TRADE

Trade means exchange of goods. It implies exchange of goods between persons. It aims at achieving increased production through division of labour.

There is, however, a number of things which make a difference between foreign trade and domestic trade and necessitate a separate theory of international trade.

They are as under:

(i) Immobility of Factors of Production:
Labour and capital do not move freely from one country to another as they do within the same country. "Man", declared Adam Smith, "is, of all forms of luggage, the most difficult to transport". Much more so when a foreign frontier has to be crossed. Hence differences in the cost of production cannot be removed by moving men and money, the result is the movement of goods.

On the contrary, between regions within the same political boundaries, people distribute themselves more or less according to opportunities. Real wages and standard of living tend to seek a common level, though they are not wholly uniform. As between nations, however, these differences continue to persist for wages and check population movements. Capital also does not move freely from- one country to another. Capital is notoriously shy.

(ii) Different Currencies:
Each country has a different currency. India for instance, has the rupee, the U.S.A. the dollar, Germany the mark, Italy the lira, Spain the peso, Japan the yen, and so on. Hence, buying and selling between nations give rise to complications absent in internal trade.

(iii) Restrictions on Trade:
Trade between different countries is not free. Very often there are restrictions imposed by custom duties, exchange restrictions, fixed quotas or other tariff barriers. For example, our own country has imposed heavy duties on import of motor cars, wines and liquors and other luxury goods.

(iv) Ignorance:
Knowledge of other countries cannot be as exact and full as of one's own country. Differences in culture, language and religion stand in the way of free communication between different countries. On the other hand, within the borders of a country, labour and capital freely move about. These factors, too, make internal trade different from international trade.

(v) Transport and Insurance Costs:
Then costs of transport and insurance also check- free international trade. The greater the distance between the two countries, the greater are these costs. Wars increase them still more.

DIFFERENCE BETWEEN INTERNAL & INTERNATIONAL TRADE

Internal Trade	International Trade
Definition	
Internal trade is trade that involves buying and selling taking place between two parties which are located within the political and geographical boundaries of a country	International trade is referred to as a trade that involves buying and selling of goods between two individuals or businesses located in two different countries or it can be trade between two different countries
Currency exchange	
There is no exchange of currency as trade takes place within the boundaries of the nation	Exchange of currency is there between the two countries/individuals/businesses involved in the trade
Trade Restrictions	
No trade restrictions for internal trade	International trade has different restrictions as the two countries involved in trade have different policies with regards to trade
Transportation Cost	
Transportation cost is less when trade is taking place within the borders of a country	Comparatively higher transportation costs as goods need to be transported across the world
Goods traded	
Only those goods and services are traded that are available in the country	Helps countries to trade goods that are produced in surplus or purchase goods that are scarcely available
Foreign reserve	
Does not generate any foreign reserve	International trade generates foreign reserves for the two trading countries

International Trade

International trade theories are simply different theories to explain international trade. Trade is the concept of exchanging goods and services between two people or entities. *International trade* is then the concept of this exchange between people or entities in two different countries.

People or entities trade because they believe that they benefit from the exchange. They may need or want the goods or services. While at the surface, this many sound very simple, there is a great deal of theory, policy, and business strategy that constitutes international trade.

DIFFERENT INTERNATIONAL TRADE THEORIES

"Around 5,200 years ago, Uruk, in southern Mesopotamia, was probably the first city the world had ever seen, housing more than 50,000 people within its six miles of wall. Uruk, its agriculture made prosperous by sophisticated irrigation canals, was home to the first class of middlemen, trade intermediaries…A cooperative trade network…set the pattern that would endure for the next 6,000 years."Matt Ridley, "Humans: Why They Triumphed

To better understand how modern global trade has evolved, it's important to understand how countries traded with one another historically. Over time, economists have developed theories to explain the mechanisms of global trade. The main historical theories are called *classical* and are from the perspective of a country, or country-based. By the mid-twentieth century, the theories began to shift to explain trade from a firm, rather than a country, perspective. These theories are referred to as *modern* and are firm-based or company-based. Both of these categories, classical and modern, consist of several international theories.

CLASSICAL OR COUNTRY-BASED TRADE THEORIES

Mercantilism

Developed in the sixteenth century, mercantilism was one of the earliest efforts to develop an economic theory. This theory stated that a country's wealth was determined by the amount of its gold and silver holdings. In it's simplest sense, mercantilists believed that a country should increase its holdings of gold and silver by promoting exports and discouraging imports. In other words, if people in other countries buy more from you (exports) than they sell to you (imports), then they have to pay you the difference in gold and silver. The objective of each country was to have a trade surplus, or a situation where the value of exports are greater than the value of imports, and to avoid a trade deficit, or a situation where the value of imports is greater than the value of exports.

A closer look at world history from the 1500s to the late 1800s helps explain why mercantilism flourished. The 1500s marked the rise of new nation-states, whose rulers wanted to strengthen their nations by building larger armies and national institutions. By increasing exports and trade, these rulers were able to amass more gold and wealth for their countries. One way that many of these new nations promoted exports was to impose restrictions on imports. This strategy is called protectionism and is still used today.

Nations expanded their wealth by using their colonies around the world in an effort to control more trade and amass more riches. The British colonial empire was one of the more successful examples; it sought to increase its wealth by using raw materials from places ranging from what are now the Americas and India. France, the Netherlands, Portugal, and Spain were also successful in building large colonial empires that generated extensive wealth for their governing nations.

Although mercantilism is one of the oldest trade theories, it remains part of modern thinking. Countries such as Japan, China, Singapore, Taiwan, and even Germany still favor exports and discourage imports through a form of neo-mercantilism in which the countries promote a combination of protectionist policies and restrictions and domestic-industry subsidies. Nearly every country, at one point or another, has implemented some form of protectionist policy to guard key industries in its economy. While export-oriented companies usually support protectionist policies that favor their industries or firms, other companies and consumers are hurt by protectionism. Taxpayers pay for government subsidies of select exports in the form of higher taxes. Import restrictions lead to higher prices for consumers, who pay more for foreign-made goods or services. Free-trade advocates highlight how free trade benefits all members of the global community, while mercantilism's protectionist policies only benefit select industries, at the expense of both consumers and other companies, within and outside of the industry.

Absolute Advantage

In 1776, Adam Smith questioned the leading mercantile theory of the time in *The Wealth of Nations*.Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations* (London: W. Strahan and T. Cadell, 1776). Recent versions have been edited by scholars and economists. Smith offered a new trade theory called absolute advantage, which focused on the ability of a country to produce a good more efficiently than another nation. Smith reasoned that trade between countries shouldn't be regulated or restricted by government policy or intervention. He stated that trade should flow naturally according to market forces. In a hypothetical two-country world, if Country A could produce a good cheaper or faster (or both) than Country B, then Country A had the advantage and could focus on specializing on producing that good. Similarly, if Country B was better at producing another good, it could focus on specialization as well. By specialization, countries would generate efficiencies, because their labor force would become more skilled by doing the same tasks. Production would also become more efficient, because there would be an incentive to create faster and better production methods to increase the specialization.

Smith's theory reasoned that with increased efficiencies, people in both countries would benefit and trade should be encouraged. His theory stated that a nation's wealth shouldn't be judged by how much gold and silver it had but rather by the living standards of its people.

Comparative Advantage

The challenge to the absolute advantage theory was that some countries may be better at producing both goods and, therefore, have an advantage in *many* areas. In contrast, another country may not have *any* useful absolute advantages. To answer this challenge, David Ricardo, an English economist, introduced the theory of comparative advantage in 1817. Ricardo reasoned that even if Country A had the absolute advantage in the production of *both* products, specialization and trade could still occur between two countries.

Comparative advantage occurs when a country cannot produce a product more efficiently than the other country; however, it *can* produce that product better and more efficiently than it does other goods. The difference between these two theories is subtle. Comparative advantage focuses on the relative productivity differences, whereas absolute advantage looks at the absolute productivity.

Let's look at a simplified hypothetical example to illustrate the subtle difference between these principles. Miranda is a Wall Street lawyer who charges $500 per hour for her legal services. It turns out that Miranda can also type faster than the administrative assistants in her office, who are paid $40 per hour. Even though Miranda clearly has the absolute advantage in both skill sets, should she do both jobs? No. For every hour Miranda decides to type instead of do legal work, she would be giving up $460 in income. Her productivity and income will be highest if she specializes in the higher-paid legal services and hires the most qualified administrative assistant, who can type fast, although a little slower than Miranda. By having both Miranda and her assistant concentrate on their respective tasks, their overall productivity as a team is higher. This is comparative advantage. A person or a country will specialize in doing what they do *relatively* better. In reality, the world economy is more complex and consists of more than two countries and products. Barriers to trade may exist, and goods must be transported, stored, and distributed. However, this simplistic example demonstrates the basis of the comparative advantage theory.

Heckscher-Ohlin Theory (Factor Proportions Theory)

The theories of Smith and Ricardo didn't help countries determine which products would give a country an advantage. Both theories assumed that free and open markets would lead countries and producers to determine which goods they could produce more efficiently. In the early 1900s, two Swedish economists, Eli Heckscher and Bertil Ohlin, focused their attention on how a country could gain comparative advantage by producing products that utilized factors that were in abundance in the country. Their theory is based on a country's production factors—land, labor, and capital, which

provide the funds for investment in plants and equipment. They determined that the cost of any factor or resource was a function of supply and demand. Factors that were in great supply relative to demand would be cheaper; factors in great demand relative to supply would be more expensive. Their theory, also called the factor proportions theory, stated that countries would produce and export goods that required resources or factors that were in great supply and, therefore, cheaper production factors. In contrast, countries would import goods that required resources that were in short supply, but higher demand.

For example, China and India are home to cheap, large pools of labor. Hence these countries have become the optimal locations for labor-intensive industries like textiles and garments.

Leontief Paradox

In the early 1950s, Russian-born American economist Wassily W. Leontief studied the US economy closely and noted that the United States was abundant in capital and, therefore, should export more capital-intensive goods. However, his research using actual data showed the opposite: the United States was importing more capital-intensive goods. According to the factor proportions theory, the United States should have been importing labor-intensive goods, but instead it was actually exporting them. His analysis became known as the Leontief Paradox because it was the reverse of what was expected by the factor proportions theory. In subsequent years, economists have noted historically at that point in time, labor in the United States was both available in steady supply and more productive than in many other countries; hence it made sense to export labor-intensive goods. Over the decades, many economists have used theories and data to explain and minimize the impact of the paradox. However, what remains clear is that international trade is complex and is impacted by numerous and often-changing factors. Trade cannot be explained neatly by one single theory, and more importantly, our understanding of international trade theories continues to evolve.

MODERN OR FIRM-BASED TRADE THEORIES

In contrast to classical, country-based trade theories, the category of modern, firm-based theories emerged after World War II and was developed in large part by business school professors, not economists. The firm-based theories evolved with the growth of the multinational company (MNC). The country-based theories couldn't adequately address the expansion of either MNCs or intraindustry trade, which refers to trade between two countries of goods produced in the same industry. For example, Japan exports Toyota vehicles to Germany and imports Mercedes-Benz automobiles from Germany.

Unlike the country-based theories, firm-based theories incorporate other product and service factors, including brand and customer loyalty, technology, and quality, into the understanding of trade flows.

Country Similarity Theory

Swedish economist Steffan Linder developed the country similarity theory in 1961, as he tried to explain the concept of intraindustry trade. Linder's theory proposed that consumers in countries that are in the same or similar stage of development would have similar preferences. In this firm-based theory, Linder suggested that companies first produce for domestic consumption. When they explore exporting, the companies often find that markets that look similar to their domestic one, in terms of customer preferences, offer the most potential for success. Linder's country similarity theory then states that most trade in manufactured goods will be between countries with similar per capita incomes, and intraindustry trade will be common. This theory is often most useful in understanding trade in goods where brand names and product reputations are important factors in the buyers' decision-making and purchasing processes.

Product Life Cycle Theory

Raymond Vernon, a Harvard Business School professor, developed the product life cycle theory in the 1960s. The theory, originating in the field of marketing, stated that a product life cycle has three distinct stages: (1) new product, (2) maturing product, and (3) standardized product. The theory assumed that production of the new product will occur completely in the home country of its innovation. In the 1960s this was a useful theory to explain the manufacturing success of the United States. US manufacturing was the globally dominant producer in many industries after World War II.

It has also been used to describe how the personal computer (PC) went through its product cycle. The PC was a new product in the 1970s and developed into a mature product during the 1980s and 1990s. Today, the PC is in the standardized product stage, and the majority of manufacturing and production process is done in low-cost countries in Asia and Mexico.

The product life cycle theory has been less able to explain current trade patterns where innovation and manufacturing occur around the world. For example, global companies even conduct research and development in developing markets where highly skilled labor and facilities are usually cheaper. Even though research and development is typically associated with the first or new product stage and therefore completed in the home country, these developing or emerging-market countries, such as India and China, offer both highly skilled labor and new research facilities at a substantial cost advantage for global firms.

Global Strategic Rivalry Theory

Global strategic rivalry theory emerged in the 1980s and was based on the work of economists Paul Krugman and Kelvin Lancaster. Their theory focused on MNCs and their efforts to gain a competitive advantage against other global firms in their industry. Firms will encounter global competition in their industries and in order to prosper, they must develop competitive advantages. The critical ways that firms can obtain a

sustainable competitive advantage are called the barriers to entry for that industry. The barriers to entry refer to the obstacles a new firm may face when trying to enter into an industry or new market. The barriers to entry that corporations may seek to optimize include:

- research and development,
- the ownership of intellectual property rights,
- economies of scale,
- unique business processes or methods as well as extensive experience in the industry, and
- the control of resources or favorable access to raw materials.

Porter's National Competitive Advantage Theory

In the continuing evolution of international trade theories, Michael Porter of Harvard Business School developed a new model to explain national competitive advantage in 1990. Porter's theory stated that a nation's competitiveness in an industry depends on the capacity of the industry to innovate and upgrade. His theory focused on explaining why some nations are more competitive in certain industries. To explain his theory, Porter identified four determinants that he linked together. The four determinants are (1) local market resources and capabilities, (2) local market demand conditions, (3) local suppliers and complementary industries, and (4) local firm characteristics.

1. **Local market resources and capabilities (factor conditions).** Porter recognized the value of the factor proportions theory, which considers a nation's resources (e.g., natural resources and available labor) as key factors in determining what products a country will import or export. Porter added to these basic factors a new list of advanced factors, which he defined as skilled labor, investments in education, technology, and infrastructure. He perceived these advanced factors as providing a country with a sustainable competitive advantage.
2. **Local market demand conditions.** Porter believed that a sophisticated home market is critical to ensuring ongoing innovation, thereby creating a sustainable competitive advantage. Companies whose domestic markets are sophisticated, trendsetting, and demanding forces continuous innovation and the development of new products and technologies. Many sources credit the demanding US consumer with forcing US software companies to continuously innovate, thus creating a sustainable competitive advantage in software products and services.
3. **Local suppliers and complementary industries.** To remain competitive, large global firms benefit from having strong, efficient supporting and related industries to provide the inputs required by the industry. Certain industries cluster geographically, which provides efficiencies and productivity.
4. **Local firm characteristics.** Local firm characteristics include firm strategy, industry structure, and industry rivalry. Local strategy affects a firm's competitiveness. A healthy level of rivalry between local firms will spur innovation and competitiveness.

In addition to the four determinants of the diamond, Porter also noted that government and chance play a part in the national competitiveness of industries. Governments can, by their actions and policies, increase the competitiveness of firms and occasionally entire industries.

Porter's theory, along with the other modern, firm-based theories, offers an interesting interpretation of international trade trends. Nevertheless, they remain relatively new and minimally tested theories.

INDIA'S INTERNAL TRADE

Characteristics

1. Internal trade is carried on within the boundaries of one country.
2. In this form of trade, goods are carried on from one place to another place through railways and roadways.
3. In this form of trade, payment is made or received in local currency.
4. In internal trade wide choice of goods are available.
5. In this type of trade, payments can be made in cash, cheque and draft.
6. In this form of trade generally license need not be obtained, whereas it is a must in foreign trade.
7. In this type of trade, local rules and regulations have to be followed.

Problems

1. Not enough work for expanding population.
2. Nearly all usable land was already in production.
3. Trade was narrowly focused on luxuries.
4. Began to experience massive famines and endemic poverty.

TRADE OF UTTAR PRADESH

Uttar Pradesh is the most populous state in India with a population of nearly **200 million** people. Uttar Pradesh shares its borders with Nepal on the north, the Indian states of Uttarakhand and Himachal Pradesh on the northwest, Haryana, Delhi and Rajasthan on the west, Madhya Pradesh on the south, Chhattisgarh and Jharkhand on the southeast and Bihar on the east.

The Gross State Domestic Product (GSDP) of Uttar Pradesh grew at a CAGR of around 8.43% between 2015-16 and 2020-21 to reach Rs. 17.06 trillion (US$ 234.96 billion). The Net State Domestic Product (NSDP) grew at a CAGR of around 8.42% between 2015-16 and 2020-21 to reach Rs. 15.12 trillion (US$ 208.34 billion).

TOURISM Uttar Pradesh is a favored tourist destination in India with Taj Mahal, one of the eight Wonders of the World, located in Agra. In 2019, domestic tourist arrivals in the state reached 535.8 million. Foreign tourist arrivals crossed over 4.74 million.

POWER GENERATION As of April 2021, Uttar Pradesh had an installed power generation capacity of 28,001.95 MW—6,242.20 MW (state utilities), 13,562.74 MW (private utilities) and 8,197.01 MW (central utilities). Thermal power contributed 20,303.33 MW to the state's total installed power generation capacity, followed by 3,424.03 MW (hydropower), 289.48 MW (nuclear power) and 3,985.11 MW (renewable power).

FOOD GRAINS Uttar Pradesh is the largest producer of food grains in India and accounted for about 17.83% share in the country's total food grain output in 2016-17. Food grain production in the state stood at 49,903.1 thousand tonnes in 2016-17 and 51,252.7 thousand tonnes in 2017-18. Major food grains produced in the state include **rice, wheat, maize, millet (bajra), gram, pea and lentils.**

PULSES Pulses production in the state stood at 2,208.0 thousand tonnes in 2017-18.
The state remains the **largest producer of vegetables** in India and produced 1,002.64 thousand MT of vegetables in 2018-19^.

SPECIAL ECONOMIC ZONES As of October 2020, Uttar Pradesh had 21 notified, 13 operational SEZs and 24 formally approved SEZs. The state offers a wide range of subsidies, policy and fiscal incentives as well as assistance for businesses under the Industrial and Service Sector Investment Policy, 2004 and Infrastructure and Industrial Investment Policy, 2012.

The state has well-drafted, **sector-specific policies for IT and biotechnology.** The new Uttar Pradesh Civil Aviation Promotion Policy 2017 was brought to promote investment and trade in Uttar Pradesh and to promote tourism while increased road connectivity along with air connectivity will create more employment avenues.

The state attracted **Foreign Direct Investment (FDI)** equity inflow worth US$ 664.66 million between October 2019 and December 2020 according to the data released by Department for Promotion of Industry and Internal Trade (DPIIT). In 2019, 147 investment intentions worth Rs. 16,799 crore (US$ 2.40 billion) were filed in Uttar Pradesh.

Merchandise exports from Uttar Pradesh reached US$ 16.99 billion in 2019-20 and US$ 12.93 billion in April 2020 to January 2021.

In 2020, the state govt. rolled out New Electronics Manufacturing Policy, 2020 and Uttar Pradesh Startup Policy, 2020, to promote the local manufacturing and new startups in the state.

Key Sectors:

- In June 2021, Greenply Industries announced that it will invest around Rs. 75 crore (US$ 10.30 million) to set up a plywood and allied products manufacturing unit at Sandila Industrial Area in Hardoi, Uttar Pradesh.

- In May 2021, Uttar Pradesh government announced that it would spend US$ 1 billion to buy COVID-19 vaccine.

- In January 2021, the state government announced its plan to build 1,038 new Ganga aarti platforms along the river in Bijnor and Ballia districts.

- In November 2020, Union minister for road transport, highways and MSMEs Mr. Nitin Gadkari inaugurated and laid the foundation stone of 16 highway projects worth Rs. 7,477 crore (US$ 1.06 billion) in Uttar Pradesh

- In November 2020, Uttar Pradesh Chief Minister, Mr. Yogi Adityanath dedicated power projects worth about Rs 216 crore (US$ 30.64 million) to Gorakhpur in a pre-Diwali gesture

- In February 2020, the state organised Defence Expo-2020 and received proposals worth Rs. 5 lakh crore (US$ 70.93 billion) for investment. Investments were focused on key sectors such as IT & ITeS, Dairy, Electronics, Tourism, Manufacturing, Renewable Energy, and Agro and Food Processing.

- In December 2019, Zurich Airport International got the approval from the state cabinet to develop and construct Jewar Aiport.

- Uttar Pradesh accounts for strong demand for fertilisers on account of the high availability of acreage coupled with the large size of the state.

COASTAL TRADE

The shipping of goods or passengers by a ship registered in one country that occurs solely from port to port along the coast of another country. It is typically governed by the portage country's national law.

Typical cargoes mainly include cement, steel, coal, scrap, oil products, grain, fertilizers, containers and passengers.

Coastal shipping in India accounts for only 6-7% of the total local freight.

The main advantages of coastal shipping includes alleviation of congestion, reduction of air pollution, overall cost savings to the shipping and government or company.

ADVANTAGES

1. Tremendous cost advantages to indian trade.
2. Immense benefits of energy savings to the country’s economy.
3. Boost transshipment at Indian ports.
4. Enhance competitive advantage of Indian exports.
5. Increase port’s potential to develop as hub ports.

6. Increase revenues and opportunities for generating both direct and in-direct employment.
7. Catalyse the development of an efficient and integrated transport and logistics system.

CHALLENGES

1. Lack of infrastructure: it is one of the biggest obstacles faced in coastal shipping industry. The government has failed to develop infrastructure that is expected to make shipment easy and efficient. Infrastructure involves electricity, road network and overall area development which supplements the use of this route.

2. Lack of lucrative government schemes: Unlike other channels of transportation, the government has not made any efforts to benefit coastal shipping users financially. Companies using coastal shipments until now had to face harsh and impartial taxes like no exemption from Income tax, customs duty on bunkers, landing fees, etc.

3. Slow and cumbersome process at Customs: The shipment process is extremely slow and laborious compared to other modes of transport which are much faster. Companies are unwilling to waste precious time in adhering to these processes (World Cement, 2010).

FACTORS RETARDING THE GROWTH OF COASTAL SHIPPING IN INDIA

1. Competition provided by rail and road transportation
2. Double handling costs involved and lack of active policy
3. Cumbersome and lengthy customs procedure.
4. High import duties on bunker oil and spares.
5. High manning scales which increase operational costs.
6. Stringent specifications for construction of vessels leading to higher capital costs.
7. Personal income tax which discourages qualityofficers from continuing on Indian coastal vessels.
8. Lack of separate berthing facilities at major ports and inadequate cargo handlinh facilities at the minor ports.
9. Absence of institutional mechanism for inter sector combination.

RECOMMENDATIONS

1. A clear cut policy for the development of an integral transport system needs to be evolved.
2. Coastal ships have to pay dutieson bunker oil. It increases the cost of operation of coastal vessels. This duty should be removed or decreased.
3. As coastal shipping is much more environment friendly and fuel efficient than other modes of transport. It should be provided tax concession both for fuels and spares.
4. Import duties on capital goods and spares should be removed.

5. Facilitative policy and supporting systems, rules and regulations and procedures similar to those existing in leading maritime nations should be implemented in India.
6. Government should grant special status to coastal shipping so as to exempt it from customs and other procedures that apply to the bigger cargo carrying vessels.

TERMS OF TRADE

Terms of trade (TOT) refer to the relationship between how much money a country pays for its imports and how much it brings in from exports. When the price of a country's exports increases over the price of its imports, economists say that the terms of trade has moved in a positive direction. The TOT is expressed as a ratio of import prices to export prices; that is, the amount of imported products/commodities that an economy can purchase, per unit of exported products/commodities. Any improvement that occurs in a country's TOT is beneficial to the economy because it means that the country can purchase more imports for the particular level of exports.

The formula below is used to calculate an economy's TOT:

Terms of Trade (TOT) = Index of Export Prices / Index of Import Prices X 100

Some of the major factors affecting the terms of trade are as follows:

The terms of trade of a country are influenced by a number of factors which are discussed as under:

1. Reciprocal Demand:

The terms of trade of a country depend upon reciprocal demand, i.e. "the strength and elasticity of each country's demand for the other country's product". Suppose there are two countries, Germany and England, which produce linen and cloth respectively.

If Germany's demand for England's cloth becomes more intense (inelastic), the price of cloth rises more than the price of linen, the commodity terms of trade will move against Germany and in favour of England. On the other hand, if England's demand for Germany's linen becomes more intense, the price of linen will rise more than the price of cloth, and the commodity terms of trade will move in favour of Germany and against England.

2. Changes in Factor Endowments:

Changes in factor endowments of a country affect its terms of trade. Changes in factor endowments may increase exports or reduce them. With tastes remaining unchanged, they may lead to changes in the terms of trade.

3. Changes in Technology:

Technological changes also affect the terms of trade of a country. The effect of technological change on terms of trade is illustrated in Fig. 79.5. Suppose there is change in technology in Germany. Before technological change the terms of trade between Germany and England are settled at point L on the OT ray where Germany exports CL of linen for OC of England cloth. With technological change, Germany's new offer curve is OG, which cuts the terms of trade line OT at L1. At this point, Germany would like to export less linen (C1L1) and import less cloth (OC1) than England wants to exchange at the terms of trade OT. So Germany's terms of trade improve when its new offer curve OG, intersects England's unchanged offer curve OE at L, where the new terms of trade are settled on the line OT1. At L2, Germany is better off because it exports less linen for more of England's cloth, i.e. C2L2 < OC2. Its terms of trade have improved with technological change.

4. Changes in Tastes:

Changes in tastes of the people of a country also influence its terms of trade with another country. Suppose England's tastes shift from Germany's linen to its own cloth. In this situation, England would export less cloth to Germany and its demand for Germany's linen would also fall. Thus England's terms of trade would improve.

5. Economic Growth:

Economic growth is another important factor which affects the terms of trade. The raising of a country's national product or income over time is called economic growth. Given the tastes and technology in a country, an increase in its productive capacity may affect favourably or adversely its terms of trade.

6.Tariff: An import tariff improves the terms of trade of the imposing country. This is explained with the help of Fig. 79.8 where the offer curves of England and Germany before the imposition of tariff are OE and OG respectively. The initial terms of trade are given by the line OT. England is exporting OC of cloth and importing CL of linen from Germany. Suppose a tariff is imposed on Germany's linen by England. It shifts the offer curve of England from OE to OE1. These changes the terms of trade OT to OT1 in favour of England.

7. Devaluation: Devaluation raises the domestic price of imports and reduces the foreign price of exports of a country devaluing its currency in relation to the currency of another country.

The effects of devaluation on the terms of trade have been much debated among economists. According to Prof. Machlup, "Devaluation is supposed to improve the balance of trade. A reduction in the physical volume of imports in relation to the physical volume of exports constitutes an adverse change in the gross barter terms of trade."

ABBREVIATIONS

AD	Antidumping
APEC	Asia Pacific Economic Cooperation
ASEAN	Association of Southeast Asian Nations
ATC	Agreement on Textiles and Clothing
BIT	Bilateral Investment Treaty
BOP	Balance of Payments
CFTA	Canada Free Trade Agreement
CTE	Committee on Trade and the Environment
CTG	Council for Trade in Goods
CVD	Countervailing Duty
DSB	Dispute Settlement Body
EAI	Enterprise for ASEAN Initiative
DSU	Dispute Settlement Understanding
EU	European Union
EFTA	European Free Trade Association
FOIA	Freedom Of Information Act
GATT	General Agreement on Tariffs and Trade
GATS	General Agreements on Trade in Services
GDP	Gross Domestic Product
GEC	Global Electronic Commerce
GSP	Generalized System of Preferences
GPA	Government Procurement Agreement
IFI	International Financial Institution
IPR	Intellectual Property Rights
ITA	Information Technology Agreement
LDBDC	Least Developed Beneficiary Developing Country
MAI	Multilateral Agreement on Investment
MEFTA	Middle East Free Trade Area
MERCOSUR	Southern Common Market
MFA	Multifiber Arrangement
MFN	Most Favored Nation
MOSS	Market-Oriented, Sector-Selective
MOU	Memorandum of Understanding
MRA	Mutual Recognition Agreement
NAFTA	North American Free Trade Agreement
NAMA	Non-Agricultural Market Access
NEC	National Economic Council
NIS	Newly Independent States
NSC	National Security Council
NTR	Normal Trade Relations
OECD	Organization for Economic Cooperation and Development

OPIC	Overseas Private Investment Corporation
PNTR	Permanent Normal Trade Relations
ROU	Record of Understanding
SRM	Specified Risk Material
TAA	Trade Adjustment Assistance
TBT	Technical Barriers to Trade
TEP	Transatlantic Economic Partnership
TIFA	Trade & Investment Framework Agreement
TPP	Trans-Pacific Strategic Economic Partnership
TPRG	Trade Policy Review Group
TPSC	Trade Policy Staff Committee
TRIMS	Trade Related Investment Measures
TRIPS	Trade Related Intellectual Property Rights
UAE	United Arab Emirates
UNCTAD	United Nations Conference on Trade & Development
UNDP	United Nations Development Program
URAA	Uruguay Round Agreements Act
WB	World Bank
WTO	World Trade Organisation