Interactions within the Global Economy

by Sophia

WHAT'S COVERED

We've already established that the world is becoming globalized. In a globalized world, it's important for businesses to understand the rules of the road. This tutorial will cover interactions within the global economy, providing an overview of trade restrictions and global markets. Our discussion breaks down as follows:

1. International Trade

One of the rules of the road for international trade is a tariff. A **tariff** is defined as any import or export tax that is placed on a group of products. International trade has increased in importance, and a lot of other nations are getting involved. As a matter of fact, you can see a globalized effort on the part of countries to get involved in international trade.

Tariffs are put in place to protect certain industries within a country. They can be revenue tariffs or protective tariffs.

> EXAMPLE The tariff or tax on sugar imports in the United States helps to protect the sugar industry here.

Tariffs also help prevent practices like dumping. Dumping is when a country offloads a lot of product onto another country or the international market for less than it costs to actually manufacture that product at home.

> EXAMPLE In 2009, the U.S. Department of Commerce ruled that steel from China was guilty of dumping. They were producing really cheap steel and selling it in the United States for less than it cost them to manufacture it at home. This had a destabilizing effect on the economy--the steel industry--here in the United States.

Another important concept to cover are **quotas**, which, in international trade, are limiting the amount of a good that can be traded to a specific amount or specific value. An **embargo** is a trade restriction that stops trade with a specific country.

> EXAMPLE A quota might dictate that you're only allowed to import 100 million tons of sugar every year into the U.S. An embargo would be restricting any trade with Iran at all.

Another method that nations can use to help limit trade or create embargoes or quotas would be foreign exchange controls. Foreign exchange controls are restricting the use or import of currency within a nation. This is achieved by fixing a particular exchange rate within a country. They can ban the currency altogether from entering the country, or they can restrict the amount that can be used or the amount that can be possessed by its citizens.

↪ EXAMPLE If the United States suddenly didn't want to accept pesos anymore, they would ban the use and import of that particular currency completely.

TERMS TO KNOW

Tariff
Any imports and exports tax that is placed on a group of products.

Quota
Limiting the amount of a good being traded to a specific amount or value.

Embargo
A trade restriction that stops trade with a specific country.

---

2. Trade Restrictions

Trade restrictions are put in place to equalize the nation's balance sheet--that balance of trade we discussed in an earlier tutorial. Trade restrictions can also help protect new or weak industries, like the sugar industry mentioned previously. It can be done for national security reasons or to protect the health of citizens.

↪ EXAMPLE If we know that a certain food product coming from a particular country is contaminated, we can impose a trade restriction to keep that particular food product out.

They are also used politically as a means of retaliation between nations. For instance, an embargo may be imposed to restrict the flow of material that can be used to produce nuclear power plants in Iran.

Lastly, countries can set up trade restrictions in order to protect new jobs or new, weak industries within that country.

TERM TO KNOW

Trade Restrictions
Artificially limiting the business conducted between nations.

---

3. Trade Agreements

Trade agreements are a trade treaty between nations which sets rates of tax and limit on any limit on restrictions. What is that, exactly? Basically, it's an agreement between two countries that helps to encourage trade between those two nations. There are several trade agreements and trade alliances that exist, and before you enter into a particular international market, you would need to consider these particular trade alliances.

Some examples of these trade agreements are:

- North American Free Trade Agreement (NAFTA): Between the United States, Mexico, and Canada.
- European Union (EU): Includes all of the countries within Europe, such as France, Germany, Belgium, Italy, and Spain, to name a few.
- Association of Southeast Asian Nations (ASEAN): Covers nations around the South Pacific.
- World Trade Organization (WTO): Represented by countries worldwide to discuss trade policy.

Note, more trade alliances exist, but this is simply an introduction to get you started.

TERM TO KNOW

Trade Agreement
A trade treaty between nations which sets rates of tax and any limit on restrictions.

---

4. Sourcing

Sourcing is determining the product location of goods based on external and internal variables. Companies will source different products around the world, depending on these factors. In fact, businesses often have whole departments or dedicated consultants that will focus solely on where to manufacture different products and where to source the resources needed to manufacture them. This can change from year to year.

EXAMPLE If a tariff or trade restriction is put in place between the U.S. and another country where you're sourcing the materials that you need--for instance, Bangladesh with clothing--you may need to look in another place to get the best deal and best quality for your customers for that particular item.

EXAMPLE If one of the trade alliances, like the European Union, decided to embargo, restrict, or open trade between that nation and the U.S. again, you would need to take this into consideration to make sure that you were maintaining the best source of your products every year, without interruption.

TERM TO KNOW

Sourcing
Determining the production location of goods based on external and internal variables of the business.

SUMMARY

Today we learned about **international trade**. We learned about certain **trade restrictions**, such as tariffs, quotas, and embargoes, and why these things are put into place. We also learned about **trade agreements** and trade alliances, like NAFTA and the European Union.

Lastly, we learned about **sourcing** and how important it is to keep up with the different international trade variables around the world. We also covered trade restrictions and trade agreements to ensure that the products you need to produce or sell in your business are sourced correctly and that you don't have an interruption in that resource.

Good luck!

Source: adapted from sophia instructor james howard

TERMS TO KNOW

Embargo
A trade restriction that stops trade with a specific country.

Quota
Limiting the amount of a good being traded to a specific amount or value.

Sourcing
Determining the production location of goods based on external and internal variables of the business.

Tariff
Any imports and exports tax that is placed on a group of products.

Trade Agreement
A trade treaty between nations which sets rates of tax and any limit on restrictions.

Trade Restrictions
Artificially limiting the business conducted between nations.