for almost 40% of the UK economy. The sector also employs considerably less people than it used it. At the end of the 1970s, it employed just under a third of the total UK workforce. And in the last year alone, an estimated 150,000 manufacturing jobs were lost.

As it gradually came on stream during the 1970s, many saw North Sea oil as a major national resource, and hoped that exports of this commodity would restore the UK's international position. Yet by the early 1990s the UK balance of payments had begun to show record deficits – and North Sea oil was actually partly to blame. Oil exports increased the value of the pound against other currencies, which in turn put manufacturing exporters under pressure by increasing their export prices.

With the exhaustion of the North Sea oil field, in the late 1990s and 2000s the financial industry was seen by some as a future motor of economic growth and employment in the UK. Ironically, monetary policy replaced oil exports as a handicap on British manufacturing exporters. Many experts repeatedly claimed that interest rates could have been lowered without necessarily causing inflation, and that as a result the pound was over-valued against other currencies.

Because of the strength of its service sector, and particularly because of the large annual flow of financial assets through the City of London, the UK registers as the fourth to sixth largest economy in the world (depending on the measurement methods used), and this type of statistic is often quoted by politicians. However, in terms of Gross Domestic Product (national income) per head, which is usually regarded as an important indicator of living standards, the UK is lower down the world league tables. It should also be noted that GDP per head is a raw average, and that most economic measures indicate that income distribution within the UK has become less equal over the last decade.

Table 1.2: UK's national income world rankings

	GDP	GDP per head
1946	3	3
1966	3	18
1986	6	25
2006	6	13

Sources: OECD; *British Historical Statistics*, Macmillan; *Human Development Report 2003*, www.undp.org; nationmaster.com

Some commentators have claimed that the UK must become an enterprise economy. Certain politicians are very obviously a great admirer of the 'enterprising' attitudes claimed by the private sector. An essential requirement of any enterprise is that it should be able to 'balance' its books. In later chapters we consider the extent to which 'UK plc' can be considered a successful enterprise if it cannot balance its international payments. Does this balancing act really matter? We consider this question in Chapter 3.

What goods and services does the UK trade in?

A familiar pattern has long been recognised by economists: as an economy develops its primary sector (agriculture, extraction) tends to get smaller as a proportion of total national output and employment, while the secondary sector (manufacture, construction) gets larger. Then gradually the tertiary sector (services) becomes the largest of all. This pattern can be recognised in the UK's international trade profile, and is also reflected in the fact that Britain has a trade gap (it spends more on imports than it earns from exports).

Some people believe that the UK is now a 'service centre' rather than a 'workshop', and while it is certainly true that a deficit in visible trade has often been compensated for by a surplus on invisibles, it can be argued that the UK's manufacturing decline has been accompanied by a fall in its position in world economic league tables in general, suggesting that modern economies need to achieve good performance in a **balance** of sectors in order to achieve high living standards. There is certainly a high demand for services in the UK, but there is also a high demand for goods. To many, it seems defeatist to accept that

Table 1.3: UK trade in goods and services, credits less debits (£m)

Year	Goods	Services	Total goods and services	Current balance (includes investment income and other current transfers)	Current balance as % of GDP
1954	-210	115	-95	160	0.9
1979	-3326	4573	1247	-1002	-0.5
2008	-92876	48878	-43998	-24493	-1.7

Source: ONS, *Annual Abstract of Statistics*, 2009

those goods should all be imported, and it appears to suggest that the destiny for many of our workers is to be consigned to relatively low-wage jobs in the retail trade, where customers purchase products where most of the real value was added in other parts of the world.

Is manufacturing unimportant, and does our future lie in services? Perhaps what is really important is the 'value added' in an economy. It is possible to have low-grade manufacturing, where workers merely assemble components designed elsewhere for products invented and ultimately marketed elsewhere. It is far better to be involved in the high 'value-added' activities of invention, design and marketing. Similarly, many jobs in the service sector are of low quality, involving unskilled part-time work, often on short term contracts at or near the minimum wage. 'Services' cover a multitude of sins, and if our future is in this sector, then we should aim to be involved in high value-added activities. Designing computer systems involves more value-added than selling computers from a high street store.

During the 1990s a worrying trend emerged, whereby manufacturers in the UK closed their British manufacturing facilities and transferred them to low-wage countries. Loss making toy manufacturers, such as the world famous Hornby Trains, became profitable once more by making their mass-produced models in China instead of in Margate, Kent. The Dyson Company, famous for its 'bagless' vacuum cleaners and synonymous with British entrepreneurship, inventive flair and imaginative design, gravely disappointed many of its admirers by 'exporting jobs' to Asia from its base in Malmesbury, Wiltshire.

What is really important is the 'value added' in an economy.

The response of many politicians was to say, in effect: "Never mind, our workers are flexible and can re-train for jobs in service industries such as computing and ICT (information and communication technology)." This position has become seriously undermined in the early years of the 21st Century by another worrying trend: large institutions such as British Telecom, HSBC and Lloyds TSB have been moving call centres and computer services to countries such as India, where English language and ICT skills are well developed, but far less well financially rewarded than in the UK.

Who does the UK trade with?

It is sometimes claimed that the UK has 'more in common' with the economies of the USA and Canada than with those of Europe. However, it can be argued that is an impression rather than a reality. The impression is created by the influence of the 'monetary' economy rather than the 'real' economy. As an important financial centre, London is an important staging post for monetary movements, most of which are in dollars. This means that UK stock and monetary markets are very much 'in phase' with north American business cycles. However, while the world of monetary movements is important, it is not as vital to the everyday lives of average citizens as the **real** economy of employment, output, and spending. We therefore should **not** conclude that the UK's future lies in some sort of north Atlantic trading association rather than in the European Union (EU). Although this is an idea that has been promoted by some sections of the UK press, most economists would regard the idea as unrealistic. In terms of the real economy the trend is clearly towards ever closer links with the EU.

Table 1.4: Main trading partners of the UK, 2007

	% volume of exports		**% volume of imports**
USA	15	Germany	14
Germany	11	USA	9
France	10	China	7
Ireland	7	Netherlands	7
Netherlands	6	France	7
Belgium	6	Belgium	5
Spain	5	Norway	5
Italy	4	Italy	4

Source: ONS

Taking the value of imports and exports together, well over 50% of UK trade is now with other members of the EU, with the rest of its trade divided more or less equally between the rest of Europe, the North Atlantic Free Trade Area, and the rest of the world. The proportion of trade with the rest of the EU is gradually increasing. At the same time, industrial structures between the UK and the continent are becoming increasingly integrated; for example mergers between British and German car manufacturers, British retail stores trading in continental city centres, and Spanish companies taking control of British companies including banks and airports.

International trade and finance are often confused as being synonymous with globalization. Indeed, trade and international finance have contributed to globalization but they are not the same. Globalization is a process that widens, deepens and speeds-up interconnectedness between people, institutions, markets and nations. Trade and finance are two arteries through which the process of globalization flows. There are many ways to conceptualize globalization. Just whose iphone is IT? The iPhone is a global product. Another relationship between globalization and international trade can be seen from the ease of communication across borders. International communication is much easier now thanks to the improvement in technology and the influence of globalization. The ease of communication facilitates international trade by making it much easier for business people to communicate with each other through the use of communication tools like the Internet, phones and letters. As such, a company in Australia can fax an order to a company in Japan for a number of photocopying machines for its corporate headquarters Trade globalization is a type of economic globalization and a measure (economic indicator) of economic integration. On a national scale, it loosely represents the proportion of all production that crosses the boundaries of a country, as well as the number of jobs in that country dependent upon external trade. On a global scale, it represents the proportion of all world production that is used for imports and exports between countries. Public Concerns about Trade. Trade and International Labor Standards. Trade and Environmental Standards. Local Perspectives.Â The tremendous growth of international trade over the past several decades has been both a primary cause and effect of globalization. The volume of world trade increased twenty-seven fold from $296 billion in 1950 to $8 trillion in 2005 (WTO, 2007). In recent years world trade has declined in volume and was down in 2012 and is expected to remain sluggish through 2013. This is a result of the struggling economies of Europe and doubt over the Euro (WTO, 2013). The continued decline of world trade was evidenced by a decrease of 0.3 percent in May, with forecasters cutting their prediction for glo...