

## Foreign Trade

**Trade** means exchange of goods & services between different areas.

- Link in different activities that depend on each other.
- Helps regions specialize in the production of different commodities,
- Provides employment.

### Benefits of trade:

- Specialization of production.
  - Demand for exports increases & domestic resources are utilized for production.
  - Employment.
  - Flow of capital & information technology from developed countries to developing countries increases economic development.
  - Developing countries then focus of producing value-added products that have a higher value in the international market.
  - Foreign exchange earned through trade can be spent on import of capital goods for industrialization.
  - Export goods are produced on a larger scale which gives economy of scale. When items are produced on a large scale, the per item cost production decreases.
  - Increases GDP/ precious foreign exchange.
1. **Import:** refers to the inflow of goods, when goods move in/ outflow of foreign exchange, usually considered as a negative indicator of trade.

Advantages	Disadvantages
Good quality & quantity can be imported.	Outflow of money.
Fulfils local needs & requirements which are not readily available.	Dependence on other countries.

2. **Export:** refers to the outflow of goods, when goods move out/ inflow of foreign exchange, usually considered as a positive indicator of trade.

Advantages	Disadvantages
Positive trade in balance.	Shortage of products for locals.
Increases GDP, earn foreign exchange & generated capital which can be used for governmental development.	

Pakistan's position is strong in some export items, with Cotton clothes contributing to 2.16%, 2.13% leather, fish & fish products 0.41% of the world.

**Trade Deficit:** is when the value of its imports exceeds the value of its exports.

**Balance of Trade** is the difference between the value of good imported & the value of goods exported. If international market prices of raw material are low & if a country's

major export consists of raw materials, then the earnings from trade would be relatively low. If import are of manufactured goods, then the balance of trade will be affected.

Balance of Trade = Value of goods exported in 1 year - Value of goods imported in 1 year

- + Balance of Trade when values of exports exceed the value of imports.
- - Balance of Trade when values of imports exceed the value of exports.

Q. 'Pakistan's value of trade is negative for decades.' What do you think are the causes of this? (6 marks)

**Balance of Payment** is the difference between the value of good & services exported & the value of goods & services imported.

Balance of Payment = Value of goods & services exported - Value of goods & services imported

Balance of trade (BOT) is the difference that is obtained from the export and import of goods. Balance of payments (BOP) is the difference between the inflow and outflow of foreign exchange.

**Economic Goods:** anything which can be bought or sold. It can be classifies into 2.

- Produced: Primary, Secondary, and Tertiary. Bases of consumption.
  - Consumer Goods: finishes on consumption. E.g. Clothes, Food etc.
  - Capital Goods: goods generate capital on usage. E.g. Cement, Tractor, Tube-well etc.
  - Raw Materials: needs to be processed further to produce capital or consumer goods. E.g. Limestone, Cotton etc.
    - ➔ Cheaper
    - ➔ Creates employment opportunities
- Some are pure consumer, some are pure capital.
- Some behave differently.
  - Car as taxi - capital.
  - Car for personal use - consumer.

**Economic Services:** any service which can be bought or sold.

**Exports:** high value-added products. Secondary products are more profitable to export. Mainly manufactured products. Promote industries & employment to people.

**Imports:** primary products. They are cheaper to purchase. Imported goods should be processed in one's own country to allow industrialization.

**Trades:** promotes industrialization, GDP, & helps attain economy.

**Capital Goods:** economic goods which are meant to produce more capital.

**Problems of export:**

- Narrow export base: high degree of dependency on very few exportable products are exported to international market. High dependence on few products.
- Export items are relatively low value: added products mostly from small scale & cottage craft industries.
- Few trading partners in international market: nearly 50% of exports go to just 7 countries of the world.

**Direction of Trade:** Pakistan trades with many countries, but its exports are concentrated to only a few.

**Trading Partners: Exports**

Countries	Goods Exported
UK & Germany	Raw cotton, sports goods.
Eastern Europe	Cloth cotton, ready-made garments.
USA	Carpets, rugs, surgical instruments, sports goods.
Middle East Countries	Rice, spices, ready-made garments, milk, meat & fruit
China	Cotton Yarn
Japan	Fish & Fish Products
Sri-Lanka	Fish & Fish Products

**Problems of Import:**

- More Raw materials:
- Light imports of capital goods:
- 14% of total imports comprising consumer goods:
- Drastic increase in imports consumer.

**Direction of Trade:** Pakistan is importing from more than a 100 countries.

**Trading Partners: Imports**

Countries	Goods Imported
UK & Germany	Machinery, Electrical appliances
Eastern Europe	Machinery, Electrical appliances
USA	Machinery, Vegetable Oil, Wheat
Middle East Countries	Mineral Oil
Malaysia	Edible Oil
China	Consumer Goods

Japan	Edible Oil
Sri-Lanka	Tea

**Remittance:** When migrants send home part of their earnings in the form of either cash or goods to support their families. Tradition started mainly after 9/11 as Muslims grew insecure. This money sent profits our economy.

### Reasons for Negative BOP:

#### 1. Less Exports:

- Few industries due to lack of capital for industrial development & few industrial estates.
- Shortage of electricity.
- Poor industrial development.
- Shortage of industrial workers.
- Unfavorable government policies.

#### 2. More Imports:

- High population growth rate leads to increasing demand & local industries are unable to fulfil local needs of population.
- Improved standard of living leads to higher demand of consumer goods- mobile sets.
- Increased urbanization leading to a higher demand of imported goods.
- Capital goods are very expensive to import.
- Large quantities of fossil fuels.
- Imports of Iron Ore.
- Edible oil has to be imported: Palm oil from Malaysia.
- Chemical Fertilizers are imported.
- Depreciating own currency.

#### 3. Higher Imports of Services:

- General trade of illiteracy.
- Lack of technical training centers.
- Shortage of skilled labor.
- Developmental projects in collaboration with other countries such as with China, UK & USA.

**Effects for Negative BOP:** The import bill consists of high-value goods that consume our foreign exchange resources & negatively affect the economy in many ways.

- Increasing burden of loans & foreign debts.
- Economy goes down/adversely affected/loss of foreign exchange.
- Economy goes under the control of creditors who exercise influence over Pakistan's economic & political affair.
- Increased taxation limits purchasing power of consumer.
- Country's currency depreciates, so imports become expensive.

- Developmental products curtailed.
- Business & commercial activity slows down.

**Measure to Control Negative BOP:**

**1. Increasing Exports:**

- Exports mainly high value-added furnished goods.
- Encouragement of cottage & small scale industries for export.
- Improves the quality of production.
- Widening export base.
- Lowering production cost.
- Communication improved:
  - Client orders.
  - Transport.
  - Advertisement.
- Establishment of export processing zones:
  - Landhi Export Processing Zone.

Q. To what extent is it possible to improve by developing trade agreements or becoming a part of national trading block? (6 marks)

➤ CPEC

**Advantages & Disadvantages of developing a trade agreement with partners in European Union:**

Advantages	Disadvantages
More exports more foreign exchange earnings helping in paying off loans, improving trade balance & national economy.	Trade activity can be stopped due to sanctions. <ol style="list-style-type: none"> <li>1. Exports of sport goods was banned due to child labor.</li> <li>2. Cotton banned due to excessive pesticides.</li> <li>3. Fish banned due to poor quality control.</li> </ol>
Cheaper imports save precious foreign exchange, improved balance.	Imports from partner countries may compete with local production/industries.
Boosts industrialization & attracting more foreign exchange investments & fewer trade barriers.	

**TDAP:** Trade development authority of Pakistan was EPB.

**EPB:** export promotion involved in planning & development of different sectors of economy & linking them with the international trade requirements. Provides opportunities to new industries.

**Export Processing Zones:** areas reserved for the development of industries. They promote industrialization, increase exports by facilitating the local & foreign investors & creates employment.

- Government offer financial & regulatory incentives.
- Infrastructure is already put in place including roads, railways & dry-ports.
- Attracts foreign & private investments.

**Land Routes:** there is great potential for foreign trade through land & sea routes.

- Trade with India is out of question due to bad terms and relations
- Khunjerab Pass - Connects Pakistan to China (KKH)
- Kurram Pass - Connects Peshawar to Afghanistan (GT Road)
- Tochi Pass - Connects Ghazni to Bannu
- Gomal Pass - Connects Afghanistan to Derajats
- RCD Highway - Iran & Turkey (Zahedan Border)
- Arabian Sea:
  - Land route is long, expensive, heavily taxed, transportation cost is high
  - Ports provide modern facilities for handling & countries are easily accessible
  - Warm water port open throughout the year while land route can be blocked

**GDP (Gross Domestic Product) & GNP (Gross National Product):**

GDP means the total monetary value of all goods & services produced within a country over a particular period of time.

GNP means the total monetary value of all goods & services produced by the resources owned by the citizens of the country. This production can be anywhere in the world.

**Difference between GDP & GNP:**

GDP defines a nation's economy in geographical terms. It focuses on domestic production that it whatever is produced inside the country regardless of who is responsible for the production. GNP on the other hand focuses on the production by nationals. This means GNP measures the output produced by the country's companies wherever they are in the world.

Pakistan: The GDP refers to whatever is produced within all 4 provinces, regardless of whosoever produces it. The GNP however measure anything produced by Pakistanis around the world.

Why it is difficult for Pakistan as a developing country to maintain or increase its share of trade with other countries?

Lack of investment is one of the core reasons why Pakistan's growth in exports has been negative over a 10-year period. Other reasons include higher tariff structure, erratic growth trends, low penetration in global markets, lack of infrastructure & technological advancement.

**Factors that may promote or limit trade:**

**Promote:**

Endowments & productivity, trade policy, exchange rates, foreign currency reserves, inflation, & demand.

**Limit:**

Corruption, political instability, trade policy, exchange rate, foreign currency reserves, inflation & demand. If a country's inflation rate increases relative to the countries with which it trades, its current account will be expected to decrease, other things being equal. Consumers and corporations in that country will most likely purchase more goods overseas (due to high local inflations), while the country's exports to other countries will decline. A country's government can have a major effect on its balance of trade due to its policies on subsidizing exporters, restrictions on imports, or lack of enforcement on piracy. Each country's currency is valued in terms of other currencies through the use of exchange rates, so that currencies can be exchanged to facilitate international transactions.

**Trading Blocs:** refer to the regional grouping of international economies to allow for greater economic cooperation & facilitations of free trade activity. It involves low or no economic restrictions between members & strong trade barriers against non-members.

Pakistan is a part of some trading blocs like:

- SAARC - South Asian Association for Regional Cooperation.
- ECO - Economic Cooperation Organization.
- EU - European Union.
- ASEAN - Association of Southeast Asian Nations

**Trade Barriers:** are measures that governments of public authorities introduce to make imported goods or services less competitive than locally produced goods & services. They are a set of restrictions to limit or stop foreign trade. E.g. Tariffs are taxes of imported goods aka duty. This is done to encourage locally produced items. Embargoes are a ban on certain imported products. Quotas are restrictions on the quantities of goods. These encourage local goods saving precious foreign exchange & gives employment.

Advantages	Disadvantages
Promotes self-sufficiency.	Limits consumer choice.
Protects local industries & creates employment.	Local industries lose efficiency.
Improves BOP	Industries manipulate production to increase prices.

**Exchange Rates:** refer to the prices of 1 currency in terms of another currency. Currency depreciation makes imports expensive & leads to inflation. Currency appreciation is when 1 unit of a currency buys greater units of another currency. This make imports cheaper & exports expensive leading to economic prosperity.

**WTO:** World Trade Organization is an international institution to allow free trade between the member countries by reducing of abolishing trade restrictions.