# 6.3 Economic integration

Name: _____ Class: _____ Date: _____ **Total: 30 marks**

**KEY WORDS** free trade area • customs union • common market • monetary union • trade creation • trade diversion

## Objective

Build the skills to answer exam questions on **economic integration** : trade agreements, trading blocs, **trade creation** and **trade diversion**, and monetary union.

**You must be able to:**

- distinguish bilateral, regional and multilateral trade agreements
- compare free trade areas, customs unions, common markets and economic and monetary unions
- explain trade creation and trade diversion
- evaluate trading blocs and monetary union

## 1 Key knowledge and worked examples

### ■ Economic integration

**Preferential trade agreements** give some countries easier access to a market. They can be **bilateral** (two countries), **regional** (a group), or **multilateral** (many countries, through the WTO).

| level of integration | features | example |
|---|---|---|
| **free trade area** (FTA) | no tariffs between members; each keeps its own tariffs on non-members | USMCA, ASEAN Free Trade Area |
| **customs union** | free trade inside plus a **common external tariff** | Southern African Customs Union |
| **common market** | customs union plus free movement of **labour and capital** | the EU single market |
| **economic and monetary union** | common market plus a **single currency** and one central bank | the eurozone |



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**Trade creation:** joining a bloc lets a country switch from a **higher-cost domestic producer** to a **lower-cost partner** producer: more efficient. **Trade diversion:** a country switches from a **low-cost producer outside** the bloc to a **higher-cost member** because of the common external tariff: less efficient.

**Advantages of trading blocs:** larger markets and economies of scale; more competition; more foreign investment; trade creation; stronger negotiating power; political cooperation.

**Disadvantages:** trade diversion; loss of national control over trade policy; harm to non-members; complex rules of origin in FTAs.

**Monetary union: benefits**: no exchange-rate costs or risks between members; price transparency; more trade and investment. **Costs**: one interest rate and exchange rate for all, even when members are in different situations; no own monetary policy or exchange rate to respond to shocks; fiscal rules may limit governments.

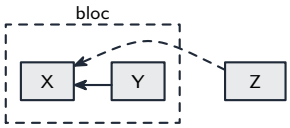
**Answer shapes:** identify the type of bloc → explain the mechanism (creation or diversion) → evaluate for members and non-members.

## 2 Practice

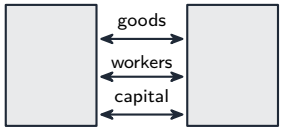
**2.1** Distinguish between a free trade area and a customs union. [2]




**2.2** Define **trade diversion**. [2]




**2.3** Explain **two** benefits for firms of joining a common market. [4]



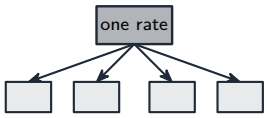



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**2.4** Before joining a customs union, country X imported TVs from country Z (outside) at \$200 plus a 10% tariff. After joining, X faces a 30% common external tariff on Z, and buys from member Y at \$240 with no tariff. Explain whether this is trade creation or trade diversion. [3]

| | before | after |
|---|---|---|
| from Z | \$220 | \$260 |
| from Y | — | \$240 |

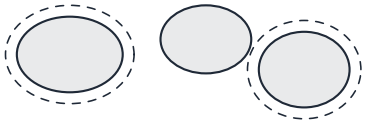
**2.5** Explain how a country that joins a monetary union loses **two** tools for dealing with a recession. [3]




## 3 Exam-style questions

**3.1** Many countries belong to regional trading blocs.

Explain why a country may benefit from joining a trading bloc, and why non-members may lose. [10]

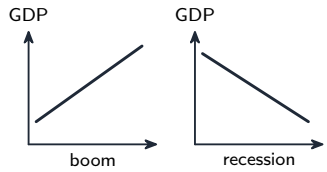




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**3.2** Some economists argue that the eurozone's single interest rate caused problems when member economies were in different situations.

Evaluate monetary union for its members. [6]






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