G9:

A Globalization Glossary

Nine Terms Often Heard in Discussions of the Global Economy

Certain terms find their way into most news stories and discussions about globalization. (OK, maybe you won't hear "absolute advantage" and "comparative advantage" quite so often as the others, but they are important concepts nevertheless.)

World Trade Organization (WTO)

Quick! For $50 and the match, what is the WTO?

You never know. This question just might come up during trivia night at the local social club. So, here's the answer, straight from the WTO web site. **http://www.wto.org/**

> The World Trade Organization (WTO) is the only global international organization dealing with the rules of trade between nations. At its heart are the WTO agreements, negotiated and signed by the bulk of the world's trading nations and ratified in their parliaments. The goal is to help producers of goods and services, exporters, and importers conduct their business.

The G8 Nations (Or is it G7? Or maybe G9?)

The G8 started out as the G6. Britain, France, Germany, Italy, Japan, and the United States first met in 1975 to discuss pressing economic and political issues. Canada joined them in 1976 (G7), and Russia became a full participant in 1998 (G8). Quoting from the G8 Information Centre **http://www.g7.utoronto.ca/**

> The G7/8 Summit has consistently dealt with macroeconomic management, international trade, and relations with developing countries. Questions of East-West economic relations, energy, and terrorism have also been of recurrent concern. From this initial foundation the summit agenda has broadened considerably to include microeconomic issues such as employment and the information highway, transnational issues such as the environment, crime and drugs, and a host of political-security issues ranging from human rights through regional security to arms control.

Tariff

In the context of international trade, a tariff is a tax placed on imported goods. Tariffs are usually intended to protect domestic industries from foreign competition by making the foreign product more expensive, hence the term "protectionism."

Example: During the first half of the 19th century, American textile manufacturers had a problem. They couldn't compete with British manufacturers who were better established and better able to produce cloth at a lower price. What to do?

The American manufacturers convinced Congress to protect them with a tariff (tax) on imported textiles. The tariff narrowed the price gap between British cloth and American cloth by making British cloth much more expensive than it actually should have been. Of course, this didn't sit well with consumers in the American South or on the western frontier because they had to pay a higher price for cloth.

Free Trade

"Free trade is the untaxed flow of goods and services between countries."

Clear and concise, this single sentence from the Wikipedia web site **http://en.wikipedia.org/wiki/Free_trade** defines free trade in its purest form — the ideal rather than the reality. But it's an ideal that seems more attainable now than at any time in recent memory. Although restrictions and tariffs haven't disappeared completely, many nations are moving in the direction of *freer* trade, making agreements that eliminate or drastically reduce trade barriers. (See NAFTA)

Fair Trade

Fair trade and free trade are not one and the same. On a general level, "fair trade" describes the ongoing effort to ensure that any two trading partners — no matter if they're big, small, or somewhere in the middle — are on an equal footing. Example: If a country's aircraft industry receives a large government subsidy, it might have an unfair advantage over the unsubsidized aircraft industry in another country.

In a more specific sense, fair trade refers to an organized effort aimed at helping producers in developing countries gain access to world markets and receive an equitable price for their products. Some of the most common fair trade items are coffee, tea, cocoa, and fresh fruit. **http://www.fairtrade.org.uk/index.htm** **http://www.guardian.co.uk/fairtrade/0,12458,794377,00.html**

Absolute Advantage and Comparative Advantage

Absolute and comparative advantage are essential to understanding the workings and benefits of trade. English economist David Ricardo developed a famous example during the early 1800s, using the production of wine and cloth in England and Portugal to illustrate his point. Follow this link if you want to read his example in the original **http://faculty.washington.edu/krumme/gloss/r.html#comparative**

If you'd prefer a shorter, contemporary example, here's one from our colleagues at the Federal Reserve Bank of Dallas. **http://www.dallasfed.org/fed/annual/2002/index.html**

> Societies reaped the benefits of specialization and trade for thousands of years before English economist David Ricardo (1772–1823) finally demonstrated why it works. His theory of comparative advantage helps explain why the United States exports soybeans to China and imports shoes in return.
>
> Suppose an average American worker can produce 100 bushels of soybeans or five pairs of shoes and a typical Chinese worker can turn out eight bushels of soybeans or four pairs of shoes.
>
> The United States is more productive than China in both industries, but consumers in both countries can still gain from specialization and trade. Shifting a U.S. worker from shoe factory to soybean farm produces a gain of 100 bushels of soybeans at the cost of five pairs of shoes. Shifting two Chinese workers from farm to factory raises shoe output by eight pairs but cuts soybean production by 16 bushels. The net effect is an increase of 84 bushels of soybeans and three pairs of shoes. Total output of both products reaches a maximum when the United States specializes in soybeans and China in shoes. Through trade, the two countries can divide the added production between themselves, leaving both better off than they were on their own.

Current Account, Balance of Payments, and Balance of Trade

We could spend a lot of time and use a lot of words trying to develop a definition, but it wouldn't be nearly as good — or as easy to understand — as the one we found on the AmosWeb Gloss*arama **http://www.amosweb.com/gls/**

> Current Account: One of two parts of a nation's balance of payments (the other is capital account). It is a record of all trade, exports and imports, between a nation and the rest of the world. The current account is separated into merchandise, services, and what's called unilateral transfers. The merchandise part is nothing other than the well-known balance of trade. There's also a lesser known balance of services — the difference between services imported and exported.

Outsourcing and Offshoring

This definition comes from another excellent online glossary, *Economics A-Z* on Economist.com **http://www.economist.com/research/Economics/** (As a bonus feature, you get to see all those cool British spellings like "specialising" and "labour.")

> [Outsourcing is] Shifting activities that used to be done inside a firm to an outside company, which can do them more cost-effectively. Big firms have outsourced a growing amount of their business since the early 1990s, including increasingly offshoring work to cheaper employees at firms in countries such as India. This has become politically controversial in countries that lose jobs as a result of offshoring. However, a firm that outsources can improve its efficiency by focusing on those activities in which it can create the most value; the firm to which it outsources can also increase efficiency by specialising in that activity. That, at least, is the theory. In practice, managing the outsourcing process can be tricky, particularly for more complex activities.

NAFTA

This definition comes from the National Council on Economic Education web site, and it's part of a lesson plan *NAFTA: Are Jobs Being Sucked Out of the United States?* Here's the link:
http://www.econedlink.org/lessons/index.cfm?lesson=EM50

> NAFTA, the North American Free Trade Agreement, went into effect on January 1, 1994. The Agreement phases out most tariffs between the United States, Canada, and Mexico. Tariffs, which are taxes on imports, increase the price of foreign goods and thereby benefit domestic producers. The participants in NAFTA agreed to reduce tariffs by 50 percent immediately and to reduce them to zero over the following 15 years. Industries suffering the most because of the increased competition from foreign goods would be given extra time to adjust to the elimination of tariffs on their foreign competitors' products. ■