The global economy

Edexcel IGCSE Economics 4EC1 sections 2.2.1-2.2.3 full package

The global economy

- explain the causes of globalisation and its effects on different groups;
- explain why multinational corporations exist and judge their effects on host countries;
- weigh the advantages and disadvantages of **free trade**;

The global economy (2)

- explain the reasons for **protection** and the methods used, and analyse a **tariff** on a diagram;
- explain trading blocs, the WTO and the pattern of world trade;
- explain how exchange rates are set and the effects of **appreciation** and depreciation.

Globalisation

- **fewer tariffs and quotas**: countries have cut barriers to trade, through the WTO and trade agreements;
- **cheaper transport**: container ships and air freight have made it cheap to move goods around the world;
- **cheaper communication**: the internet and mobile phones let firms run factories and offices across continents;

Globalisation (2)

- **the growth of multinational corporations**, which spread their production across many countries.
- to gain **economies of scale** by selling in many countries;
- to get **natural resources** and cheaper materials and labour;

Globalisation (3)

- to cut **transport and communication costs** by producing close to customers;
- to reach **customers** in different regions, sometimes getting round tariffs.

Figure: Globalisation



- A container port: falling transport costs tie national economies together.
- Match each part of the diagram to the text.

International trade

- **Advantages**: consumers get lower prices and more choice; businesses get cheaper raw materials and parts, and bigger markets to sell to.
- **Disadvantages**: foreign competition can force domestic firms to close, and unemployment rises in those industries. Economists estimate that cheap imports from China cost the United States about a million manufacturing jobs between 1999 and 2011, while American buyers gained cheaper goods.
- to stop **dumping** : foreign firms selling exports below their normal price at home;

International trade (2)

- to protect jobs at home;
- to protect **infant industries** until they are big enough to compete;
- to raise revenue from tariffs;

International trade (3)

- to protect consumers from unsafe products;
- to reduce a current-account deficit;
- to **retaliate** against another country's barriers.

Figure: International trade



- A **tariff** of 4 raises the price from 12 to 16, cuts imports from 48 to 24 and raises 96 in revenue.
- Match each part of the diagram to the text.

Exchange rates

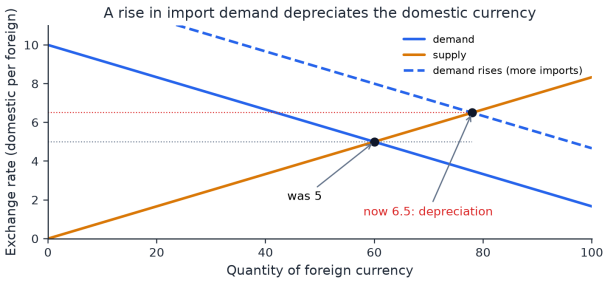
- **Exports**: foreign buyers of a country's goods need its currency, so more exports raise demand for the currency.
- **Imports**: importers sell their own currency to buy foreign currency, so more imports raise the supply of the currency.
- **Interest rates**: higher interest rates attract savings from abroad, raising demand for the currency.

Exchange rates (2)

- **Speculators** buy currencies they expect to rise and sell those they expect to fall. In September 1992 **speculators**, led by George Soros, sold pounds on such a scale that the UK had to stop defending the pound's value.
- An imported good priced at 100 foreign units cost $100 \times 5 = 500$ domestic units; now it costs $100 \times 6.5 = 650$, which is 30% more.
- An export priced at 1,300 domestic units cost foreign buyers $1{,}300 \div 5 = 260$ foreign units; now it costs $1{,}300 \div 6.5 = 200$, about 23% less.

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Figure: Exchange rates



- More demand for foreign currency raises its price from 5 to 6.5: the domestic currency depreciates.
- Match each part of the diagram to the text.

Data-response practice

- (a) Define ***depreciation*** of a currency. [2]
- (b) Using the extract, explain **one** reason why the yen depreciated. [3]
- (c) A Japanese car costs ¥3,000,000. Calculate its price in US dollars at 120 yen per dollar and at 150 yen per dollar. [2]

Data-response practice (2)

- (d) A barrel of oil costs \$80. Calculate its cost in yen at 120 and at 150 yen per dollar, and the percentage change. [2]
- (e) Analyse how the **depreciation** affected Japan's tourism industry. [4]
- (f) Evaluate whether the weak yen was good for the Japanese economy. [9]

Common errors

- Writing "globalisation" without its causes: lower trade barriers, cheaper transport and communication, and the growth of MNCs.
- Listing only the benefits of MNCs. Judge both sides for the host country.
- Confusing a **tariff** (a tax on imports) with a **quota** (a limit on the quantity of imports).

Common errors (2)

- Using "**devaluation**" for a floating currency. Floating currencies depreciate; fixed ones are devalued.
- Saying a **depreciation** makes exports dearer. It makes exports **cheaper** abroad and imports dearer at home.
- Forgetting that a depreciation can cause inflation through dearer imports.

Key terms

- **Globalisation**: the growing integration and interdependence of the world's economies.
- **Multinational corporation**: a firm that produces in more than one country.
- **Foreign direct investment**: building or buying productive assets in another country.

Key terms (2)

- **Free trade**: trade without barriers such as tariffs and quotas.
- **Dumping**: selling exports below their normal price in the home market.
- **Tariff / quota**: a tax on imports / a limit on the quantity of imports.

Key terms (3)

- **Trading bloc**: a group of countries that remove trade barriers between themselves.
- **Appreciation / depreciation**: a rise / fall in the value of a floating currency.

Check yourself

- 1.
- Give two reasons for the growth of globalisation. 2.
- Give one advantage and one disadvantage for a host country when an MNC builds a factory there. 3.
- Explain why a government might protect an infant industry. 4.